# Сборник докладов IV Международной студенческой научно-практической конференции «Unbalanced global economy: recent developments and prospects»

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# Сборник докладов IV Международной студенческой научно-практической конференции

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# МЕЖДУНАРОДНАЯ СТУДЕНЧЕСКАЯ НАУЧНО-ПРАКТИЧЕСКАЯ КОНФЕРЕНЦИЯ ЭКОНОМИЧЕСКОГО ФАКУЛЬТЕТА МГУ ИМЕНИ М. В. ЛОМОНОСОВА

# UNBALANCED GLOBAL ECONOMY: RECENT DEVELOPMENTS AND PROSPECTS

2 апреля 2015 г. на экономическом факультете МГУ под эгидой кафедры иностранных языков прошла IV Международная студенческая научно-практическая конференция «Unbalanced Global Economy: Recent Developments and Prospects». Более 85 участников, бакалавров, магистров и аспирантов различных ВУЗов экономического профиля России, СНГ и Европы имели возможность представить и обсудить темы своей специальности с российскими и зарубежными коллегами-студентами на языке международного общения – английском.

Обширная тематика конференции была представлена на пленарном заседании и в шести секциях:

1. **Meeting the Rules of the Game — Strategy to Succeed in the Eurozone And Emerging Markets**
2. **Russia in Conditions of Sanctions and its Development Strategy**
3. **Finance: Prospects in Unbalanced Global Economy**
4. **Marketing Today: New Strategies or Traditional Approaches?**
5. **Ideas and Solutions in a Challenging Environment**
6. **Present Day of Economic Science — Issues to Resolve**

В докладах, сделанных на высоком уровне, были представлены различные аспекты анализа: макроэкономического, регионального, секторального, диахронического, аксиологического, кросс-культурного и пр. Актуальные проблемы современности (от зарубежных инвестиций и стратегий семейного бизнеса до цветовой психологии, от России в условиях санкций до краудфандинга, от проблем в финансовом секторе до особенностей развития маркетинга и туризма) вызвали активную полемику и обсуждение всех участников.

Наиболее интересные результаты исследований нашли отражение в настоящем сборнике на английском языке, что не только дает студентам возможность практики написания научной статьи в соответствии с международными стандартами, но и является начальной ступенью их научной деятельности в академическом сообществе.

Экономический факультет МГУ имени М. В. Ломоносова благодарит всех участников конференции, а также преподавателей, усилия которых позволили выступающим продемонстрировать как глубокое проникновение в предмет исследования, так и отличное владение стилем научного изложения на английском языке. Кафедра иностранных языков выражает искреннюю благодарность своим партнерам – издательству Cambridge University Press и департаменту экзаменов Кембриджского университета, издательствам Macmillan, Pearson Education, Oxford University Press и “Книжному Дому” Санкт-Петербурга за постоянную и активную поддержку этого важного начинания. Информационная поддержка конференции осуществлялась порталом “Научная Россия”. Надеемся, что большой интерес, который вызвала эта конференция, сохранится и в дальнейшем.

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# FAMILY BUSINESS IN RETROSPECT: LESSONS WE CAN LEARN FROM MORGANS

## Abstract

*The article describes the road to success of Morgan family, famous American billionaires. What can make an ordinary family business international? What's the difference between develop family business and develop a business as a partner in non-family business? And can a family business be international? The article is for students of economics and for everybody who is interested in strategic management.*

***Key words:*** *family business, non-family business, strategic management.*

## Introduction

What do we usually mean by family business? A small or middle-sized enterprise managed by a head of a family and other members of the family as employees. Sometimes "family business" means that the firm is passed down from father to son, and other members of the family don't work in the firm. According to the definition in Longman Business English Dictionary, family business is a business that is owned and managed by members of the same family.

Perhaps, everybody knows the "American dream": start with nothing, work hard and get to the top. But, to turn a small family business into international ones, hardworking isn't enough. So, what can make an ordinary family business international? What's the difference between develop family business and develop a business as a partner in non-family business? To answer the questions, let's explore the history of Morgan family, one of the families that started with nothing and managed to turn their business into an international billion-dollar one.

## The Morgans dynasty: origins

The first Morgan, Junius Spencer Morgan (1813 — 1890), started his business without a benefit of a college education. He started with dabbing in commercial life of New York, then he organized a dry goods firm in Connecticut. His enterprises were successful and so, when in 1840$^{th}$ Morgan family moved to Boston, Junius Morgan was able to invest a considerable sum of capital in foreign trade finance company "J. M. Beebe, Morgan and Company". This firm financed the exports and imports channeled through Boston harbor. Even here Morgan didn't remain for a long time; his next position was a partner in highly respected international bank of George Peabody and Company, in London [1]. The firm served as a financial link between Europe and the United States. After Peabody retired from the business, the company was renamed J. S. Morgan and Company.

Junius Spencer Morgan had done a lot for the family's business. But, despite all his achievements, the real progenitor of the Morgan's dynasty is considered to be his son, John Pierpont (J.P.) Morgan (1837–1913). So, what makes the difference between the father, an ordinary middle-sized businessman, and the son, the progenitor of a dynasty of billionaires?

## A model of success

Firstly, the investments in industries that have strategic importance. J. S. Morgan left his son million-dollar fortune and business, but the most important part of the legacy was a unique position of "J. S. Morgan and Company" as a financial intermediary between the USA and Europe. In the middle of the XIX century, the USA was rapidly developing country, and J. P. Morgan placed European capital in the United States. He invaded management in the firms where the capital was placed for the purpose of safeguarding his European clients' investments. Therefore, John Pierpont Morgan extended his control and influence over the industries.

Secondly, investments in developing industries. J. P. Morgan started with railroad industry. Railroading was one of the most rapidly-developing industries, but Morgan's interest emerged also due to heavy speculating and financial chaos surrounded railroading. It was so called Morganization process [2]. There were three phases of Morganization. Firstly, a financial reorganization of a company and change of a dividend policy: a company paid its investors dividends only once, at the beginning of Morganization. Secondly, consolidation and community of interest: the division of market between competing companies and elimination of competition. And, finally, control: Morgan's firm purchased controlling interest or used interlocking directorates. As the result, by 1904 Morgan had expanded his influence over railroad industry. The total mileage directly controlled by this time was over 47 000 miles; combined capital of Morgan's railroad business amounted to nearly one-fourth of the capital of the USA railroad industry.

As for diversification. As to diversification of the Morgan's family business, it was really outstanding. By means of stock purchases Morgan entered farm machinery industry. In 1902, J. P. Morgan merged the "McCormick Harvesting Machine Company" and "Deering Harvester Company" along with three smaller agricultural equipment firms to "International Harvester" [3]. "International Harvester" was the US market leader from 1902 till 1979 and had factories in other countries, including Russian Empire (before the revolution of 1917). The other firms were Otis Elevator Company, New York insurance companies (in which Morgan entered using interlocking directorates), US Steel (the first US company with turnover more then $ 1 billion), International Merchant Marine (the monopolist in overseas transport, owned White Star Line which had build notorious Titanic) and General Motors.

The fourth key of the Morgans' wealth was innovations. In 1876 Alexander Graham Bell invented telephone, and Morgans were one of the first entrepreneurs who invested in telephone companies and factories. As the result, by $1920^{th}$ the Morgans owned almost all telephone lines, plants and scientific institutes related to the telephone industry [4].

In 1892 the Morgans merged "Edison General Electric" and "Thompson Hauston Electric" to "General Electric Company", the company that still exist nowadays and is ranked as the $6^{th}$ largest firm in the U.S. ("Fortune", 2011). After the World War I, "General Electric" became the US leader in production and distribution of radio equipment. "Radio Corporation of America", a subsidiary company of "General Electric" and Morgans, worked in broadcasting industry.

"Millionaires use consultants, billionaires use astrologers", — this phrase of John Pierpont Morgan is probably one of the most important to understand the basic point of success of his business. Probably, relying on intuition along with financial analysis makes the biggest difference between the father, an ordinary middle-sized businessman, and the son, the progenitor of a dynasty of billionaires. Nowadays railroads, radio, telephone and electronic devices are taken for granted and have become a part of our everyday life. But more then one hundred years ago they were rather risky thing to invest.

So, there are several points of the Morgans' business success: identifying strategic industries and investing in them; investments in rapidly developing industries, diversification and innovations. It was the official history of Morgans, the traditional American story where thrift, diligence and purposefulness lead to happy end. But the secret of great fortunes without apparent cause is a crime forgotten, for it was properly done ("Father Goriot", Honore de Balzac), and the history of the first Morgans has also shadow sides. It was the final point in turning a small Morgans' family business into international ones.

## Money doesn't smell

During the American Civil war (1861–1865) young J. P. Morgan speculated in arms and gold. He had bought 5 000 defected rifles at the price of $3,5 per unit from the army, the then, when the position of the army become worth, sold the rifles to the same army at the price of 22 dollars per unit. The "North" and the "South" fought with each other, but before the war the economies of industrial North and agricultural South were closely connected. So, during the war J. P. Morgan managed the firm "Dreksell, Morgan and Co" that sold cotton from South to North and manufactured goods from North to South.

From the foundation of the dynasty, the military business and everything linked with military supplies were the arena of Morgans. In 1870 the Franco-

Prussian war started, and J. P. Morgan gave a credit in the amount of $50 million to the French government (about $1 billion in current value). Since J. P. Morgan, the Morgans took part in military supplies of the USA army and sometimes even of the armies of other countries. For example, the Morgans awarded contracts arms delivery during Spanish-American war (1898, to the US army), South African wars (1879-1915, to the British army). The reason for South African wars were high-grade deposits of gold and diamonds striked in 1860th in the region, and J. P. Morgan gave a credit amounted to $223 million (about $4,4 billion in current value) to the British government for the war. The seizure of the Panama Canal at the beginning of the XX century was also financed by J. P. Morgan [5].

Especially profitable for the house of Morgans was the First World War. Financial links between Europe the USA were monopolized by Morgans, and the House became the biggest weapon supplier for Great Britain and France. Moreover, purchasing weapons was very expensive, so Great Britain and France became heavily indebted to Morgans once again. After the First World war, several plans of restoration of the German economy were accepted, Dawes Plan and Young Plan. And Owen D. Young, one of the authors of the Young Plan, worked in Morgan's "General Electric" as a founder of a subsidiary company "Radio Corporation of America"...

## Millionaires use consultants, billionaires use astrologers

So, what can make an ordinary family business international? Everybody who is hardworking, thrifty and purposeful can become an average small or middle-sized businessman. But it isn't enough for international level of business. Perhaps, according to the history of Morgan dynasty, an international businessman has to rely on intuition. It means that a person should be able to see the most perspective and fast-growing industries and invest in them. "Millionaires use consultants" and optimize the business they already have. But "billionaires use astrologers" and invest in their future business, especially in innovative business, rather then in their current one. Moreover, money does not smell (Vespasian, the Roman Emperor, 9–79 AD), and all legal industries are good for investments.

And, of course, a good luck. As was mentioned in this article, J. P. Morgan was a co-owner of International Merchant Marine with a subsidiary company White Star Line which had build notorious Titanic. So, during the maiden voyage of Titanic in 1912 J. P. Morgan had to be aboard the ship, but for several reasons he didn't, in spite of he had even sent his luggage to the ship. On the 16th of September 1920 terrorists blasted a bomb in a headquarters of J. P. Morgan Inc. 33 persons were killed and more then 400 were injured, but there were no Morgans among them. On the 11th of September 2001 terrorists attacked World Trade Center where worked 3700 employees of Morgan Stanley, and 3690 of them successfully rescued...

## Conclusion

Every point mentioned above is suitable to all kinds of business. But what's the difference between develop family business and develop a business as a partner in non-family business? Difference lies in the kind of investments: a person wants to pass down the business to the children, so the "family" entrepreneur will more likely choose long-term investments such as investing in innovative business or investments in solid assets. Another difference is in family traditions of managing the business.

As to Morgans' family business, the situation is different. After J. P. Morgan, the legendary progenitor of the dynasty, there were no Morgans as famous and outstanding as John Pierpont. Money begets money; new generations of Morgans became more and more wealthy, but there is nothing special about them. Nowadays international corporations are governed by hired managers and by a board of directors, not by J. P. Morgan's descendants.

It's a peculiarity of today. We know that Edison invented a light bulb, Stephenson invented steam locomotive. But today it's rather difficult to identify a particular author of a new device or a new artificial material: they are so complex that usually are created by a group of professionals. So do in business. The decisions in international corporations are made by a number of professionals that have replaced an outstanding entrepreneur.

According to the family business, it means that small or middle-sized business can be family business passing down from father to son with its history, traditions and reputation. But it's rather difficult to find a really big international family business passing down. The biggest international family businesses in the world are Wal-Mart Stores, LG Group, Fiat Group, PSA Peugeot Citroen, BMW, Hyundai Motor, Robert Bosch GmbH, Motorola, Auchan. Are they really family firms, or is it just a sort of marketing strategy?

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# LEARNING LESSONS FROM FOREIGN CAPITAL REGULATION IN LATIN AMERICA EMERGING MARKET

## Abstract

*The purpose of the present research is to identify the level of efficiency of foreign capital contribution to Latin America economy. According to statistical and comparative analysis, the paper focuses on countries where the potential outcome of investment is high. Moreover, the report considers risks and benefits of foreign capital for national economies. The experience of Latin America in foreign capital flows regulation has crucial importance for Russia, since these two regions dispose the similar level of market development.*

***Key words:*** *foreign capital, FDI, Latin America, Brazil, Mexico, inward investment, Russia, investment strategy*
***JEL codes:*** *E 290, F 210*

## Introduction

Foreign direct investment is an important leverage of the world economy. It encourages the development of human capital, technological progress; it provides national industries with financial resources. Furthermore, FDI is the way of collaborating in the global world. However, a large foreign capital inflow into the country does not automatically facilitate growth and prosperity of the national economy, because it requires the appropriate regulation by minimizing the threats of foreign investment and applying its opportunities in the most effective way.

Russia has not achieved to turn foreign capital into the main driver of economic growth. Consumption remains the force that still determines the country's output. One reason for this is a significant outward flow that constantly accompanies the inward FDI. The account balance of capital transactions of our balance of payments has been negative for the majority of years. According to the Central Bank of the RF, the net capital flow in 2014 is estimated approximately \$151,5 billion of outflow [6]. The other reason is the speculative nature of investment, in other words, foreign capital is not received by the real sector of the economy.

Moreover, it is worth noting that the value of consumption in the economy of Russia is decreasing in current conditions and the solution is to address the FDI as an incentive for economic growth. That is why it is vital to yield lessons according to the results of foreign capital regulation in Latin America in order to prevent a sharp decline in the growth rate of the Russian output.

## Current trends in capital flows

The European Union and North America was able to attract about 17% of total amount of FDIin 2013 while the share of Latin America in FDI inflows was 20,1% [3, 36]. The statistic data lead to the conclusion that the Latin American region is highly attractive for foreign investors, occupying the second place after Asia. Besides, a battle between China and Americais springing up now for the areas of influence in the region: China has declared to be ready to invest $ 250 billion in the next 10 years [8] that has become a serious threat for US — a constant investor of Latin America.

Thus, the question arises, what is the key to success of Latin America being as sweet as honey for investors' money and how it manages this huge foreign capital inflow.

## Investment strategies

Unfortunately, the region both enjoys the opportunities and suffers from diseases caused by participating in foreign capital flows. The comparative analysis of investment strategies of some countries of the given regionwill help to understand how foreign investment influences the national economy in compliance with the selected method of regulation.

Firstly, the economies of Venezuela and Ecuador are under consideration since they represent a commonly used strategy that Russia also applies. In Venezuela oil and gas account for the one fourth of the country's GDP and approximately 97% of export revenues [2]. Likewise, the Russian economy also rely mostly on oil and gas that represent 71% of merchandise exports. Therefore, the decline in oil prices has brought the countries to the brink of turmoil. On the one hand, a significant reserve of energy resources serves as a guarantee in current economic instability and allows Venezuela to obtain debt financing in spite of a considerable credit risk arising from the recession. On the other hand, these riches make the country more dependent on investors at the same time. Thus, China — one of the principal investors of Venezuela — has provided the country with over $50 billion since 2007 in exchange for oil supply to the tune of 500 thousand barrels per day and is ready to continue giving loans. However, the generous investor is aimed at establishing its own rules of the game and requires more oil supply now(600 barrels per day).

Another country of Latin America — Ecuador — also hopes on Chinese investment. In 2013, 61% of public expenditure of the country was funded by Chinese money. But there is not much oil left in the national reserves. Ecuador has already sold about 90% of its oil to China.

As a result of this homogeneous investment vector, the two countries are subject to the world conjuncture and are vulnerable to exchange rate fluctuations.

On the other hand, there are two other different strategies of dealing with FDI on the example of Brazil and Mexico — two leading countries in the region regarding investment inflows.

Mexico disposes the export-oriented way of participation in global value chain that means that the end market of manufacturing products are developed countries, mainly the US. It attracts FDI by allowing foreign companies to re-export goods and services with no payment of taxes, no compensatory quotas and other specific benefits. Thus, the competitive advantage of Mexico's economyis low cost of labor and the country does not have firm linkages with local investors and suppliers.

On the contrary, Brazil domestic-market-oriented strategy makes rigorous requirements of its investors. The objective is to develop domestic production and balance regional infrastructure. Firstly, the branches lacking financing in each state are identified; secondly, the global market is examined for finding and inviting the required investors. In addition, the Brazilian government has recently embarked on a policy aimed at allowing foreign banks and venture capital companies to enter the market, but only that are willing to credit the real sector of the economy and invest in innovative sectors, and not focused on financial speculation. Moreover, manufacturing industry in Brazil has benefited from the advantages offered by a large internal and regional market, and thus has expanded into more complex and diverse activities, generating local innovation.

It is worth mentioning that due to the differences in the investment strategies of these two countries, the standard of living is higher in Brazil. According to Legatum Prosperity Index Brazil is 15 positions above Mexico. The country of South America occupies the 49 position in the ranking, while Mexico has achieved only the 64$^{th}$ place. Russia is even lower (68$^{th}$ place) [9]. The possible reason for Latin American countries to pass ahead of Russia in the given ranking is a progressive tax system applied both in Mexico and Brazilthat encourages a more equal income distribution.

## Correlation analysis

To confirm that competent investment involvement in the emerging market functioning should evoke output growth, a brief correlation analysis was conducted based on the statistical data for the period from 1970 to 2013. The correlation coefficient in this case indicates the degree of linear tightness betweenGDP and FDI. In order to determine the direction of causation the two options areunder consideration. In the first case, we calculate the correlation coefficient under the condition that data of FDI inflows is one period later that GDP. The second case reflects the situation in reverse. As we can see, the level of tightness is higher for the first option almost for all the selected countries (see Table 1).

*Table 1*

**The degree of linear tightness between GDP and FDI**

| | Argentina | Brazil | Chile | Colombia | Mexico | Peru |
|---|---|---|---|---|---|---|
| GDP 0 FDI 1 | 76% | 95% | 97% | 94% | 91% | 96% |
| GDP 1 FDI 0 | 77% | 87% | 95% | 92% | 89% | 96% |

As a matter of the table, we can conclude that it is more likely that GDP influences the investment inflows. Thus, it is necessary to ensure the GDP growth at the expense of domestic production at first, and then use foreign direct investment as an incentive for further development.

## Conclusion

Russian economy disposes the similar level of market development as Latin America. Chronologically, the economy of the Russian Federationhave a lot in common with Brazil — the largest Latin American country. The period of industrializationwas endured almost at the same time. Moreover, the two countries began a painful reorganization both in politics and in the economy almost simultaneously, in the 90s of the last century. And finally, the beginning of the new millennium was the time for both countries to revitalize.

The difference is that the current welfare of Russia is mostly based on high oil prices. Once a decline in demand for the black gold, the economy of our country is on the point of collapse, revealing lots of weaknesses.In this respect it resembles Venezuela and Ecuador.

Mexico has also many features in common with Russia. It is a country with a large internal market(population exceeds 100 million people: 122,33 million people in 2014 [4]), Mexico is rich in mineral resources, especially in oil,being a raw material appendage of developed countries. Both of these countries are characterized by a low level of mineral processing, resulting in low economic efficiency in primary and secondary sectors. As well as in Russia, Mexico'sbudget is based on revenues from mineral resources' export revenues, except for the fact that Russia is supplying its resources mainly to the European Union, and Mexico — to the United States.

Taking it all into consideration, the experience of Latin America in foreign capital regulation is of crucial importance. Therefore, the following lessons should be learned to improve the investment strategy in Russia:

- Diversification of investment involvement guarantees economic stability.

The sustainable economic development is only possible when the national economy relies on a variety of successful sectors. It allows to hedge against the sharp drop in prices of a particular product and secures constant amount of revenues.

- Domestic-market orientation encourages innovation.

It is necessary to give a chance for national industry to develop enough for participating in global value chain, otherwise in would not bear the external competition. In addition, the protectionism at the first stages guarantees the human capital accumulation that encourages participation in more complex and diversified activities.

- Local linkages guard from world market fluctuations.

The support of local suppliers is a way to avoid instability. Besides, Russia has an opportunity to cooperate with Brazil being a member of BRICS. In July2014, The BRICS Development Bank was founded as an alternative to the existing US-dominated World Bank and International Monetary Fund. This bank gives its members a chance to escape high interest rates and be more independent from developed economies.

- Floating exchange rate decreases investment risks.

This type of exchange rate regulation applied in Latin America supposes inflation targeting. In turn, this makesthe situation in the country more predictable for foreign investors. On November,10 2014 The Bank of Russia abolished the existing mechanism of exchange rate policy, repealing the exchange rate maintenance within the interval framework of admissible values of the bi-currency basket [6]. However, the crisis of 2014 -2015 has obliged the Central Bank to conduct foreign exchange transactions in order to stabilize ruble exchange rate that can undermine investors' trust.

- Progressive tax reduces inequality.

It is high time for Russia to introduce a progressive tax system, learning the example of Brazil, where it encourages economic growth. The excess funds should be spent on education and health that will significantly improve the quality of the labor force, and therefore encourage faster growth.

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# THE SUKHOI SUPERJET 100 PROJECT AS AN OPPORTUNITY TO HELP RUSSIA STRIKE THE RIGHT BALANCE BETWEEN ECONOMIC SECTORS

## Abstract

*Russia's economy has always been in trouble because of structural imbalances. Diversification is the best solution to this challenge. In particular, the intensification of aircraft production can become a great way to support Russia's industrial sector. There are several projects, e.g.the SukhoiSuperjet 100, the development of which can stimulate the growth of Russia's non-oil and gas exports. The leading-edge technologies penetrate every stage of this project, delivering a modern, economically efficient and globally marketable aircraft.*

***Key words:*** *aircraft building, diversification, new technologies, international competition.*

Russia's economy has always been in trouble because of structural imbalances. It is common knowledge that Russia is hugely dependent on oil and gas production. Therefore the falling oil price caused the upcoming recession, severe financial crisis and collapse of the national currency. Furthermore, western sanctions restrict Russian companies from refinancing their debts, which makes the situation even worse.

Many economists believe that diversification is the best solution to this challenge. Russia needs to improve economic institutions and mobilize resources in order to develop areas other than oil and gas. For example, Russia has a great potential for the production of weapons and military equipment, agricultural goods and certain elements of high-tech products (e.g. titanium forgings for aircraft). According to Prime Minister Dmitry Medvedev, the situation with sanctions is to be used to find new opportunities for growth [5].

In particular, the intensification of aircraft production can become a great way to support Russia's industrial sector. Besides, it is sure to contribute to the development of regional transport networks and increase the export potential.

Aircraft manufacturing in Russia has been developing since the beginning of the 20$^{th}$century. At the outbreak of the First World War, Russia had twenty-four aircraft manufacturers, which produced 1,893 units from 1914 to 1916 [1]. However, they were dependent on foreign engines, importing thousands of those during this period. Unfortunately, after the February Revolution the aircraft production declined sharply and virtually ceased in 1918.

In the Soviet era, free market competition between companies was seen as wasteful. Instead, there was a multi-tiered system, the components of which were design bureaus (OKBs) and manufacturing complexes. Requirements for proposed aircraft were created by the Soviet air forces, whereas state research institutes provided OKBs with information on aerodynamics and available systems. Due to political considerations the assignment of production was widely dispersed, and the role of state planning was paramount.

In the late 1980s, the Soviet Union accounted for 25% of the worldwide civil and 40% of the worldwide military aircraft production [1]. The dissolution of the USSR led to disconnection between end users, export companies, assembly plants and component manufacturers. Entire segments of Russia's aviation requirements were now located in foreign countries, including Ukraine, Georgia, Czechoslovakia and Poland.

The whole manufacturing sector was devastated by imports. As a result, the civil aircraft industry experienced a deep crisis. In fact, in 2000, the country produced only 4 aircraft for civil purposes, whereas in 1990, the number reached 715. Fortunately, in 2001-2006, the industry started receiving new orders from leasing companies, which was the beginning of recovery. Aircraft manufacturers managed to pay their debts or get them restructured, and the production levels started increasing again.

In 2005, the government under President Vladimir Putin initiated an industry consolidation programme and created the United Aircraft Corporation (UAC) in order to optimize production lines and minimize losses. The programme was divided into three parts:

1) reorganization and crisis management (2007–2010),
2) evolution of existing projects (2010–2015),
3) further progress within the newly created structure (2015–2025).

The deliveries of civil aircraft increased to 6 in 2005, and in 2014 the industry delivered 37 aircraft, both to domestic and international customers. However, this quantity is not sufficient since more than 90% of aircraft used by Russian airlines are built in the West. It makes the industry vulnerable to potential future sanctions imposed due to the Ukraine crisis.

Curiously enough, the United Aircraft Corporation (UAC) is aimed at becoming the world's third largest producer of military and civil aircraft by 2025, Boeing and Airbus still being leaders in aircraft manufacturing [7]. In order to reach this goal, Russia will have to build from 250 to 300 planes by 2025. First of all, the industry needs to deal with an urgent productivity problem anddiversify away from a long-standing orientation towards military production.

While Russia is still a prominent exporter of military aircraft, it lags behind in the civil aircraft market. However, there are several projects, namely the SukhoiSuperjet 100 (SSJ-100) and the Irkut MC-21, whose development can stimulate the growth of Russia's non-oil and gas exports. The first flight of the MC-21 is going to take place in 2016-2017, whereas more than 80 of SSJ-100 aircraft have already been manufactured.

The Sukhoi Superjet 100 regional airliner's development was launched in the early 1990s. The plane, which first flew in 2008, has already been referred to as the most important and successful civil aircraft programme of the Russian aerospace industry. The leading-edge technologies penetrate every stage of this project — from design and development to final assembly, delivering a modern, economically efficient and globally marketable aircraft.

The SSJ-100's production sites are located in three Russian cities. The plane's airframe parts are manufactured in Komsomolsk-on-Amur (KnAAPO) and Novosibirsk (NAPO), while the technologically advanced production site is situated in Voronezh (VASO).

The project is developing with active participation of foreign companies. Thus, in June 2007, Sukhoi Company, Italian Finmeccanica Group, Sukhoi Civil Aircraft Company (SCAC) and AleniaAeronautica (Italy) signed a General Agreement to establish a strategic partnership, which outlined the foundation of a joint venture. This Agreement stipulates that AleniaAeronautica acquires 25% + 1 share in SCAC and provides with no less than 25% of financing [2].

In 2007, AleniaAeronautica and Sukhoi Holding formed SuperJet International, a joint venture (51% — AleniaAeronautica, and 49% — Sukhoi Holding), which became responsible for marketing, sales and aircraft delivery in Europe, North and South America, Africa, Japan and Oceania. In addition, it is supposed to offer aircraft customization for western customers and a full package of aftersales support.

Another strategic partner of the project is Snecma, a globally recognized engine manufacturer. A joint venture of Snecma and NPO Saturn (a Russian aircraft engine producer) provides the SSJ-100 with the SaM146 engine applicable for the entire aircraft family. This engine guarantees that the SSJ-100 perfectly fits the ICAO current and perspective noise and emission requirements.

Besides, the project's consultant is Boeing, the world leader in manufacturing and selling airplanes, rotorcraft, rockets and satellites. Under the long-term cooperation agreement signed in 2002, Boeing consults SCAC in the field of marketing, design and manufacturing, certification and quality system, supplier management, and after-sales support.

It is noteworthy that Boeing and Russia have long-term partnerships in multiple areas, including not only aviation, but metallurgy, space, engineering, information technology (IT) and communications. The company has a long track record of successful investment and partnerships with Russian industry and science. What is more, Boeing purchases 35% of its titanium supply from the Russian producer VSMPO-AVISMA [6]. Titanium forgings from Russia are used for manufacturing Boeing 787, 777 and 737 commercial airplane models.

The Russian aircraft has several significant advantages, which makes the airplane competitive on the global market. First, the SSJ-100 aerodynamic configuration is specifically optimized in order to reach high cruise speed without any dramatic increase in fuel consumption. Besides, the aircraft's enhanced take-off and landing performance along with all-weather operation make the

SSJ-100 an efficient route developer. As a result, the SukhoiSuperjet 100 offers 10% decrease of operation costs compared to its rivals [2].

Secondly, optimal piloting in automated mode together with the failure-safe flight control system can ensure additional fuel efficiency and improve flight safety. Actually, the SukhoiSuperjet 100 is sure to become the first regional aircraft, using advanced control system features.

Thirdly, noise and emissions levels of the SSJ-100 meet the strictest ecological demands and surpass the highest existing and future ICAO requirements. In fact, the SSJ-100 is the first Russian airliner to attain EASA certification, which is a significant achievement for the country's civil aviation sector.

There are several other notable advantages of the SSJ-100 [3], such as:

- high level of unification of the aircraft systems family, which reduces the cost of maintaining the fleet;
- development of the aircraft according to the demands of potential customers, which are the members of the Advisory Board;
- avionics system which allows pilots to carry out landing in adverse weather conditions;
- high aerodynamic efficiency formed on the basis of extensive testing and advanced technology design.

The figures for the key characteristics of the aircraft given in Tables 1 and 2 below illustratethe performance of the SSJ-100 in comparison with its rivals.

*Table 1*

**Operating Characteristics**

| | EMB 190 | CRJ 1000 | ARJ 21-700 | TU-334 | SSJ 100/95 |
|---|---|---|---|---|---|
| Number of passengers (seat pitch 32») | 98 | 100 | 90 | 102 | 98 |
| *Flight range* | | | | | |
| Standard, km | 3,148 | 2,761 | 2,225 | 2,800 | 3,045 |
| Extended, km | 4,260 | 3,131 | 3,700 | — | 4,420 |
| *Maximum takeoff weight* | | | | | |
| Standard, kg | 47,790 | 40,824 | 40,500 | 47,900 | 45,880 |
| Extended, kg | 50,300 | 41,640 | 43,500 | | 49,450 |
| Annual flying hours | 2,800–3,000 | - | - | 2,200 | 3,000–3,200 |

Source: http://superjet.wikidot.com/compare

*Table 2*

**Comfort**

| | EMB 190 | CRJ 1000 | ARJ 21-700 | TU-334 | SSJ 100/95 |
|---|---|---|---|---|---|
| Cabin width, m | 2.5 | 2.2 | 3.1 | 3.5 | 3.2 |
| Cabin height, m | 2 | 1.9 | 2 | 2.1 | 2.1 |
| Seat width, mm | 463 | 440 | 455 | 420 | 465 |
| Luggage racks size, $m^3$ | 53 | 42 | - | 53 | 70 |

Source: http://superjet.wikidot.com/compare

The first SukhoiSuperjet production was delivered to the Armenian airline Armavia in 2011. Armavia was going to operate its Superjet 100 on flights between Yerevan, Sochi and Ukrainian cities. The airline expected to receive its second Superjet in June 2011.However, in 2012,Armavia went bankrupt and both of its ordered airplanes were returned toSCAC.

Nowadays, according to official data, the SukhoiSuperjet order backlog is about 180 aircraft, including already delivered machines. The company's customers are Aeroflot, Gazpromavia, Lao Central Airlines, Sky Aviation (Indonesia) and several more airlines. It is worth mentioning that in 2011 Mexico's third largest airline Interjet signed a $650 million deal for 15 Sukhoi Superjet-100 civil aircraft, with an option to purchase five more. It is the first airline of the Americas to order a SukhoiSuperjet 100 and the first success of SCAC in approaching the North American market.

At the end of October 2013, Interjet confirmed outstanding results in terms of operations. Representatives of the airline claimed that they are truly impressed by the SSJ-100. Miguel Aleman, the owner of a private foundation "Miguel Aleman Foundation", which also owns "Interjet", said that the aircraft is "the best that we had".

In October 2014,SCAC signed a contract with Belgian VLM Airlines. The company is going to deliver 2 aircraft in 2015. This is another significant step for the Russian manufacturer, which may become a good start of the successful operation of the Superjet in Europe.

Nevertheless, the sales system of the SSJ-100 has to be seriously strengthened [4], developing cooperation with leasing companies. SCAC needs to learn to respond to any questions from potential customers, even though they are going to order only two or three planes. Moreover, the potential of new and fast-growing airlines is not to be underestimated. Recalling the experience of the Mexican Interjet, those companies may become new leaders of the regional markets, using the SSJ-100 as one of the means to success. Consequently, other potential customers, including the world's major airlines, are likely to become more interested in Russia's civil aircraft production. Of course, competition in the aircraft manufacturing market is quite tough. However, the current crisis can motivate the United Aircraft Corporation to explore new opportunities for growth and develop its marketing strategy.

To sum up, the SukhoiSuperjet 100 is a hope for the Russian civil aviation sector. In the context of upcoming recession and Western sanctions there are not so many options to strike the right balance in Russia's economy. However, the development of this project is the real chance to help Russia become not only oil and gas exporter, but one of the world's best manufacturers of machines and high-tech equipment.

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# THE RUSSIAN RESPONSE TO THE SANCTIONS. THE IMPLICATIONS IN THE FUTURE COOPERATION

## Abstract

*The research analyses the implications in the future cooperation between the Russian Federation and the country-members of the European Union due to solid economic ties, such as: energy industry (85% of Russian exports to the EU), mineral resources (6%), machinery and equipment (1,5%) and others. It stresses the importance of reconciliation between the Russian Federation and the European Union in order to mitigate the disruptive influence of sanctions on the economies of the stated countries and their well-being.*

***Key words**: sanctions, Ukrainian crisis, food embargo, diplomatic sanctions, Restrictive measures, Sectoral sanctions.*
***JEL codes:** F 51, D 72*

## Introduction

The main reason for the sanctions from the part of the EU is the de-escalation of the current crisis in Ukraine. According to the officials of the European Union the Russian Federation violated the sovereignty and territorial integrity of the neighboring state and thus, answering to the occupation and to the aggression of the RF, the EU on the 3 of March 2014 called on Russia to refrain from further violation of the international law and to withdraw its forces from the occupied territory (the EU officials relied upon the presence of the Russian troops in the Crimea as well as the authorization of the Federation Council of Russian on the 1 of March 2014 to use Russian armed forces abroad on the discretion of the president). Following the 3 of March the Heads of State or Government in the EU assembled on the extraordinary meeting on the 6 of March in order to outline that the only possible solution to the existing crisis was the peace talks between the Russian Federation and the Ukraine with the possibility of multilateral negotiations. Due to the absence of de-escalatory steps from the RF the EU on the 17 of March 2014 imposed the first round of sanctions on the officials of the Russian Federation directly or indirectly involving or profiting from "the annexation of the Crimea".

Overall the sanctions can be divided into several groups: diplomatic sanctions, restrictive measures, restriction for Crimea and Sevastopol and sectoral sanctions [4].

**Diplomatic sanctions.**

The planned meeting of the G8 was on the way to be held in Sochi but it was suspended and instead the leaders of the ex-G8 now G7 (excluding Russia) met in Brussels on the 4 of June. Additionally the country-members of the European Union decided to suspend the negotiations concerning the Russian membership in the OECD and the International Energy Agency. Moreover regular bilateral summits between the Russian Federation and the European Union were cancelled as were the negotiations concerning the facilitation of the visa regime between the country-members of the EU and the RF. According to the existing information the process of revision of the existing partnership and cooperation programs between the countries is on the way and the result will depend solemnly on the outcome of the crisis as well as on the future diplomatic cooperation between the countries.

**Restrictive measures.**

As it was noted before the officials of the European Union decided to impose personal sanctions on a number of Russian public persons directly or indirectly involved in the crisis in order to push the negotiation process and to gain leverage in the peace talks. Thus 151 persons were targeted by the sanctions — government (Sergei Naryshkin, Vladislav Surkov, Dmitry Rogozin) and military representatives, the so-called inner circle (Arkady and Boris Rotenberg; Sergei Chemezov; Vyacheslav Volodin) [7] — the businessmen closely related to the president (which are able to express their opinion and influence that of the president) and the companies (37 entities — mainly the export companies in the oil and gas sector, military export companies (Kalashnokov Concern, Almaz-Antey) and the 5 largest banks(Ban Rossiya, Vnesheconombank, Gazprombank, Sberbank). The ones directly touched by the sanctions are now having their assets frozen (it is impossible to operate them) and the visas banned.

**Restrictions for Crimea and Sevastopol.**

According to the current position of the EU officials the Crimea was annexed by the Russian Federation and thus it is the primary target of the sanctions in order to stimulate the peace talks and eventually restore the territory integrity of the Ukraine and protect its sovereignty.

From the 17 of March 2014 all imports from the peninsula are banned unless they are accompanied by the certificate of origin provided by the Ukrainian authorities. Additionally all investments in the Crimea are banned, Europeans and European companies are prohibited to acquire the real estate, establish companies, provide financing for the companies or even supply services in the peninsula, it also applies to the tourist sphere while no European operators are allowed to offer their services in the Crimea and the cruise ships are forbidden to call at the Crimean ports (unless it is an emergency), it also applies not only to the cruise ships but to the cargo ships or any other ships flying under the European banner [1].

A number of sectors is targeted especially in the Crimea: transport, telecommunications, energy sectors, upstream, midstream and downstream for the oil and gas industry and mineral resources. All types of technical assistance, servicing or supply of necessary technologies is strictly forbidden for the Peninsula.

**Sectoral sanctions.**

Firstly it is utmost important to point out the financial side of the sanctions. Since the 17 of March 2014 the Europeans and the European companies and prohibited to participate in the financial activities — acquire or sell any financial instruments with the maturity exceeding 30 days by the three major Russian energy companies, three major Russian defense companies and five major state-owned Russian banks (as well as their subsidiaries or any entities under their control). Additionally, no financial services can be provided to the following companies.

The European Union worked out a «military list» specifying the banned lethal and non-lethal armaments which can't be exported or imported in the Russian Federation (as well as related materials and necessary technologies). Moreover, the EU worked out a second list — «list of dual use goods» which prohibits the imports and exports of any goods on the list on the basis that they can be used both in military and civil sectors, thus imposing additional restrictions on the Russian economy and weakening the existing partnership with the European companies.

The energy sector is one of the crucial for the economy of the Russian Federation and it was also targeted by the European sanctions in order to gain additional leverage during the peace-talks. Thus the equipment used in the energy sphere (the export and the import) now, prior to the agreements and the payments, has to be authorized by the European officials in order to be approved or disapproved for further transportation and exchange (mainly in the domain of technologies). In case the technologies of the equipment is destined for the deep water oil exploration, arctic oil exploration or shale oil projects in the Russian Federation the technologies will not be provided and the contracts will be annulled. Additionally, no service can be provided in the stated oil and gas projects in order to put an additional pressure on the key sector of the Russian economy.

## The sanctions of the Russian Federation against the EU

In order to assure the colleagues in the European Union of the political position of the Russian Federation it worked out a number of sanctions (both personal and sectoral) as a set of counter-measures against the rising pressure from the country-members of the European Union.

On the 6 of August 2014 the President signed a decree «On the use of specific economic measures» which authorized a one-year embargo on fruit, vegetables, meat, fish, nuts, milk and dairy imports not only from the EU but also that coming from the US, Australia, Canada and Norway. The food exports from the EU to the RF were worth 11,8 bn. € (10% of the total exports of food) — only 5 bn. € were actually affected as Russia did not impose restrictions on soft drinks and alcohol. Additionally, the Ukrainian aircraft were banned from the Russian airspace and Russian officials consider the possibility of banning the airspace for the European countries [2].

As for the personal sanctions — in the winter 2014/2015 three politicians (members of the national senate of the European parliament) from Lithuania, Latvia and Poland were blocked from crossing the border of the Russian Federation.

The impact of the sanctions differs greatly among the country-members of the European Union. This is due to the difference in the scale of cooperation between the country-members and the Russian Federation. Germany leads the commercial trade with Russia with 75 bn. €, the Netherlands 37 bn. €, Italy 30 bn. € and Poland 26 bn. € [8]. Moreover, the segments of cooperation are highly diverse varying from the machinery to the food sector. The ones most affected by the currency depreciation and the European ban on the dual use of technology are the countries mainly interested in the machinery exports to the Russian Federation — Germany, Italy and France. While the ones mostly affected by the direct Russian sanctions are Poland, Finland, Greece and Spain as they were cooperating with the Russian Federation in the food sector.

## Conclusion

On the 13 of March 2015 the officials of the European Union decided to prolong the sanctions against the Russian Federation due to the lack of cooperation on the part of the RF in resolving the issue with the Ukrainian sovereignty and integrity. Further prolongation of the sanctions will be discussed prior to the 15 of September 2015.

The Russian officials consider a partial withdrawal of sectoral sanctions banning the import of food in the RF. The condition for the lifting of imports will be the need to subsequently process imported food in Russia as a measure aimed to support national food industry. Moreover, in the lower chamber of the Russian Parliament (Russian State Duma) was submitted a draft lifting the trade embargo, but, due to the current political situation it is unlikely that this project will pass the lower chamber of the Parliament or the Federation Council of the Russian Federation. [6]

According to the member of the European Parliament Gabrielius Landsbergis «The sanctions' main aim was to get Russia to change its policies»[5]. Moreover, the infrastructure projects that are on the way in Russia are the victims of the impact due to the negative synergies spurred by the sanctions of the EU and the negative dynamics for oil prices. Additionally, the EU now is trying to prove that it is ready to disagree with and oppose the Russian foreign policy when it comes to the oppression and the violation of the sovereignty of the neighboring nation in the Europe.

Nevertheless, not everybody in the EU shares the same point of view — according to the Greek prime minister Alexis Tsipras his country can become a bridge between the two worlds — the Russian and the European one in order to deal with the sanctions and with the whole political crisis, additionally he claimed that his government disagrees with the sanctions and that Russian companies will participate in the tender for deep-sea oil and gas exploration in Greece (now Russia supplies 57% of the natural gas in Greece) [3].

In the light of the recent meeting between the representative of the Russian and the French businesses (Movement of the Enterprises of France) — “Reliable business cooperation. Russia out of the conjuncture” — the sanctions were claimed to be the economic weapon of the XXI century and thus counterproductive because they don’t serve their purpose as they endanger foreign companies as well as Russian companies and the possible cooperation between the countries in general.

As a result — the EU is now divided in the political and economic matters because the future cooperation in many spheres is now endangered due to the imposition of Russian and European counter-sanctions. However, we can notice (according to the officials from both sides) that the situation is slowly recovering and turning to the better side as both parties (mainly businesses) are striving to renew the cooperation in order to work for the betterment of all stakeholders involved.

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# INNOVATIVE TECHNOLOGIES FOR WATER TRANSPORT AND ITS INFRASTRUCTURE

## Abstract

*The economic benefits of using products made of composite materials are expressed in the use of a stronger material. The economic effect is achieved directly by reducing the cost of production of the required product, the ability to withstand long-term corrosion and temperature changes. Everything mentioned is confirmed by comparative calculations of the economic efficiency of the application of different materials in different conditions.*

***Key words:*** *composite materials, water transport and its infrastructure.*

## Introduction

There are many innovative technologies today. One of them is the use of composite materials and products made of them in aerospace and sports equipment as well as in other branches of industry and agriculture, including water transport and its infrastructure. Besides, composite and polymeric materials are used in shipbuilding.

## 1. A brief history of composite materials

Materials which people use in their activities always played an important role in the progress of civilization. They gave the names of the stages of human development, such as the Stone Age, the Bronze Age, and the Iron Age. The history of the use of composite materials numbers many centuries. The modern era can be called the century of composite materials and polymers [5, 35].

Understanding of composite materials is borrowed by humans from nature. The use of natural bitumen enabled them to increase the water resistance of natural materials and produce vessels of reeds, impregnated with bitumen. For a long time features of bamboo have been used for making ships' masts. Thus, the creation of composites is not only the achievement of modern technology [1, 31]. And at the same time only in the XX century composites became widespread. The science of composite materials was born in 1960-s. The science of composites is considering both properties and production technology [2, 8-9].

As a result, it now permits to produce a huge number of different types of composite materials and their products.

## 2. The advantages of composites

The composites are combinations of two or more materials (reinforcing elements and resin) which retain their identities while acting in concert. The composites are a safe and reliable material which is capable to withstand any conditions and different environments and have outperformed traditional materials for many years.

Composites offer the following important benefits.

- First of all it is **light weight** — Composite parts are lighter than steel parts with similar thermomechanical properties.
- Secondly it is **high strength**, because glass fibers are stronger than steel.
- Also they are **easy to shape** — Composites can be molded into complex shapes at relatively low cost. This flexibility offers designers an extensive range in new product design.
- **Integration of functions** is also important. The reason is, parts with multiple functions can often be made in a single step with the help of composites.
- Then comes **corrosion resistance** — Composites provide long-term resistance to severe chemical and temperature environments.
- Also there is **durability** — Composite structures have an exceedingly long life span. Coupled with low maintenance requirements, the longevity of composites is a benefit when used in critical applications. After a half-century of use many well-designed composite structures have yet to wear out.
- And finally **Cost savings** — Thanks to their low weight and high mechanical properties the use of composites in many applications reduces manufacturing, shipping and maintenance costs compared to traditional materials such as steel [7, 18].

## 3. Modern perspectives of the use and application of composite materials in water transport and its infrastructure

Now there is a rapid increase in the production of polymer composites and products from them and their imbedding into a variety of technology, the successful penetration into many traditional materials, ceramics, glass, wood and polymers. Accordingly we witness a growing number of inventions and new technologies, conferences, specialists and scientific publications.

The widespread introduction of composites in shipbuilding based on synthetic resins and high-strength non-metallic fibers took place in the 70-80s.

Thus the following were produced:

- small and sports vessels;
- coatings of different kinds;
- cylinders, pressure vessels, manufactured by method of winding;
- protective constructions using composite armor and others.

Today the main areas of application of composites in shipbuilding are:

- the production of ultrastrong ship's hulls (housing element);
- the use of composites in the hulls and elements of marine engines and propulsors;
- the decoration of ship's rooms;
- ship's fire and heat protection.

At the present time various kinds of composite materials are actively used in hydraulic engineering.

For example in:

- beaching;
- strengthening of slopes;
- flood protection;
- landscape works;
- creation of artificial reservoirs, hydraulic structures, etc.

To fulfil these works we use various kinds of sheet piles, including the sheet piles made of composite materials.

Nevertheless in spite of all these beneficial factors various kinds of products made of composite materials are still not actively used in water transport and its infrastructure.

First, this is due to the fact that the experts do not have the necessary information about the possibilities and characteristics of the composites.

Secondly, a list of normative and technical documentation, which regulate the requirements for the production and application of composites, is missing.

Thirdly, we witness the ignoring of the available regulatory documents confirming the suitability for the application of new technical solutions with the use of composites.

As a result, not only the introduction of new technical solutions with the use of composites is inhibited, but also the use of technical solutions that have been previously applied and have proved their technical and economic efficiency, reliability and safety is slowed down. This is especially true in water transport and its infrastructure, where the use of such solutions can provide significant savings invested in their budget.

For a radical change in the situation regarding the use of composites, structures and products made of them (Order number MS-91-r dated 11.09.2013), the Ministry of Transport of the Russian Federation has approved a program of the implementation of composite materials, structures and products made of them in the field of transport. The aim of the program is the creation of the conditions for a prompt and large-scale introduction and widespread use of modern and effective composites, structures and products made of them [6].

This issue was heatedly discussed at the meeting of the Union of transport workers on February 26 this year.

Composite materials have advantages over traditional building materials. In an interview with a journalist from the newspaper Vedomosti on 30 January 2012, Prime Minister Vladimir Putin called the development of the composite industry one of the strategic directions of the development of industry in Russia in the near future [4].

The aforementioned program has been developed in accordance with the list of orders of the President of the Russian Federation on November 12, 2012 № pr3028 following the meeting of the Presidential Council for economic modernization and innovative development of Russia [8].

The subject of the use of composite materials in water transport and its infrastructure was lively discussed at the meeting of the Council of state administrations of Maritime and River Transport of The coordinating transport

Council of the States-participants of CIS (Commonwealth of Independent States), which was held on October 7, 2014 in Minsk, under the chairmanship of the Head of the Federal Agency of Sea and River Transport A. Davydenko. The Council was attended by the delegations from Azerbaijan, Belarus, Kazakhstan, Moldova and Russia, as well as business structures. Among other issues, the participants discussed the problem connected with the use of composite materials which are made with the use of pultrusion technology in the construction and repair of hydraulic structures.

All this shows a high practical significance of the scientific development of this issue for the use of the products of composite materials in water transport and its infrastructure, not only in Russia, but also in the countries of the Commonwealth of Independent States.

## 4. Economic efficiency of the use of composite materials for water transport and its infrastructure

Profit is a major element in providing self-financing of enterprises, the possibility of which is largely determined by how revenues exceed costs.

Finance, credit, price, cost and other tools are directly or indirectly linked to profit. The main tasks for the domestic production in the current economic conditions are as follows:

- to reduce the production cycle;
- to improve the quality of products;
- to reduce manufacturing costs.

The manufacturing process of industrial production of composites (fiberglass, basalt, carbon plastic) is becoming increasingly important due to the depletion of natural resources and the rising cost of energy. In the long term, the creation and development of composite industry is caused by the need of the economic transition to an innovative way of development, the support of the economic growth and gross domestic product of the country at the expense of the processing industries of secondary raw materials and industrial waste, as well as the diversification of export potential.

The innovative production of composite materials leads to an increase of competitiveness of enterprise, strengthens the position of the enterprise in the market and sales promotion of goods, improvement of basic economic indicators of economic activity of the enterprise.

The nomenclature of composite materials used in the economy is developing, which leads to lower capital costs and the opportunity to work at a small and rapidly changing output. The authorities offered to create branch programs on the use of composite materials in related sectors of economics. As a result, by 2020 the volume of domestic production of composites will grow from the current 16.6 billion to 120 billion rbl, while the share of exports will increase from 1% to 10% [9].

From this it follows that the products of composite materials have a great perspective and will be increasingly introduced into the practical activities of water transport facilities and infrastructure.

## ECONOMIC JUSTIFICATION OF MATERIALS REPLACEMENT
### in the project of Strengthening the coast line of 1120 metres Russia, Republic of Tatarstan, Volga River*

| Cost of materials (option with L-5 UM) | | | | | Cost of materials (option with SK-150) | | | | |
|---|---|---|---|---|---|---|---|---|---|
| *The coastline is 1120 m* | | | | | | | | | |
| **Name of materials** | **Unit of measurement** | **Amount** | **Cost of per unit, rub.** | **The sum, rub.** | **Name of materials** | **Unit of measurement** | **Amount** | **Cost of per unit, rub.** | **The sum, rub.** |
| **The sheet pile Larsen Л 5 UM L = 8,0 m** | t | 2171 | 38 500 | 83 583 500 | The sheet pile SK-150 L=8, м | $m^2$ | 8960 | 4 500 | 40 320 000 |
| | | | | | The corner connector USK-150 | running meter | 48 | 1 100 | 52 800 |
| | | | | | The pipe Ø 108x3.5 (under conductor) | t | 16,868 | 28 090 | 473 822 |
| | | | | | The channel section №10 (under conductor) | t | 20,204 | 26 190 | 529 143 |
| | | | | | The channel section №12 (distribution zone) | t | 11,648 | 24 690 | 287 589 |
| | | | | | The anchor pile pipeØ159x6 | t | 42,382 | 28 190 | 1 194 749 |
| | | | | | The anchor traction steel circle Ø30 | t | 15,585 | 24 690 | 384 794 |
| | | | | | The stone prism. The stoneD max= 70 cm | t | 10080 | 750 | 7 560 000 |
| | | | | | The nut M 30 | unit | 1404 | 24 | 33 696 |
| **TOTAL:** | | | | **83 583 500** | **TOTAL:** | | | | **5036592** |

The total sum of project was reduced by more than 32 million roubles in the result of replacing steel sheet pile L-5UM for composite sheet pile SK-150! The saving is amazingly over 35%.

* Information on the basis of the report of the research project “Analysis of the developed technologies of application of composite materials of new generation and design and technological solutions for possible use at the water transport and infrastructure». Number state registration 114 121 55 00 13.

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# FOREIGN DIRECT INVESTMENT IN CHINA AS ONE OF THE MAIN GROWTH DRIVERS FOR EMERGING ECONOMY

## Abstract

*Nowadays, all countries aspire to reach significant economic growth. It makes very actual scrutiny of strategy to succeed in emerging markets in terms of globalization. The paper under consideration covers the role of foreign direct investment in China as one of significant factors for developing economies. Chinese government realized potential and strengthens of national economy, implementing policy of openness and all advantages of FDI. Through time-line analysis we highlight interconnection between FDI and current state of economy of China.*

***Key words:*** *emerging markets, Chinese economy, Foreign Direct Investment, economic growth.*
***JEL codes:*** *E 200, F 210*

## Introduction

There are different opinions about national economy of China. The situation is that there are few reasons for classifying China as a country with transition economy. Firstly, China is a country with low per capita income. Secondly, China is in the process of opening up market. Thirdly, state is implementing transition reforms. Moreover, experts claim that Chinese economy is fast growing, and this progress includes an increase in local and foreign investment. At the moment, there is a combination of state-owned sector and an open market economy.

During transition reforms the Government has been changing the type of national economy from a planned economy, in which the “hand” of the state defines all the parameters, to a market economy. A gradual phasing out of government pressure and control on companies contributed to their development as well as become self-supporting, which beneficially affected domestic market in China. Market pricing led to internal competition among manufacturers, and it improved the quality of products and production efficiency. The latter ensures a strong demand for the products of Chinese manufacturers, which has increased production and provide employment. These factors are attractive to foreign investors [23].

Remain under state control interest rates, tariffs for public utilities, prices of petroleum products. The influence of the state on pricing mechanisms for other products is permissible only temporarily and in the case of high inflation.

State control is maintained only at the macro-level, using the tools of fiscal and monetary policy [24].

If we compare China with other developing countries, China's economy has one of the most favourable investment climates in the world. This particular advantage makes possible to export products to foreign markets, new technologies for enterprises in China. At the same time, China is beginning to invest more in companies abroad.

Thus, foreign capital was essential for the economic miracle of the PRC. Indeed, foreign investors contribute, not only by investing, but also introducing new technologies, creating jobs, expanding the geography of the market for goods of Chinese enterprises. This in turn increases the performance of export volumes, which is important [5], [6].

Such recognition of China as an effective recipient of foreign direct investment, makes the country interesting to study its experience, which can be used to increase the investment attractiveness of other countries.

## Features of Foreign Direct Investments in China

The concept of foreign investment involves investments of non-residents in the national economy. Non-residents of the countryare the economic actors, whose origin and legal capacity, which is not in the jurisdiction of the country. Foreign investment — is the use of non-residents investments in items of business activity in the country.

In research we cover real Foreign Direct Investment. In case of "green field" investment, investors need to create an entirely new production in the territory of recipient country, widely used technology, knowledge of investor. In case of "brown field" FDI, it acts as an additional source of funds, that are used to enhance and improve production efficiency at existing enterprises [4]. Exampleof «greenfield» FDI is «Coca-ColaChinaIndustries». Jointventurewasestablishedin 1979 with 10,5% governmentshare [26].Exampleof «brownfield» FDI is «ChanganFordMazdaAutomobile». Jointventurewasestablishedin 2001. State-owned«ChanganAutomobilegroup» owns50%, «Ford» owns 35% and «Mazda» — 15% [27].

One of the features of FDI that investor is able to influence and control the activities of an enterprise, located in the territory of the recipient country. However, for possibility to manage and control the company, it is required that investments is long-term. Moreover, to gain control over enterprise, investor need to purchase at least 10% of the total assets of the enterprise.

*What do make FDI especial for recipient countries?*

- FDI is invested in the production, to be more precise, it means stability for the host country and FDI enterprises. Investor may optionally take out a license, technology of production, equipment and other movable property, but property will remain in the territory of country. Especially because removal and transportation costs could exceed the cost of the equipment, making it pointless export from the recipient country.

- If FDI used for services, it also makes investment extraction impossible.
- FDI is long-term, this leads to the fact that it is quite difficult to put out of business.
- In any case, FDI remain in the recipient country.

At the same time, FDI give a number of benefits over loans. Firstly, the loans are possible only if the creditor (source of capital) trusts company. Secondly, loans must be returned temporarily. Otherwise, the funds obtained in this way can increase the size of the public debt, because the warranty is the state of the recipient country [2].

## Time-line analysis

To understand Chinese miracle, we have to make a retrospective analysis and examine closely its stages of success. The time-line is divided into 4 basic stages. The table below shows a detailed time-line analysis of Chinese success.

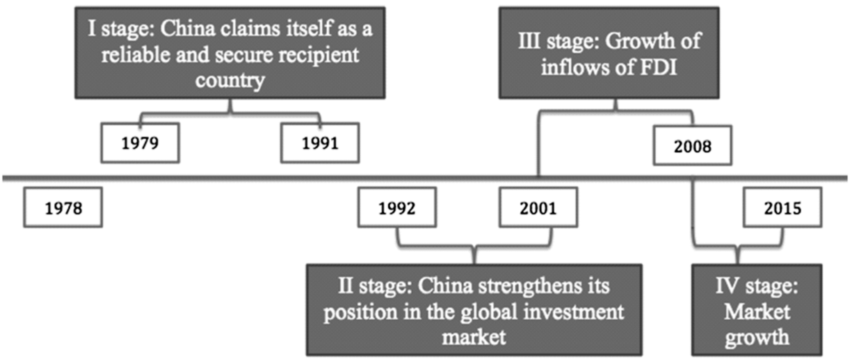


***Figure 1.*** Stages of FDI inflows in China
Created by the author on the basis of time-line analysis

*Table 1*

**Time-line analysis of evolution of FDI inflows.**

| Years | Description |
|---|---|
| **I stage. 1979–1991** | Small amounts of capital were invested in various projects in order to explore possible areas for future investment. During this period, China recommended itself as a reliable and secure recipient country , in the future this will be an advantage over other countries. The main form of investment was loans. This is due to the fact that FDI involves more investment and the investor's responsibility, in case of failure, investor irrevocably loses it's capital. In the form of a loan, it is easier to control your capital, this type of investment is more liquid. During this period, there were developed mainly garment and textile enterprises due to not very large costs. |

| | |
|---|---|
| 1978, December | The beginning of the reforms. The basis of the reform program was the «four modernizations» concept, which meant that transition reforms were related to the industry, the agricultural sector, education and the armed forces. |
| 1979 | The government was implementing «a policy of openness» |
| 1980 | China started to receive loans from the governments of developed countries, the World Bank and the International Monetary Fund. |
| 1983 | There were promulgated regulations in which, among other things, it was noted that « joint ventures created in China contribute to the development of China's economy and improve its scientific and technological development, favor the socialist modernization.» There were allowed FDI in industries associated with the extraction of energy resources, production of building materials, chemical industry, metallurgy, machinery, measuring instruments, equipment for oil production from offshore fields, electrical engineering, computers and telecommunications equipment, light and textile industry, food processing, pharmaceuticals, related to medical equipment, packaging, agriculture, started opening up to foreign investors of the tourism industry. |
| 1984 | To attract foreign investors were initially created four Free Economic Zones (SEZs) and 14 «open» coastal cities. Location of Zones and cities is good for transportation and trade logistics. Transportation by sea is the cheapest way. |
| 1985 | Were created Open Economic Region; territory in the delta area of significant large rivers and territory of some provinces. Wide territory of zones and open regions provides investors with choise. |
| 80-th of XX century | Capital comes mainly from Hong Kong, Macao and neighboring regions because of the proximity and business owners who were ethnic Chinese |
| 1986 | Government provided incentives to FDI enterprises, in case of production for export and production of high-tech products. These benefits include a reduction in prices for the rental of land, use of transport and communication, utility services. Businesses operating within the territory of FEZ and areas of development, typically pay 10% tax. |
| **II stage. 1992–2001** | China strengthenedit's position in the global investment market. Major policies to attract FDI in China during this period can be called desire for significant growth in coming into the country as foreign capital through further expansion of areas with favorable conditions for foreign investment. Government realized principle of favorable treatment to foreign investors. |
| 1992 | A sharp increase in FDI inflows to China. |
| 1993 | China became the largest recipient of foreign capital, and the next two years, the volume doubled (approximately 50 billion US$). |
| 1994 | Growth of FDI inflows in the Chinese economy can be explained by the fact, that there was a hard peg of the RMB (yuan) against US$. US-based rather profitable for Chinese exporters rate. |
| End of XX century | Development of information technology became an important sector of the economy. FDI is used mainly in industry. In 1999, the share of FDI in the manufacturing industry accounted for 56.06%, and increased for 69.03% in 2003. |

| | |
|---|---|
| Till 2000 | There were encouraged investment in 170 industries, including agriculture, energy, development of protection and conservation of the environment, mining, infrastructure, construction and repair of roads, airports, telecommunications. Government welcomed and created incentives for companies, which invested in high-tech industries and tended to increase profitability, improve product quality and increase exports. |
| 2001 | China joined the WTO, it has led to the creation of the «Regulations of the PRC on the regulation of the sector to attract foreign investment.» This meant an increase in foreign investors' access to the national economy, reduced the number of branches inaccessible to foreign investors. After that, it became possible to invest in the city communications, gas, water and heat. The ban remained in air traffic, the MIC, the media, the industry related to national economic security, communications, film and video. Especially a priority for investors announced the development of natural resources, renewable resources, technical re-equipment and the use of modern developments in traditional industries. |
| **III stage. 2001–2008** | Growth of inflows of FDI. At the end of 2001, China was admitted to the WTO with the status of «emerging economy». The process of accession to the WTO has demanded from the PRC significant improvement in the sphere of legal regulation of FDI. |
| **IV stage. Present time** | Capital inflows from countries and regions that use and develop modern technologies (materials, methods of production, development on effective management). The distribution of investments during all the time of reforms has been changing. At the beginning of the main part was invested in the processing industry, after China's WTO accession has also increased investment in the transport system, development of information technology, trade and real estate. |

Sources: [1], [5], [7]–[22]

## Features of reforms for "policy of openness":

1. The transition to a market economy, the positive dynamics of attachment soothe investors so that they continue to invest in China's economy [1].
2. The establishment of political stability [1].
3. During reforms there were created Specifics of taxation (profits earned outside China are not taxed), facilitating financial transactions, procedure of getting credit, protection of intellectual property, the system of patenting and licensing inventions investors [1], [3].
4. Socialist reforms and economic growth has led to the fact that the standard of living has improved. The population will have more purchasing power, it is also good for the domestic real market [1], [3].
5. One of the main features of the Chinese economic model — a large number of workers. And if you compare wages in Europe and in China, in the second case wages less. This allows companies from the same European organize production with lower labor costs, it reduces the cost of production, which allows goods from China to win over other

products in terms of price competition. The demand for Chinese goods allows to increase exports [1].

6. Inflows of foreign capital stimulates the state to carry out measures which make investments in China profitable and safe. China is involved in many unions and associations [1], [3].
7. Simple procedure for drawing up documents, loans. Such an attitude from State toward potential investors, is captivating and makes the climate in the country stable and attractive for foreign investors. Creating favorable conditions for doing business, the Chinese government has complied with its own plan, which guaranteed a leap in development. For companies with a majority stake owned by foreign companies, it is necessary that one of the conditions: the use of advanced technologies in production and manufacture products that are competitive on the world market (to increase the volume of exports) [1].

## Conclusion

Dynamics of growth of FDI inflows can be divided according to the above mentioned stages. The graph shows us a sharp upward trand during the third stage since 2001 till 2008. The fourth stage — present time is the period of Market growth.

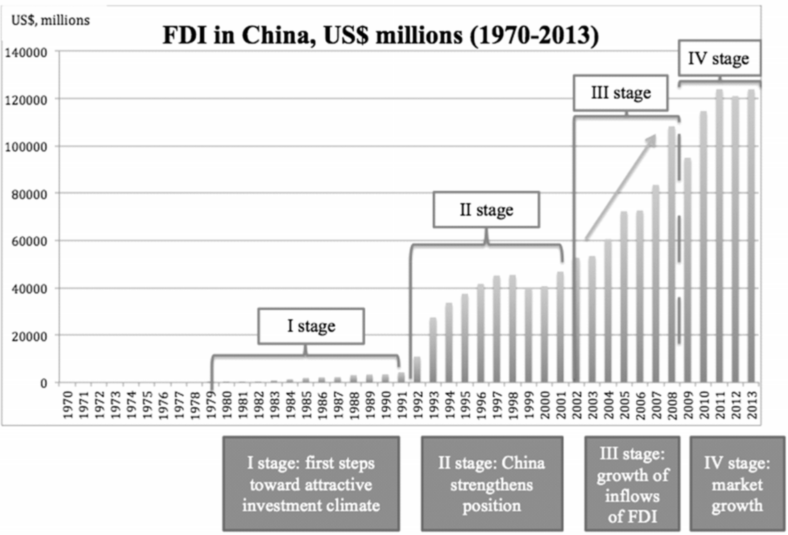


***Figure 2.*** Dynamicsof FDI inflowsinChina
Createdbytheauthoronthebasisoftime-lineanalysisand [25]

Now let us examine correlation of FDI and GDP. We can see significant growth of GDP at the same time with increase of FDI — third and fourth stages.

The greater the amount of foreign capital that enters the economy, the greater the volume of foreign trade activity of the country.

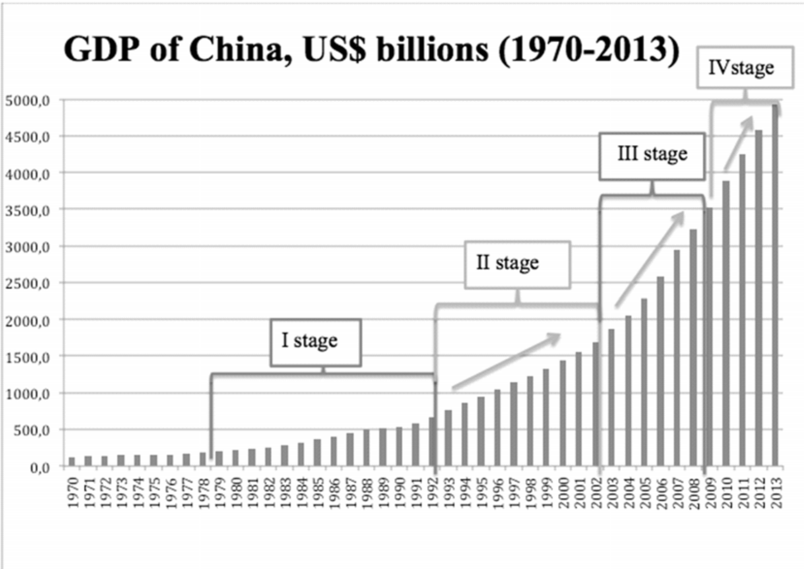


***Figure 3.*** Correlationof FDI and GDP ofChina
Created by the author on the basis of time-line analysis and [25]

This brings us to basic ingredients of FDI effect on national economy. Human resources improved because of investor's influence and foreign experience. Moreover, FDI introduced new technologies in enterprises. All of these assure prospects for economic growth

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# MODERN ASPECTS OF MILITARY AND TECHNICAL COOPERATION BETWEEN RUSSIA AND THE ARAB EAST

## Abstract

*In this presentation the basic directions of military and technical cooperation of Russia with certain countries of North Africa and the Middle East are considered. The author analyses prospects of Russia on the arms market of North Africa and the Middle East.*

*On the basis of research the author claims that the military-technical cooperation between Russia and the countries of the Arab world encounters serious difficulties and challenges. Russia needs to adhere to pragmatic approach in this sphere in order to uphold her global interests in the region.*

***Key words:*** *military cooperation, technical cooperation. Russia, Arab world, pragmatic approach*

## Introduction

It is known that the main strategic direction of development in Russia — is its economic growth, and here, the sphere of military and technical cooperation plays an important role, being a considerable source of currency receipts in the federal budget. According to the management of "Rosoboronexport", the cost of a portfolio of orders remains high, despite the western sanctions. Nearly 50 billion dollars from all orders worldwide.

Speaking about the modern situation in the Arab world, it should be noted that for the last decade there were serious shocks in the countries of North Africa and the Middle East, such as: rise in Islamic radicalism and the beginning of global war against terror, foreign invasion into Iraq, military confrontation of Israel with the Arab forces, and the revolutionary process of "the Arab spring" which began in 2011 and became for the region an event of historical value. Cut-throat competition and unforeseen political complications in this region create for military and technical cooperation of Russia high probability of risks [1].

## The Russian-Arab cooperation in particular countries

**Bahrain. Qatar. Kuwait. United Arab Emirates.** To these countries only single deliveries of military equipment were carried out [1]. For example, recently UAE signed the contract with the Tula Instrument Design Bureau for the supply of various types of ammunition [2].

Cooperation with this group of countries in this sphere is doubtful, due to their orientation to the west. On prospect, it is possible to expect that small contracts will be signed, such as repairing of earlier supplied equipment. Why do they buy our military equipment? Perhaps, they want to diversify their own arms.

**Saudi Arabia.** In the summer of 2008 the framework agreement between Russia and Saudi Arabia was signed. Later it was often reported about collaboration over this agreement on purchase of anti-aircraft weapons, Russian helicopters and armored machinery for the sum more than 4 billion dollars. Nevertheless, there is no information on a condition of these negotiations. However, the messages about their folding also weren't received [3].

**Yemen.** In 1998 Russia and Yemen signed the contract, according to which the deliveries of arms were carried out. Also the equipment of the Soviet period was modernized. There was a preliminary arrangement on purchase of the Russian military equipment by Yemen for the sum more than 1 billion dollars [4], but due to events of "the Arab spring" it is impossible to realize these plans.

**Libya.** The situation in Libya is much worse. As armed forces of Libya are equipped up to 90% with technology of the Soviet production, this country can be considered by Russia as the potential customer on its modernization. However, the signing of agreements is difficult, considering the extremely unstable situation in Libya.

**Jordan.** All volume of the Russian export by 2015 amounted to 120 million dollars. It is predicted that till 2016 Russia will be able to keep the positions on the Jordanian arms market [5].

**Algeria.** It is the main partner of Russia. ANDR received large consignments of the Russian military equipment at the beginning of 2000, 2006 and 2010. The closest plans of the Algerian partners include acquirement of two corvettes "Tiger". On more remote prospect (2025–2030) experts consider that Algeria can take a place among buyers of the fighter of the fifth generation [6].

**Iraq.** After invasion into Iraq in 2003 of the international coalition led by the USA, Russia managed to carry out only a few deliveries of helicopters. But in 2012 Russia and Iraq agreed on the purchase of arms for the sum more than 4 billion dollars. And it became the beginning of normalizing relations. For example, in October of 2014 Russia delivered to Iraq the first party of new air defense systems. The Ministry of Defence of Iraq noted that the air defense systems supplied from Russia will help to protect the vital objects from attacks of Islamists.

**Syria.** Syria remains the most important partner of Russia in the Middle East counting on long-term cooperation. Since the end of the 20th century various arms were delivered to Syria. The Soviet equipment was modernized. The volume of the Russian deliveries of arms to Syria from 2008 till 2015 reached about 2 billion dollars, despite a difficult situation in the country.

**Egypt.** History of military and technical cooperation of Russia with Egypt has deep roots. In the 1960–1970th the USSR was the main supplier of arms for the Egyptian army.

Now cooperation with Egypt revives fully. In the middle of February of 2014 Russia and Egypt signed the contract for delivery of arms and military equipment for the total sum more than three billion dollars.

The Egyptian army is seeking to build its own weapons industry and this will be reflected in any joint-ventures between Russia and Egypt. Military exchanges and joint tactical manoeuvres and exercises will become part of further agreements between two countries. All in all, the background for a significant expansion of Russian-Egyptian military cooperation is very good [7].

This is a general picture of Military and technical cooperation of Russia with the Arab countries nowadays.

## Conclusion

The Russian cooperation on the military line with the Arab East will meet serious difficulties and calls because of position of some monarchies on the Syrian question and strong competition with Great Britain, Germany, France and of course the USA. On the slide you can see the table of distribution of supplies in two regions.

Nevertheless, Russia has all opportunities to cope with these calls, but also to strengthen its position. In particular, in Algeria, Egypt, Syria and Iraq. Also some opportunities of cooperation with Jordan and Yemen can be perspective. Maintenance of earlier supplied equipment makes a significant contribution to the total amount of the Russian military export. Therefore it is necessary to increase number of the relevant contracts. Russia under the current circumstances should adhere to pragmatic approach in the sphere of Military and technical cooperation with the Arab countries in order to bring the competition on arms markets into the civilized framework.

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# USAGE, TRANSLATION AND INTERPRETATION OF ECONOMIC TERMS IN JOURNALISTIC PUBLICATIONS

## Abstract

*The article deals with peculiarities of functioning, translating and interpreting economic terms in journalistic publication style. Theoretical issues on term definition and structural classification are given as well as polysemy, monosemy, unicity and universality of economic terms are studied. Examples of determinologisation are presented. Special attention is paid to techniques of translation and interpretation of the economic terms.*

***Key words:*** *determinologisation, emotionality, university, polysemy, techniques of translation*
***JEL codes****: A12*

## Introduction

Day by day people are getting more and more involved in the economic sphere and their dependence on it keeps increasing. This affects not only specialists in economics but also common citizens. “The informational blow-up” which accompanies the scientific-technical revolution finds the corresponding coverage in press the main purpose of which is to inform people about the events taking place and to describe them in detail.

Another proof of the growing interest among non-specialists is the fact that economic terms cease to be used only in a narrow sense and go into common language acquiring new meanings. Thus, the mass media intensify the process of term popularization using them in press. This process is known as determinologisation (i.e. popularization and semantic modification).

Here are several examples of determinologisation.

| A word | An economic term | Meaning in common language |
|---|---|---|
| ***Loan*** | an amount of money that you borrow from a bank | something you borrow or rent for some time |
| ***Credit*** | 1) borrowing, loan<br>2) debt<br>3) sum, amount | 1) belief, trust<br>2) good reputation, esteem, honor<br>3) praise |
| ***economist*** | someone who studies the way in which money and goods are produced and used and the systems of business and trade | someone who is economical |

| | | |
|---|---|---|
| ***bond*** | 1) an official document promising that a government or company will pay back money that it has borrowed,<br>2) a written agreement to do something, that makes you legally responsible for doing it | 1) something that unites two or more people or groups, such as love, or a shared interest or idea<br>2) something that limits your freedom and prevents you from doing what you want |

## Theoretical concept of economic terms

Since an average man obtains information mainly through the work of mass media both Russian and foreign, the problem of economic translation is nowadays very urgent, as only due to the appropriate translation the information can be brought to a reader correctly and in full scope.

First of all, from the linguistic point of view these are economic terms that distinguish the economic journalistic publication style.

What is the term and what are the main difficulties appearing while translating economic terms? According to the definition of a Russian philologist Vladimir Leichik, «a term is a lexical unit of a particular language for special purposes, denoting general (concrete or abstract) theoretical concept of particular special field of knowledge or occupation». [1, 27]

Economic terms used in magazines and newspapers represent a heterogeneous group of terms, but in this article we will concentrate only on actual terms — words and phrases, quasi-terms, unique and universal terms, polysemantic and monosemantic terms.

**Word terms:**

***Income*** — the money that you earn from your work or that you receive from investments, the government (noun)

***monetary*** — relating to money, especially all the money in a particular country (adjective)

***drastically*** — radically, fundamentally (*adverb*)

***monopolize*** — to have complete control over something so that other people cannot share it or take part in it (verb)

In this article we tried to find out what parts of speech more often represent themselves as economic terms. According to the results of the analysis, noun terms are used in newspapers most often (63%), verb terms are the second (9%), adjective terms are the third (7%) and adverb terms are the last (6%). Thus, terms naming things, phenomena and objects provide more meaning than terms describing their features.

**Phrase terms:**

Some economic terms are used to build new terms, for example: a word "*card*", with the definition «a small piece of plastic, especially one given by a bank, used for buying things or obtaining money» can be used as following:

- ***debit card***
- ***card fraud***
- ***credit card debt***

**Quasi-terms** (terms which are not recorded in economic dictionaries, but used as terms in journalistic publication style):

1) easily-translated phrases

***capital spending***

***long-life asset***

***bond interest rate***

1) phrases which translation requires a context

***A-rated bonds*** — bonds which bring great profit

***dividend-yielding stocks*** — securities bringing dividends

***alternative investment strategist*** *— analyst of speculative investment foundation dealing with high-risk operations which are not connected to direct ownership of block of shares.*

The analysis of terms usage showed that word terms (50%) are more often used in newspapers, than quasi-terms (31%) and phrase terms (19%). This happens because the latter two categories are often more difficult for understanding and can be translated ambiguously.

As a rule, during the translation of specialized articles the main emphasis is laid on the accuracy of translation. It is also necessary to draw attention to another important factor — "emotionality" in the course of translation of economic articles.

## Problems occurring during translation

The reader's perception of information depends on right data submission. Thus, in newspapers terms have simultaneously the function of providing information and also of making an impact on the reader. The realization of this function suggests the presence of emotionally charged units. Therefore, terms in journalistic publication style become emotionally colored:

***toxic debt*** (*" Credit card customers would never be paid off and would be faced with a very large reservoir of very toxic debt* ) *means "a big debt"* [4];

***eye-watering rates*** (*" This prompt concerns that more consumers would be forced in to the hands of doorstep lenders and payday loans companies which can have eye-watering rates of up to 3.000 per cent* ) *mean "big fee"* [2];

***bubble crash*** ( *"He also called for sharp rate rises as early as 2004 to try and avert a debt binge leading to a property bubble crash* ) *means the artificial increase of the property prices".* [3]

The above-mentioned examples confirm that economic terms in journalistic publications realize the function of making impact and convincing, influencing the recipient's viewpoint, spurring him into action. This function has peculiar style characteristics: evaluation, expressiveness and emotionality. Thus, getting to newspaper articles terms acquire all these characteristics. The effect produced on a reader depends on the accuracy of translation and presence (or on the contrary neutralizing) the emotional color.

Some difficulties connected with the peculiarities of economic term can arise during the translation of economic articles. Here are some of them.

Dependent on usage sphere there are universal and unique terms. The former are terms used in many different related (scientific) spheres, the latter are used only in one sphere. During translation universal terms cause particular difficulties, as they simultaneously can be used in some other spheres except for economical, for example: juridical, computer, technical, scientific and even medical, combining completely different meanings.

Here are some examples of unique and universal terms:

**Unique terms:**

***bail-out* (*bailout*)** *— an act of giving money to a company, a foreign country, that has very serious financial problems*

***cash flow*** *— the movement of money into and out of business as goods are bought and sold*

***capital gains*** *— profits that you make from selling something, especially property*

**Universal terms:**

***figure*** *— 1) a number 2) a particular amount of money (economics); drawing(Information technologies); geometric shape(mathematics); diagram (science)*

***benefit*** *— 1) allowance, financial aid; 2) profit (economics);3) immunity from jurisdiction (jurisprudence); 4)benefit performance(theatre)*

One more significant problem appearing during translation of economic articles is polysemy in journalistic publication style. It hampers the understanding of the terms and leads to various mistakes and inaccuracies.

**Monosemantic terms:**

***capital gains*** *— profits that you make from selling something, especially property*

***mutual funds*** *— is a form of collective investment constituted under a trust deed*

Polysemantic terms:

***economics*** —1. *the study of how a society organizes its money, trade and industry; 2. the way in which money influences, or is organized within an area of business or society (1. economics (science, subject matter); 2. political economy)*

***fee*** — 1. an amount of money that you pay for professional advice or services 2. an amount of money that you pay to join an organization , or to do something

According to the results of analysis, monosemantic terms can acquire additional meanings during their translation into Russian, while polysemantic terms in English can lose some of their meanings during their translation into Russian thus becoming monosemantic. This should be certainly taken into account during translation.

## Conclusion

Finally, it is necessary to examine the standard techniques used in translating economic terms:

1. Replication (terms are given by means of Russian words and phrases, replicating English words and phrases word for word):

***tax evasion*** — уклонение от уплаты налога

2. Descriptive translation

***Write-off*** *— списанная со счета сумма, возникшая вследствие уценки товара*

3. Translation by means of analogues(in this case one English term can have several analogues in Russian)

***Interest —*** *1*) доля*; 2*) проценты*; 3*) доход.

4. Technique, when English words are inserted in Russian translation

hedge — хеджевый

Summarizing the above-mentioned, it is necessary to say that the quality of translation of journalistic publications containing economic terms depends mainly on solving such problems as term polysemy and university. Furthermore, the saving of emotional coloring can fulfill both the informative and convincing functions. No matter what the part of speech is used, or what the classifications are, the standard techniques of translation such as replication, descriptive translation, translation by means of analogues and technique, when English words are inserted in Russian translation are used. Only in this way it is possible to make a full, accurate translation and give necessary information to a reader, thereby helping him not only to get acquainted with the material, but also to extend the volume of his economic knowledge, what is particularly significant in the period of modern economic developments.

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# STRENGTHS AND OPPORTUNITIES OF KRASNODAR REGION. ATTRACTING INVESTMENTS: THREE PROMISING SECTORS

## Abstract

*Today the Krasnodar Region is one of Russia's most dynamically developing regions, which offers a unique range of investment opportunities in a highly favourable business climate. From the perspective of investment attractiveness, three promising sectors in Krasnodar Region are agriculture, tourism, information technology. Based on SWOT analysis, the article presents possible solutions of investment issues.*

***Keywords:*** *investments, agriculture, tourism, information technology*

Nowadays the region of Krasnodar, in southern Russia, attracts much attention a promising economic area. As a matter of fact, this area has generated some controversy about its own revival which, despite the large funds brought by major events, still late in coming.

Of course, it is hardly possible to present all the points and analyze all the aspects of the region within a short article, but I will try to focus on those which, in my opinion, are the most interesting and thought-provoking ones, which certainly deserve attention, since they would represent very promising investment sectors.

The first promising sector is *agriculture*. Obviously, it is well known that the region of Krasnodar is the biggest Russian provider of agricultural products. The fierce competition from China, North Africa and South America could probably make us think that agriculture is an industry which may be not so promising any more, or at least not so significant for the future of the region. However, it is precisely this competition that should ensure that efforts should focus on quality rather than maintain a set speed on production quantity. From a quality system, it would certainly be possible to generate more income and would also increase exports of high-level, without even mentioning how this new supply curve of a high standard would go to intercept the new growing desire to rediscover their culinary traditions and food, obviously closely related with agriculture. A great example of a great product that can arise from quality agriculture is definitely the wine production. An increase of an already good quality could break the barriers for this unknown jewel.

Why to invest in quality agriculture? Because there is high demand in food quality, health and safety.

How to attract? Incentives, micro-credit for SME, encouraging qualifying products agriculture are the important methods, to name but a few.

The second promising sector is *tourism*. In general terms, the spatial distribution of tourism in Russia is very uneven. While the role of tourism in the economy of Russia is insignificant, there are few regions that are dependent on tourism. The Krasnodar Region boasts unique recreational and natural therapeutic resources 1,000 kilometers of beaches, snow-covered mountain tops, and forest reserves, to unique natural landmarks, and historical, architectural and archaeological monuments. A mixture of health resort facilities, hotels, specialized and individual accommodation facilities, travel agencies and sightseeing firms, infrastructure facilities, and places of interest. The unique for Russia natural resources and physical conditions of the region, availability of the leading medical establishments and technologies, cultural and historical places of interest create a potential for development of a highly effective, competitive tourist and recreational complex of an international level, building a positive image of the country at the international arena and providing the growing needs of the population in the services connected with leisure and recreation, health and medical treatment, travel and tourism. Regional administration has to be aware that a tourism industry based mainly on domestic flows is not convenient for the exploitation of the full economical potential. As far as the promotion, communication and marketing are concerned, the region faces a lot of weaknesses. For example, it is curious how, from the two main regional airports (Sochi and Krasnodar), only three flights directly go outside Russia and only one of them — to Vienna, Western Europe. Plenty of other examples could be pointed out, such as very little information about the area in question is available in foreign languages or the region promotion outside the Russian borders is very weak. In promoting investment in the Krasnodar Region's tourism industry, the strategic goal is to create a modern, highly effective and competitive health resort and tourism sector that can meet the needs of Russian and international tourists for a variety of services.

Why to invest in tourism in Krasnodar? What you need is the return on investment, as far as the tourism is concerned.

How to attract investments in tourism? Just make it brighter, catchy and shining. Focus on enhancement and improvement of the infostructures, as well as transportations which are absolutely needed, especially for business travelers.

The third promising sector is *information technology*. Considering the excessive bureaucracy and the over-distance between the administration and the citizen / enterprise is a big impediment in attracting investment. Creating a more direct and faster telematic line, without having to follow-ending process in dozens of different offices, will be a magnet for new companies wishing to start new businesses. Information system development projects covering all aspects of life in the region are being implemented within the framework of specialized regional programs. These include:

- a single electronic document flow system for the Krasnodar Region Administration and municipal authorities;
- a video conference system;
- a system for planning and monitoring the social and economic development of the Krasnodar Region;
- a data collection and processing center for the remote surveying of agricultural lands;
- an integrated system called Health Care Management and a medical television network for the region's health care facilities;
- digitalizing archives and library collections;
- a comprehensive public safety system;
- creating an "Open Government" system in the Krasnodar Region.

I decided to insert the field of information technology among the most important sectors requiring investments because surely an effective informatization, especially in public administration, both internally and externally, would open the door to several new realities and above all would prepare a base for efficient management of this region, which is essential to be competitive in the future.

This was a brief glance of all the opportunities exploitable in the region, of course, if we had to really investigate what are all the economic aspects of this region we could talk and talk for hours. But I hope I have provided the points of reflection from which to start, even just to quantify the potential of this region. Obviously, there are much more business areas in Krasnodar Region worth considering and promoting, I just highlighted three of such areas I find most promising in this region. The successful examples that could be made are countless. However, as many Krasnodar's winemakers admitted in the latest wine-fair, the poor image of Russian destinations abroad remains the greatest obstacle to the expansion of the business. In a few words, a newer and better marketing and communication strategy would have a rejuvenating effect over this outstanding region, a region with the full potential for being at least at the top of Eastern Europe tourist destinations rankings.

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# PROSPECTS OF NON-OIL EXPORT DEVELOPMENT IN THE ECONOMY OF RUSSIA

## Abstract

*One of the main problems in Russian economy is that the volume of non-oil products for export is not big enough. In our opinion, high-tech export is the main factor for effective economic development. It will allow Russian economy to be involved in the world market as an active player but not as a recipient of foreign technologies. It will demonstrate diversified character of national economy. Introducing of non-oil export will help to overcome an economic crisis. This type of export proves that there is a sector of technological specialization in national economy, and at the same time it manifests its integration into the system of global technological correlation and demonstrates diversified character of national economy. Introducing of non-oil export will benefit for the development of Russian economy.*

***Key words:*** *non-oil products, export development, world market, technological specialization, Russia*

The Prime Minister of the Russian Federation Dmitry Medvedev, delivering a speech at "Gaidar Forum 2015", said that the economic model based on oil and raw materials should be changed. He emphasized that even the best macroeconomic system would not be efficient if there were some structural problems. D. Medvedev promised that the state support of non-oil export would be increased. He said, "We have much to offer in the fields of IT, nuclear energy, aircraft construction, rocket space industry and in some others"[1].

Global "innovative race" is not only a competition between innovative systems but also a competition between approaches of financial, informational and organizational support of high-tech technologies. Therefore, a new system of the state support is needed for the development of effective economic system. The state support of high-tech exports involves the development of the conceptual state policy and mechanisms of formation and implementation of new approaches [3].

Dmitry Medvedev said that the country would operate under the National Technology Initiative, which identifies the most promising technological niche. He also said that the government had taken measures to support industry, to sign investment contracts, creating industrial parks like silicon valley in the US created by Industry Support Fund [1].

The conceptual development of this policy is based on the analysis of global trends and dynamics of innovative and technological development. Moving to the sixth level of technological development has an impact on changes in technology market. Western sanctions against Russia revealed the technological dependence of Russia in many sectors of economy. However, it has become clear that Russia depends not only on the developed Western countries participating in the sanctions but also on the Eastern region, on such countries as China and India. The development of export of national high-tech products faces external challenges of global technological and economic character. Therefore, as a threat to the intensification of high-tech exports the vulnerability of the export of primary products can be mentioned. High-tech exports of Russian products must find its place in the global economy in relation to its potential and harmoniously complementing the high-tech world. There is no doubt, such a place is incompatible with the technological backwardness. As a result, the government should take great efforts for the development of the industrial sector of the Russian economy. Such efforts have been taken in recent years in scientific and industrial research and development.

In fact, Russia today is the world's largest exporter of a wide range of high-tech goods and services. If in future unexpectedly Russian oil and gas will not be sold at all, economic disaster will not happen.

In 2014 the fall in oil prices worsened the situation. As a result, there was reduction of growth of gross national product. There was a collapse of the ruble, and as a consequence, the rise in prices. However, the ruble has recently stabilized, in 2015, the Russian economy is showing signs of positive growth (even if it is "miserably low") and the feared credit crunch of February 2015, when Russian companies were scheduled to pay back significant amounts of dollar-denominated debt, never materialized. In fact, trade between the U.S. and Russia is still active, and actually increased by almost 5 percent in 2014, despite the U.S. economic sanctions against Russia [2]. The U.S. policy of isolating Russia on the world stage may end up boomeranging and hitting the very people it was not supposed to impact.

It is not just that economic sanctions against Russia are not having their desired effect. The U.S. policy of isolating Russia on the world stage may end up boomeranging and hitting the very people it was not supposed to impact, multinational companies that have invested in Russia for smaller companies, entrepreneurs, and young Russians who have embraced both globalization and innovation.

It should be noted that only 49.3 billion of Russian exports are really high-tech exports, referring to the 5th and 6th levels of techno-economic development. This includes:

- Heavy engineering
- Shipbuilding
- Aviation
- Optics
- Instruments, scientific equipment
- Machines and tools

- The software (Kaspersky Anti-Virus program, text recognizers, etc)
- Consumer goods

The state pays great attention to the support of high-tech exports. As improvements in public support for high-tech exports can be identified, systemic unity of pre-export and export promotion of technology and high-tech products is of great importance[4]. It includes:

- financial support of exhibition activity;
- compensation arrangements of R & D costs,
- provision of concessional lending,
- organization and financial assistance in various international projects,
- effective mechanisms for customs control of the import and export of equipment.

Financial support should be combined with non-financial support, such as developing a network of sales offices. The Department of Economic Development has created a Committee on economy, science and technology, as well as the Working Group on Innovation, the work of which involves representatives of high-tech companies. Multilateral innovation cooperation has been created for the development of high-tech exports, manifested through international organizations, such as:

- Committee on Industry, Innovation and Entrepreneurship)
- Committee on Science and Technology Policy
- Working Group on Innovation and Technology Policy [5].

It should be mentioned that information portal has been launched (http://www.ved.gov.ru), containing a list of institutions and tools to support foreign trade. Information transparency is of great importance for stimulating high-tech exports.

High-tech export strategy complements the State's sustainable development. National exports, as a criterion for their competitiveness, has to meet current consumer expectations that these technologies can be attributed to environmentally friendly technologies. This especially affects our country exporting nuclear and space technology. Serious work is needed on monitoring the development of the modern market of environmentally friendly technologies.

Formation of modern innovation infrastructure and advancement of high-tech exports, part of the national innovation system and institutional tool for public policy, requires a systematic approach to its legal and organizational support. This involves not only monitoring necessary changes in the existing mechanism of legal regulation of export activities, but also the development of new mechanisms of legal regulation, which also means integration of the best global practices.

Another direction is to analyze the possibilities of high-tech exports to developing countries. There is no doubt, success depends on the optimal balance of price and quality. This trend is the only possible way for the application of export of national technologies. In this regard, a promising direction is research, technological and innovative cooperation between Russia within the framework of the BRICS, including the development of technological exchange[6].

Achieving the goals of the development of Russian high-tech exports provides integration strategies and policies for state companies in the development strategy for economic and technological integration of Russia at global, regional and transcontinental level.

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# REBALANCING CHINA'S ECONOMY

## Abstract

*China's outstanding economic growth has long been fueled by unsustainable investment flow, preferably in coastal provinces, accompanied by soaring budgetary allocations, mainly in long-term infrastructural development. This growth model results in distorted saving and consumption pattern as well as in critically increasing disparity between FDI-attracting coastal provinces and inland backwater, thus jeopardizing national well-being.*

***Key words:*** *China, local government debt, deficit financing, infrastructure investment.*
***JEL codes:*** *R 580, H 100, H 620*

## Introduction

In 2007 Wen Jiabao characterized China's economy as "unsteady, unbalanced, uncoordinated and unsustainable" [20]. Internal imbalances that led China's prime-minister to give such an estimate are widely known and have been carefully scrutinized by major economists and sinologists over the past years. Among them one can identify extremely low share of private consumption expenditure, super-elevated share of investment in GDP, outsized manufacturing sector, increasingly high and likely unsustainable rate of investment in residential property. Nicholas Lardy, an expert on China's economy at the Peterson Institute for International Economics, considers financial repression, appeared in negative average real return on short-term deposits in Chinese banks since 2003 in contrast to 3 per cent real rate during the years 1997-2003, to be the main cause of these imbalances. Negative rates result in depressed growth of household income and increased share of after-tax income that goes to savings, leading to lower consumption [6, 1–3].

## Regional disparity

National accounts still being noteworthy however provide no sign of sure disaster or inevitable decline below estimated "around 7%" of GDP growth [1] [5]. Meanwhile the real writing on the wall is local budgets. Graph of GRP growth from 2003 to 2013 (Figure 1) shows explosive growth of GRP of eastern provinces of Central China. The rest of the country either exhibits far slower growth rates or do not grow at all.

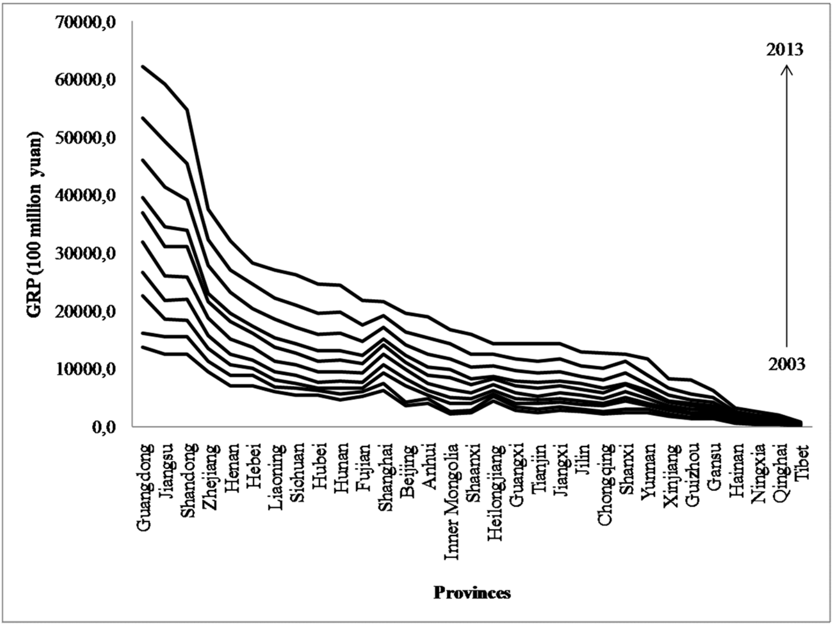


***Figure 1.*** Composition of GRP 2003-2013
Source: China Statistical Yearbook (*Zhongguo Tongji Nianian*), various years [7-17]; author's calculations

Funding of capital intensive infrastructural and other projects, which comprise basis for GRP growth, was provided through government expenditure, loans from development banks and direct foreign investment. Statistical consolidation of the latter two elements is practically impossible due to the limited accessibile data. Available data suggest that during the sample period under review provinces of the Central and Western China implemented policy of increased budget expenditures to boost GRP (Figure 2).

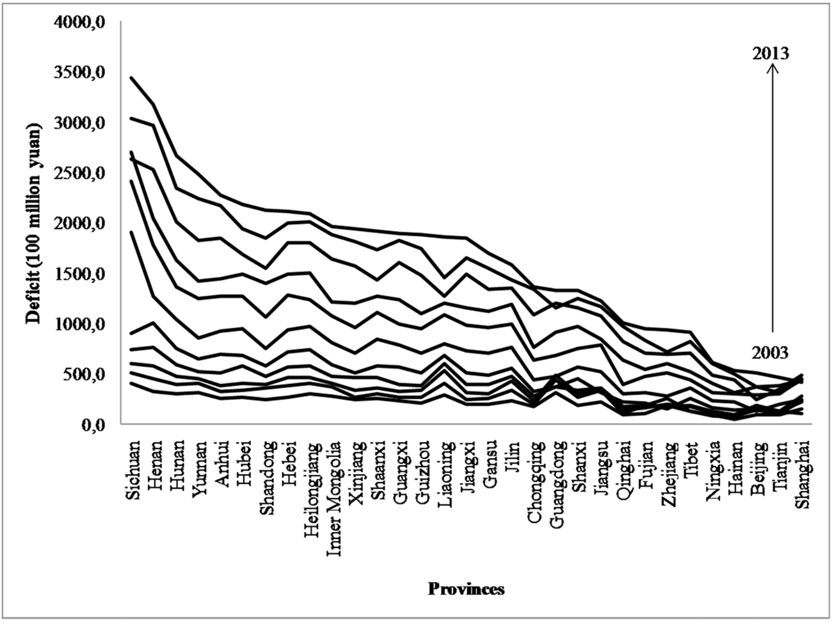


***Figure 2.*** Composition of local government deficits 2003–2013
Source: China Statistical Yearbook (*Zhongguo Tongji Nianian*), various years, [7-17]; author's calculations

Figure 3 (polynomial trend lines were drawn employing OLS method) clearly shows: over the sample period the development gap between provinces increases rapidly. It may be characterized by deviation from trend of Zhejiang, Henan, Hebei, Liaoning, Sichuan, Hubei provinces (Table 1).

*Table 1*

**Regional development gap**

| | China | | (Zhejiang, Henan, Hebei, Liaoning, Sichuan, Hubei provinces) | |
|---|---|---|---|---|
| Year | Standart deviation (GRP), 100 mn yuan | Median absolute deviation (GRP), 100 mn yuan | Standart deviation (GRP), 100 mn yuan | Median absolute deviation (GRP), 100 mn yuan |
| 2003 | 3588,6 | 1808,3 | 2730,0 | 3695,1 |
| 2008 | 8938,4 | 4131,2 | 5880,0 | 6525,9 |
| 2013 | 15597,4 | 8038,4 | 10007,1 | 11644,3 |

Source: China Statistical Yearbook (*Zhongguo Tongji Nianian*), various years, [7-17]; author's calculations

Coastal provinces become more increasingly detached from major regions of the country. Available statistical data enable us to distinguish three groups of territories on the basis of GRP (PPP) per capita [3]: 1) rapidly growing eastern and coastal provinces with GRP per capita comparable with ones of developed countries; 2) Central China provinces with GRP exceeding most of developing countries; 3) backward provinces of Western China.

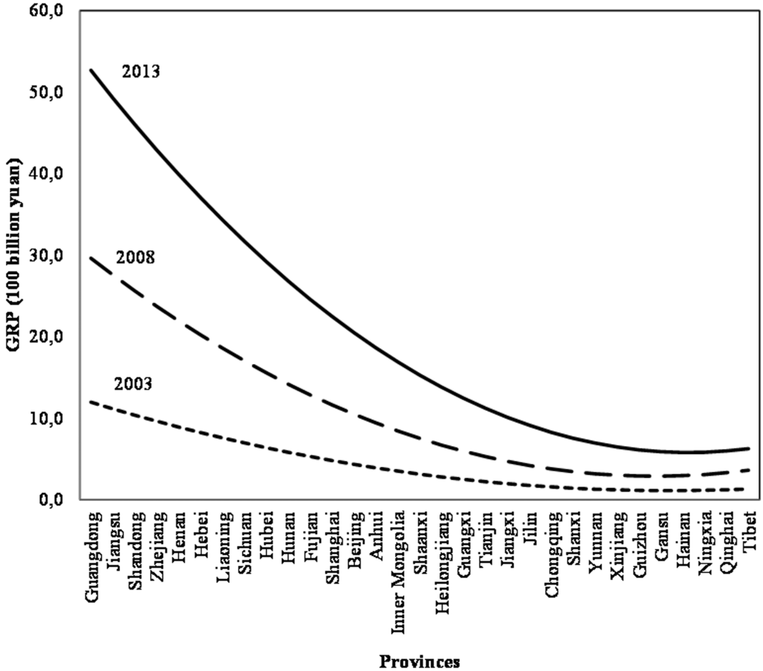


***Figure 3.*** Composition of GRP trends 2003–2013
Source: China Statistical Yearbook (*Zhongguo Tongji Nianian*), various years, [7-17]; author's calculations

Comparison of Figure 1 and Figure 4 shows that model of deficit financing was not equally successfully implemented all across the country. Coastal provinces possess a substantial advantage over inland regions of China by having access to direct foreign investment and national private investments. Most of the inland provinces are bound principally to budgetary allocations and debt buildup for economic growth fuelling. Such practice enforces disequilibrium of national fiscal system and lead to further deepening of regional disparities in socio-economic development. Figure 4 suggests that superior GRP growth with comparable levels of fiscal deficit is plausible only under combination of budgetary allocations along with private (national and foreign) direct investments.

For instance, western provinces exhibit almost no growth despite ever-growing local government debt (Gansu, Hainan, Ningxia, Qinghai provinces, and Tibet). Another group of "poor provinces" may be distinguished by peculiar combination of growth rates below the national average and significant volatility of budget allocations (Henan, Hebei, Liaoning, Sichuan provinces).

Partly, such outcomes can be attributed to low efficiency of public investment major share, for example, in transport infrastructure [18]. Likewise, Construction of "engineering miracle" of Qinghai-Tibet railway did not however become a catalyst for economic growth yet [20].

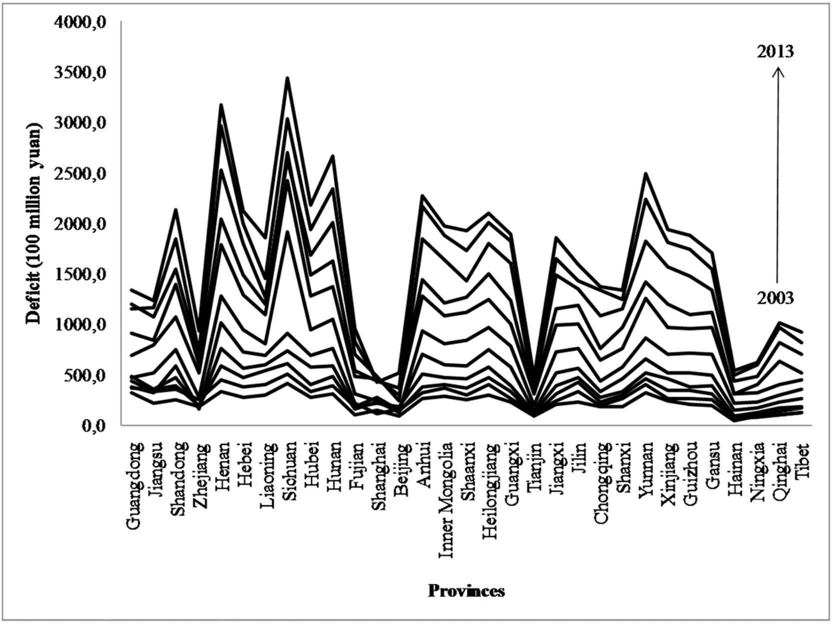


***Figure 4.*** Composition of local government deficit 2003-2013 (provinces ranged by GRP) Source: China Statistical Yearbook (*Zhongguo Tongji Nianian*), various years, [7–17]; author's calculations

Drawn trend lines on the chart of local government deficit (Figure 5) also emphasize exponential nature of provincial economics development gap caused by increasing Central and Eastern provinces' dependence not on private investment or "third-party" financing but on budgetary allocations (Shaanxi, Guangxi, Guizhou, Liaoning, Jiangxi, Gansu, Jilin, Chongqing, provinces).

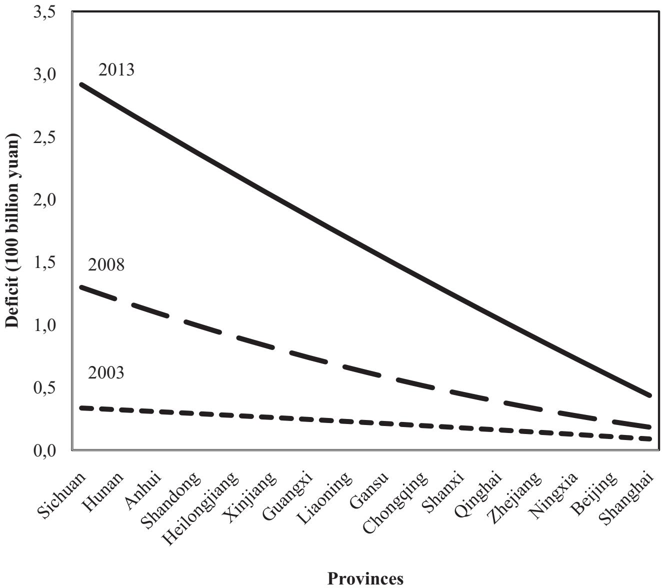


***Figure 5.*** Composition of local government deficit trends 2003–2013
Source: China Statistical Yearbook (*Zhongguo Tongji Nianian*), various years, [7–17]; author's calculations

## Conclusion

Deng Xiaoping proclaimed an idea of "wave-like" development, implied that economic growth of maritime "belt" accompanied by attraction of foreign capital after achieving initial high level of prosperity will transmit, in turn, growth stimuli inland, involving less developed regions of the country into rapid growth [2, 235–236].

Consequent transference of growth areas to less developed regions was intended to trigger transition from unstable export-oriented and investment-driven (mainly by public and direct foreign investment) economy to more sustainable model relying on domestic consumption. However dynamics of GRP and local government debt growth over the past 10 years indicates that anticipated growth drivers do not cope with their role. Disparity between provinces is widening. This development gap poses high level threat on prospective well-being of the nation through disruption of domestic stability, distortion of labor market and erosive effect on financial system [4, 1–2].

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# THE ROLE OF THE SOCIAL MEDIA IN THE FUTURE CAREER BUILDING

## Abstract

*The paper presents a refined analysis of a new human resource management technique and its application to the Russian labor market. The investigation focuses on the peculiarities of the current Russian market situation and advantages of social media approach in the process of effective recruitment. The author provides the guidelines for HR managers to evaluate the applicants from alternative perspective. The article will be of interest for HRM students and also recruiters to select perfect candidates.*

***Key words:*** *human resource management technique, Russian labor market, social media approach, recruitment.*
***JEL codes:*** *L 820, O 150.*

## Introduction

The spread of the Internet has revolutionized the way, in which individuals can communicate with one another and with organizations on a work-related issues. Over the past ten years social media tools and social networking sites have tremendously evolved not only as effective link methods but also have became principal elements for career success. Originally these aims were used as simple communication channels. Rapid Internet development, on the one hand, and unstable labor market situation, on the other hand, led first to the emergence of professional social networks, and then to their use for labor-market assessment. Now employers should actively participate in the e-recruitment market to find better quality candidates and improve hiring decisions, all in less time and at lower cost. Thus the Internet has drastically changed the entire process of recruitment while social media and social networks appear to be the key elements in the job research process. Thus, the question arises: How to measure the impact of the social media for a career success for both: candidates and recruiters?

## The Internet and Social media revolution in the recruitment process

Facing a problem of personnel recruitment there use a great variety of instruments to search the employees. These instruments can be traditional (direct or indirect) or new media ones. It can be search in company's own database through potential candidates, online and print media, direct search, search through the recommendations, the appeal to the recruitment agency, acquaintance at the fairs, work with the higher education institutions, the address on public service of employment, the subway advertisement and in other public means transport: at stops, in trains of suburban trains, etc. E-recruitment, where employers use the Internet in some form to facilitate conventional recruitment processes, has a number of important advantages compared to the common forms of recruiting, according to Smith and Rupp [2, 61–74]. Social media is a broad category, encompassing practices such as blogging, twittering, text messaging, podcasting, Internet videos, and HR e-mail marketing, which are some of the most widespread approaches used in recruitment [1, 51–59]. In addition to these tools, there are a number of highly popular sites, which employers use more and more. They are Facebook, Twitter, LinkedIn, and Google+.

## The benefits of the social media for candidates and recruiters

There is a wide range of benefits associated with using social media in recruitment. First of all, as social media is a complex tool providing employers with the opportunity to hire employees both locally and globally, significantly opens up opportunities beyond traditional staff recruitment. Second of all, it can help to reduce company's recruiting costs much. Organizations may decide to post job openings on their own website, which is very cost-efficient for small and medium sized companies. Moreover, such an approach allows employers to get information about the candidates in addition to a resume, cover letter, or interview. At the same time job seekers to learn about companies they are interested in, connect future candidates with current and former employees and inform about job vacancies instantaneously, among other things [3].

The recent international studies provide evidence about the role of social media in the recruitment Process. In 2014 CareerBuilding.com (the global leader in human capital solutions) asked 2,303 hiring managers and human resource professionals whether they use social media in their hiring process and if yes, than how and why incorporate it into their hiring process. First they found that 37% of employers use social networks to screen potential job candidates. That means that about two in five companies browse a future worker social media profiles to evaluate applicant's character and personality–and some even base their hiring decision on what they find [4]. CareerBuilder also asked employers why they use social networks to retrieve information about candidates, and 65% said they use it to see if the job seeker presents himself or herself professionally. About half of the employers (51%) want to know if the candidate is a good fit for the company's culture, and the other 45% want to learn more about his or her qualification background, skills and working experience. The interesting fact is that managers are not just screening candidates to find some unpleasant facts about them but they are also looking for the information that could possibly be advantageous for the applicants. The CareerBuilder survey revealed that 29% of surveyed hiring managers found something positive in a profile that drove them to offer the candidate a job [5].In Russia recruiters began to use social media for the solution of personnel tasks only in 2006–2007 (in the world — slightly earlier). Social networks such as Facebook, Twitter, LinkedIn, Google + and the local ones including Vk.com, e-xecutive.ru, Livejournal, Odnoklassniki have become widely used among domestic recruiters. One of the recent research on popularity of social networks among human resources managers was carried out by a portal on employment www.hh.ru in September, 2012 while 500 HR specialists were interviewed. The majority of them (57%) admitted that they resorted to the search of the personnel through social networks.

Nevertheless, in the world practise, the share of those who don't consider social networks as one of methods to screen employees, is still substantial — 43%. Generally it might be beacuse HR managers have already enough conventional recruiting technologies. This fact is confirmed by results of the research: 61% of HR managers are quite satisfied with traditional methods of search and so don't see the need in social networks as an additional tool of recruitment. HR managers apply social media in recruitment guided by by company-specific characteristics. For exmaple, 10% of employers refused recruiting through social networks since most of candidates in social networks don't meet the requirements of their vacancy (mainlyit is the companies working in the field of medicine and construction).

As one would expect, most often success in «head hunt» is achieved by those employers who conduct active search of candidates, rsather than wait fora new applicants. Though the number of these managers was divided almost equally: 53% of employers wait for activity from candidates, 47% — actively look for candidate.

From candidates perspective social media can play a crucial role. Under the current economic uncertainties social media have substantially changed the way people find, secure and interview for jobs and. It presents the various forms of user-generated content and a great variety of multimedia tools that are required standards for the successful profiles, that is why it is so crucial to initially determine your strengths and decide how to put it in the best possible light. Nowadays more and more people use social networks to communicate with friends in the everyday conversations or to share some personal experience, however using social media for a professional purpose differs slightly. It is more career-focused, that means that you should pay special attention to the professional content, like simply refining your language or building up your network circles. Network is one of the most valuable assets that you may have. You can be very knowledgeable and skillful labor market player, but the most important thing is that you have those people who know that you know about your knowledge and skill. What is noteworthy is that you may keep the network updated with your positive career or some relevant news that will probably be of interest to your friends and, what is even more essential, to your future employee and, moreover, it actually means that you are open to educate yourself with a plenty of ideas. Think about what forms of contact will give your audience more value. Platforms like Facebook, Vk.com and Twitter let us post our ideas and thoughts worldwide and at any moment, but try not to overload your list of contacts with the inappropriate or better to say not very much business-related content. Some companies even have a policy that forbid to publish any negative posts that may have an impact on company's reputation. Another thing that you as a social media user may benefit from is the ability to connect directly to the organizations that you would love to work for. There are only two things to be done: establish the relationship and make a report. Keep in mind: Be positive, Be proactive, Be career — oriented. Thus, considering all this you may create your own strategic approach how to make your profile career-oriented you're your candidacy «business appealing».

Now, considering benefits from the social media for the employees. Using social networks as a screening tool is an important aspect of employers' social media use to consider. On the one hand, as it was already mentioned earlier, it provides an increased pool of applicants reached, and being able to target recruitment at specific groups of potential candidates, but a at a lower cost. On the other hand, potential employers may have access to detailed information about candidates, which would not be possible by other means. Social media platforms such Facebook, Vk.com, Twitter and LinkedIn play an important role in the general process around recruitment, as it fosters realistic job expectation among potential employees. Through the social media pages, a potential candidate may collect a lot of information about the company to which he wants to apply, its business performance, organizational culture and some other basic assumptions. This can help applicants to make a decision whether they like the general feel of a company. If the answer is not positive, then they can simply choose not to apply and save an organization a lot of time and money. However, even though we see that social media clearly offers particular advantages for both: employer and employee, it still carries certain costs and risks. Recruiters should nevertheless consider the accuracy of online information when making HR decisions and pay serious attention to the fact that using social media in recruitment may put a candidate, who do not have access to or do not use social media, at a serious disadvantage. So, it is crucial to make the competition fair between these two categories.

## Social media trends on the Russian labor market

Analyzing future trends on the Russian labor market, probably the defining characteristic of the role of the social media in the career building is the speed at which it develops. Overall, it is pretty clear, as companies actively experiment with the new social media tools pursuing the goal to increase its brand-awareness and two-way communication with potential candidates. Even though there are some issues related to employee privacy and candidates' equality, social media tools sweepingly pick up steam.

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# RUSSIA IN CONDITIONS OF SANCTIONS: PUTIN LOOKS EAST

## Abstract

*This article is devoted to different development strategies of Russia in the era of sanctions with special attention paid to economic and diplomatic cooperation with China. The author examines advantages, disadvantages and possible threats. This will be of interest to students in Economics as well as government officials.*

***Key words:*** *sanctions, Russia's economic future, China*

## Introduction

Arguments about the threat of economic sanctions gradually subside and seven members of the European Union support the lifting sanctions on Russia. These sanctions have really hurt the main consumers of Russian gas and oil whose economy is dependent on the imports from Russia and on the revenues from the flow of Russian tourists. According to the experts, imposed sanctions have served the good turn to our country because the government is allowed to run weak processes of structural adjustment due to them. But what an impact this situation will have on the country in the measurable future? What is the scenario of Russia's economic future? Whether it will continue focus on the deepening of raw materials specialization? Restructure its economy to a principally new level? Continue adopting inconspicuous changes? Cooperate with the Eastern countries? In this article I would like to give a brief description of each strategy and analyze it as well as concentrate on the economic and political cooperation with the East and China in particular.

The problem is now becoming ever more relevant because of increasing uncertainty in our country, new sanctions against Russia announced by the USA and lack of understanding of the government policy among non-specialists. I will try to explain all these things from the perspective of the future economist.

## Deepening of raw materials specialization

This scenario is extremely beneficial for the West. Major developing countries take up dominant positions in many product markets [1] and Russia is desperate to deepen its raw specialization, increase raw materials in the export structure and reduce government spending and public investment in fixed assets.

According to the experts this scenario remains one of the most possible and I believe that it is the worst course of events, because it is not about development at all.

### Restructuring the economy

This scenario is the most desirable for Russia. Igor Rudensky, Chairman of the State Duma Committee on Economic Policy, affirms that sanctions are a chance for the Russian economy to get rid of the excessive external dependence [2]. Presidential adviser S. Glazyev points out that Russia, which has played a role of the source of raw materials and the buyer of foreign currency is able to change its goals, objectives and tools dramatically under the threat of sanctions [3]. He also offers to move to settlements in rubles at the energy exports and imports and create an internal mechanism of credit to reduce the number of loans made in the foreign markets. These measures are extremely costly and the capital flight from Russia may be \$90–\$100 Billion in 2015[4] while the Russian economy is deprived of essential financial resources. Many experts believe that such a scenario for Russia would be the most beneficial and the only revitalizing, but it requires massive mobilization of available resources and sound policies.

### Economic inactivity strategy

Russian politicians are afraid of making the situation worse adopting ill-considered policy. This scenario is likely to be implemented in Russia because we observe appearance of point solutions only and fundamental decisions are not accepted. For example, giving some preferences to domestic businesses, prohibition for the public authorities to purchase imported equipment etc., but all these measures do not stimulate the economy. Even now fixed capital expenditures are falling that means slowdown in economic growth [5]. Many economists share one view that Russian economy needs profound changes and drastic measures in order not to be left entirely at the periphery of the world.

### Cooperation with the East or dependence on it?

Due to geopolitical position, Russia comes close to the West and to the East at the same time. In these latter days almost everyone talks about the need to turn to the East in order to win a strong supporter. The reasons are quite compelling. It is a geographically close region, and simultaneously a dynamic market with high growth rates which is open to cooperation.

Some of the facts are telling about the priority of Eastern direction. This is a proclamation of the Far East's development as a national priority [6], the revision of the Energy Strategy in favor of increasing cooperation with the countries of the Asia-Pacific region [7], frequent visits in Korea and China, the organization of the first Russian business mission to ASEAN countries.

Let us dwell upon business mission to ASEAN. This event became the first in the history of Russia and was aimed at the cooperation with Indonesia, Malaysia and Singapore. The main advantage of the trade is a high share of exports of machinery and equipment. But at the same time, the geographical distance, different set of mind, the low level of investment cooperation suggests that this market in the coming years will not affect the balance of forces. The economy will remain raw material. If we do not want the transformation of Russian into the economically and politically weak country we should keep the course on innovative development of Russia and the expansion of the scientific-technical cooperation.

Excessive commitment to the East or more precisely to the Chinese market can really put the country in dependence on China. Already, China imports' rate of growth is 56,1% in 2015 in comparison with 2014 and growth rate of export from China in 2015 is 75,6% [8]. Theoretically, Russia should expand exports to China, and not turn into a consumer of Chinese goods. Now we buy from China high-tech products, machinery and sell fuel and energy resources.

Besides, faced with the challenges of the global economy, the Chinese government announced that it would strive to expand and stimulate home consumption to no longer depend largely on the world situation [9]. It means that China will soon need money itself in order to finance credit provision that in turn will force Chinese to save less and increase consumption.

## Positive aspects of Russian-Chinese cooperation from the experts' point of view and the author's criticism

Chinese experts acknowledge that formally Russia has more to do with Europe in terms of infrastructure, business, market and investment. However, the importance of Asia region is growing and there are some advantages of cooperation with Asia, especially China, which Europe is not able to give to Russia [10]. They point out that China is able to help Russia to move away from the raw model of the economy. I cannot agree with this statement because China is interested in import of raw materials from Russia and there is no sense for China in searching any alternatives to Russian raw material economy. Secondly, they emphasize that the development of high technologies is virtually unavailable for Russia and China is able to provide invaluable assistance because this country is technology intensive. In my opinion, it is true because we import high-tech products from China, but soon we can be dependent on their assistance. Thirdly, they mention that Russia in short supply of finance and China could be a great investor. The development of investment relations will redound to advantage of the both economies. I would find difficulty to quarrel with this statement, but China can require something in return (e.g. turn the blind eye to increasing number of Chinese in the Far East). I strongly believe that military cooperation is one of the greatest advantages because Chinese army is the largest in the world and under current conditions it is a weighty argument.

## Negative aspects of Russian-Chinese cooperation from the experts' point of view and the author's criticism

There is a number of problems and potential negative consequences of the union of Russia and China. First of all, these are Russia's internal problems that can interfere the development of innovative activity. I agree that such problems as a great number of incompetents and underfunding of science thwart progress of our country. The second negative aspect is a bad reputation of Russian investment market and its uncertainty. Undoubtedly, Chinese economy is too strong to suffer from such poor conditions but China is able to dictate terms due to its subprime investment. The third aspect is different religious traditions which are able to complicate regulations. I do not think that religious beliefs are able to impede talks so this aspect is quite controversial.

## Conclusion

The problem of Russia-China relations is very serious and there is a lot to discuss. I have learned a lot of opinions of the various experts, examined Russian and foreign information resources, analyzed financial reports, talked with specialists, made conclusions and submitted to your approval. Taking all the aforesaid into consideration I will venture to affirm that the cooperation with China is beneficial undoubtedly but China will never offer that amount of money which we could get from the USA. China is still a competitor and "too close" neighbor. This country is highly interested in energy supplies from Russia but it is not interested in Russia's strengthening. Finally, we must not forget that, despite the economic growth and the rapid development of technology in China, it remains dependent on the United States in terms of finance and innovation. And the successes achieved by China today are based on the intensive cooperation with the West, primarily the United States. The cooperation between Russia and China is inevitable but it should be just one of the directions of the Russian Federation's foreign policy. Our government must not concentrate all attention on this direction but must try to act in different directions.

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# NEW APPROACH TO MARKETING: FASHION AND BEAUTY BLOGS AS A TOOL OF BOOSTING DEMAND

## Abstract

*In «likes» and «haul» videos fashion and beauty bloggers show what they buy and use with a brief review. The purpose of this report is to show how popular blogs influence the consumer behavior. Even their usual videos contain some sort of advertisement. Through analyzing statistics, Euromonitor reports and monitoring social networks, this research shows correlation between bloggers and consumer trends. The recieved results confirm that bloggers are milch cows for marketologists. The report will be interesting for marketing managers.*

***Key words:*** *Beauty bloggers, fashion bloggers, marketing, promotion, YouTube*

## Introduction

YouTube today is not only a video-sharing website or some sort of social network, it is a place where everyone can express themselves and introduce their talents to the world. If you want to find out how to repair a car or how to do a perfect eyeliner, welcome to an incredible world of YouTube. Over 72 hours of footage is uploading to YouTube every minute.

YouTube itself is a story of a great success. It was founded by three friends almost ten years ago. According to the story, which is provided by social media, Chad Hurley, Steve Chen and Jawed Karim decided to make their own video-sharing website after a dinner, because they had problems with sharing content which had been shot at this party. We do not know if it is a hundred percent true, but this fact reflects the idea that all great ideas come unexpectedly.

Almost every YouTube blogger has the same story of success. Such top ones as PewDiePie (over 35500 million subscribers), Jenna Marbles (over 14800 million subscribers) or Michelle Phan (over 7500 million subscribers) have started their channels just for fun. And playing videogames on camera brings almost 2 million pound annual earnings for PewDiePie. L'Oreal launched a new cosmetic line called «em» by Michelle Phan. That's pretty amazing for a hobby, is not it?

According to the «Variaty» survey, which was carried out in July, 2014, the most popular people among American teenagers are YouTube bloggers. Just imagine: 19-years old beauty and fashion blogger Bethany Mota is more popular than Leonardo DiCaprio [6].

In this report I want to focus on beauty and fashion bloggers, because they are the most attractive ones for brands' promotion. You may ask why. So, let's find it out.

## Beauty and fashion bloggers and their target audience

The answer is that this kind of bloggers talks about cosmetics and clothes and their target audience are women from 13 to 34 years. Or the female part of «generation Z» and «generation Y». These ladies have at least an account in one social network. That means they share their life with their friends by posting photos almost every week, so they want to be attractive on them. This is proved by Eurononitor research [2] where it is said that popular brands often create special beauty or fashion flashmobs in social netwotks. For example, Dior launched a «Selfie-beauty» campaign: women could post their minimum-makeup photos to show their natural beauty using a special hashtag. But many of the participants are not confident with their appearance without any makeup. They prefer to use foundation, mascara and nude eyeshadow to feel more comfortable. But where can they find the best products? Who can tell women about their magical effects honestly, not like consultants in shops? And how to do a perfect makeup? The answer is YouTube bloggers.

As 24-years old blogger TomSka said, «There are people who are obsessed with youtubers. They can say «This is the lipstick I use». And their admirers would go and buy it. Brands know this». He is absolutely right.

## The story of making money

The main secret of beauty and fashion bloggers is that they act like your sisters or your close friends, so you trust them and listen to their opinion about stuff like clothes and cosmetics. And you want to buy, for example, shoes just because your favorite blogger owns them.

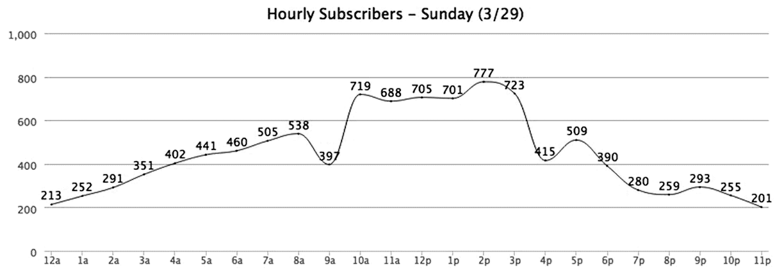
YouTube celebrities usually talk about the stuff they really enjoyed during a month or longer («Likes» video) or about something they bought a day before the video («Haul» video). But don't forget that they are people of working age who does not have a classical job with a monthly salary. They make money from YouTube partner program, but collaboration with brands brings bigger earnings.

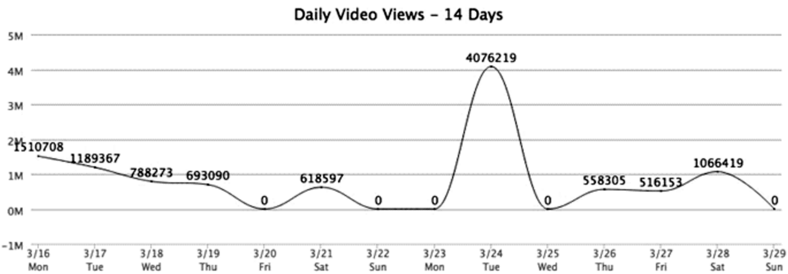
According to «The Guardian», «American reports have claimed that beauty vloggers (a term for bloggers on YouTube) can make $5 million a year, earning $10000 to $15000 per product placement...Fees appear to vary wildly — an original video or a collaboration can vary from £500 to £20000, with many of the deals running through a company called Style Haul, a network that monetises all the beauty channels. «The brands' interest depends a lot on the tone of the person», the insider says. «But beauty is a really attractive industry online, because it's a purchase that's easy to make. A video of a girl applying eyeliner in her room directly translates into sales for a brand like Topshop» [5].

«I do have sponsorship with brands, but I would say it's probably only 10%, because my audience is interested in my honest opinion. You know, is this mascara really good or you've been paid to say this? I'm going to talk about a product only when I really would like to recommend it», said Zoella in «The Creators» video. But let's have a look on the statistics of her channel.

## An ordinary beauty and fashion YouTube blog: Zoella

According to Cision's blog ranking, Zoella is number one UK beauty and fashion blogger [1]. She has 7,717,677 (31 March) subscribers.



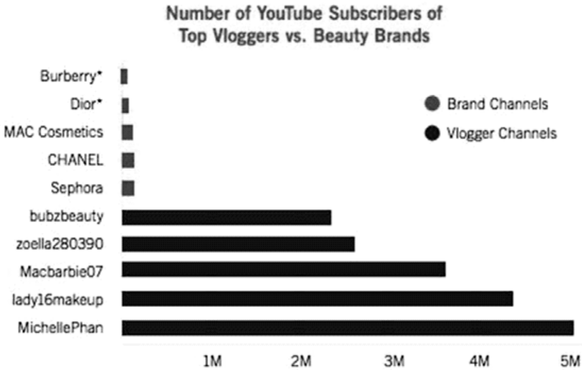

As you can see from the graphs [7], almost every hour more than 200 people subscribe to her channel. The average amount of her videos views is 679,030 in the period from 16.03.2015 to 29.03.2015. That means that almost 700 thousand people would see the advertisement of a product made by Zoella.

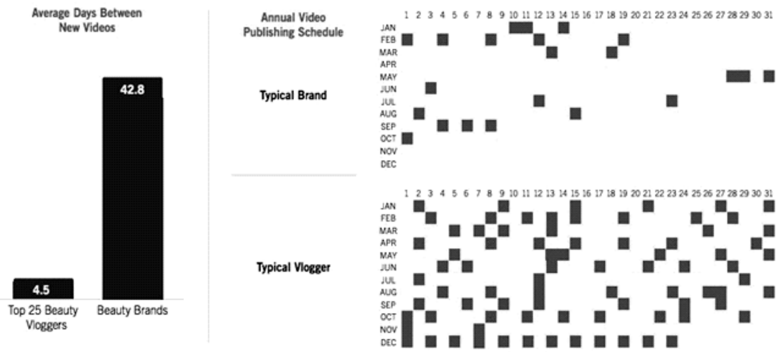
## Foreign bloggers and the Advertising Standards Authority

According to the Advertising Standards Authority, bloggers must clearly tell their fans when they are paid by advertisers. There should be an information about if the video is sponsored or not in the description of the video. So the viewers can think about «to buy or not to buy» problem in terms of if the video is just a promotion or a real opinion.

## Brand channels vs. Vloggers

To speak generally, according to the statistics [4], in 2013, beauty-related content generated more than 700 million views per month. Popular types of YouTube beauty content include tutorials and Do-It-Yourself videos, reviews, haul videos and videos produced by beauty vloggers. In January 2013, more than 27,000 beauty videos were published on the online video platform.




The graphs [3,15] above show that Brand channels are far less subscribed than ordinary vloggers channels. That is a proof that for brands it’s more beneficial to pay bloggers for the promotion instead of developing their own channels, because it costs less to pay a blogger for promotion than to create an expensive advertisement with Hollywood stars every week, that’s why the annual amount of videos is higher among bloggers, not brands’ channels.

## Fashion world in blogging

Let’s move to the clothes promotion. The situation is almost the same, but there are several features. There is no doubt that price range among the clothes, shoes and accessories is wider than among cosmetics. Luxury cosmetics is more affordable than, for example, Chanel bag. That's why Lancôme did a collaboration with Michelle Phan, but there is no collaboration with Louis Vuitton.

So different collaborations with bloggers are made by online stores, which sell rather cheap clothes. For example, CutiePieMarzia (over 5 million subscribers) made an advertisement video for boohoo.com (an average dress costs 20 pounds) and dresslink.com (the average price for a clothing item is less than 10 dollars). She was paid to show these items (websites are not only paid for the video, but they also sent her some clothes for free), but it's interesting that she grades every item she gets. So the blouse which costed 6,89 dollars got 5,5/10 because of the quality.

Some sites do not pay for the advertisement directly, but such sites as asos.com and chictopia.com have a loyalty programs for fashion bloggers: if they show the clothes from the site in videos or post looks in social networks, they can have a special discount for them. That is a less costly but an effective method of promotion.

## Does it really work?

The question is bound to arise: does the promotion by collaborating with bloggers really work? The answer is obvious: of course, because if it was not, brands would stop collaborating with bloggers.

A brilliant example is CutiePieMarzia and her collaboration with Memebox1. She created 4 Memeboxes and each of them was sold out less than in a week.

It is also important to mention that beauty and fashion bloggers have an impact on consumer trends. The proof can be found in the comments (lots of people write that their favourite blogger influences their style and they try to be like them by buying the same clothes and cosmetics) and in the period in which the clothing item was sold out after the date of posting video. An example is Sonya Esman (over 1 million subscribers) and her orange dress from asos.com. I saw it a month before her video and there were all the sizes, from uk4 to uk14. Nobody wanted to buy it, but after the video it was sold out in two days. It seems to be bizzare.

But at the same time it is difficult to define if bloggers create or just support popular trends. In my personal opinion, bloggers combine both. Without their support a lot of trends would not be so widespread.

## Beauty and fashion bloggers in Russia

Now let's have a look on Russian bloggers. YouTube in Russia develops rapidly and more and more people want to become famous. There are few

[1] A box with Korean cosmetics, every month there appears a new box

bloggers who have been making videos for more than 2 years: Kate Clapp (started as a life-blogger, but now it's difficult to define only one field of activity), Maria Way (beauty blogger), Sonya Esman (fashion blogger). Each of them has more than 1 million subscribers.

But Russian YouTube has one interesting characteristic: bloggers do not have to tell if they were paid to show different products. When you watch Russian YouTube, you feel like you watch a commercial. Our bloggers do not work for an idea like foreign ones, but they want to earn more today. It is a great problem, because people begin to criticize bloggers for their desire to make more money. Almost every video of a Russian beauty and fashion blogger contains an ad (in her last video Maria Way told about her collaboration with «Fairy» which is perfect for your hands). From my point of view it can be explained by some kind of Russian way of thinking: for example, small business in Russia are focused not on long-term relationship with their partners and consumers, but on short-term earnings.

## Conclusion

So, taking everything in consideration, YouTube bloggers are milch cows for beauty and fashion brands. The cost of a collaboration video is lower than a TV-ad price. And the result would be more effective, because bloggers today have a great power and influence on people, who watch their videos almost every week. A collaboration is more targeted than an ordinary ad, the reason is that you follow a blogger only if he or she is really interesting for you. So the probability that you have the same style in routine life is almost 100%.

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# BUSINESS IN PHARMACEUTICAL INDUSTRY: REGIONAL DIFFERENCES

## Abstract

*Economy is globally unbalanced. This fact is particularly obvious for the pharmaceutical industry. There are different regions in the world that develop not in the same way in this sphere. Sometimes it is not so simple to conquer a new market, because the basic business model is not applicable for all the regions. The article explains the tendencies in the markets of various countries and discrepancy of possible business models.*

***Key words:*** *pharmaceutical industry, multinational business, global pharmaceutical tendencies, regional healthcare differences.*
***JEL codes:*** *F 230, F 290, I 110, I 180*

## Introduction

Pharmaceutical industry is one of the most profitable industries in the world. The average yield of the invested capital is comparatively big, that is why this business area attracts many entrepreneurs. Generally pharmaceutical companies develop, produce, and market drugs or pharmaceuticals licensed for use as medications[5]. There are two main types of medications companies are allowed to make — innovative and generic.Innovative medications are protected by the patent system. Usually companies spend about 1,2 bln dollars for a product — from pre-clinical trials to actual launch including marketing expenses — and about 10–12 years. Other important areas may be presented by medical devices, parapharmaceuticals.

## Major tendencies in pharmaceutical industry

The interesting fact is that, according to Deloitte agency[1], smaller companies tend to be more cost-effective and their return on research & development (from now on — R&D) is higher. Not only smaller companies are more efficient but those covering less therapeutic areas, which are more specialized. Big transnational organizations have followed the "specialization tendency" recently. One may notice enlargement of certain departments in several multi-national corporations. For example, in 2015 there was completed a set of transactions between Novartis and GSK [6] (both of them belong to Big Pharma — top 10 pharmaceutical companies with the highest revenue). Novartis bought an oncology portfolio of GSK and the latter purchased a vaccines department. They also created a joint venture in consumer healthcare area. In the media release dedicated to this event is also said about the focus of Novartis company on three segments: innovative pharmaceuticals, eye care and generics. As an another sound example Novo Nordisk company may be introduced. It is stated on the corporate web-site and in numerous reports that the main objective is to fight diabetes in all forms. Not only the cost-effectiveness is probably high, but in people's minds the organization is presumed specialist in this area. Companies define spheres of influence both to conquer minds and operate more efficiently in the conditions of suppressed competition.

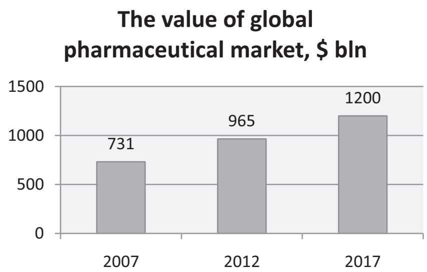
With the course of time business in the pharmaceutical industry becomes more complicated and challenging. The majority of the biggest companies exist for average 100 years. Most of the time the financial model was rather simple. Organizations used patent protection for high margin profits, the revenues were tremendous. The situation has changed dramatically. However the patent protection is still of a great importance the return on investments in R&D is much lower, competition is tougher, marketing is more complicated and various law regulations rapidly evolve. Nowadays one the oft-debated questions lays in the issue of ratio between marketing and R&D costs. Unfortunately, the difference is hardly if possible distinguishable. So earlier the key success factors were qualified representatives and fortunate trials. The attention imposed on these factors is acute, but in many countries government reforms made many representatives' activities prohibited. Now it is very important to maintain flexibility towards the outside world, various law regulations, economic and geographic shifts. The question of generics has also become critical. Principally new medication is not produced. Generics, on the other hand, are sold broadly. They do not require big investments and are affordable for most people.

Some of the world tendencies affecting pharmaceuticals industry should be introduced. HP company defines 6 of them[4]. The first one is demographic shift. Longevity is increasing, the number of kids born decreases in developed countries. This tendency creates a "population bubble". Governments are more affected by the obligation of retirement payments while receive less taxes. The Center for Strategic and International Studies give intriguing statistics: the aging population in the USA is around 15% nowadays — and even higher in Europe and Japan. The second factor is conveyed by rising costs. The third is healthcare reforms. Many countries introduce price regulations (Europe, Russia as examples), different laws being obstacles for foreign companies and other forms of government initiatives. For instance, it is forbidden to base a foreign company in China, organizations often circumvent the rule by M&A mechanism. "M&A" stands for "mergers and acquisitions". Basically if a company wants to conquer a Chinese market it either buys an organization there or merges with one. The fourth factor is clients' empowerment. People in developed countries become more engrossed in the process of choosing the medication and the type of treatment; they browse through the Internet looking for the applicable data. The fifth tendency is extension of social media usage. Both patients and doctor unite in such "nets" exchanging useful information.

The last factor is entrance into genome era — path to individualism. We can already say that specialized medicine is actively developing and it is not nearly the end. Probably in the foreseeable future we will be able to receive personalized treatment which could be very effective.

## Regional differences in pharmaceuticals and healthcare

At this point we have come closely to the main idea of the article. Obviously each country needs its own approach of business model. We can divide all the countries into three categories. These would be developed, pharmerging and emerging markets. USA, Japan, South Korea and Europe comprise developed markets. They are saturated (competition is comparatively high), not rapidly evolving (only the USA market grows steadily), seeking for innovations and specialized medicine. Pharmerging part is composed by those countries which growth is considerable from year to year and have developing government regulation of the sphere. Currently there are 20 of them (China, Russia, Brazil, India, Mexico, Turkey, Venezuela, Poland, Saudi Arabia, Indonesia, Columbia, Thailand, Ukraine, South Africa, Egypt, Romaine, Algeria, Vietnam, Pakistan and Nigeria). The list in its modern version exists since 2013. Emerging markets are not interesting for the direct investments yet for the markets of there are not mature enough to produce revenue for the foreign companies.




Globally pharmaceutical market grows every year. It is easily explained by the population growth. According to the IMS Health forecast the value of global pharmaceutical market will grow from 731 bln dollars in 2007 up to 1200 bln dollars [2] in 2017. The growth of the developing countries is stronger comparing to the developed countries[3, 8–10]. The biggest pharmaceutical market is North America with 45% share of total global sales in 2014, but the most noticeable growth is performed by China — 7,4% in 2014 (7,7 in 2013). The region of China is not unique on the path of growth. Sub-Saharan Africa market's growth was 4,5% in 2014.

There are many price regulations all around the world that affect pharmaceutical companies. For instance, demographic shift causes pressure on the budgets of many European countries, which leads to the shrinking of investments in healthcare. This problem has also touched Japan pricing scheme resulting in 2,7% reduction.

Healthcare systems of the emerging markets vary greatly. Most of them strive to align their regulations with ones that exist in the USA, Europe and Japan. Some countries require local clinical trials for approval (among them are Russia, China, Vietnam etc.). Developing countries also improve their healthcare systems by the expansion of the government-funded health schemes (such as China and India).

The issue of intellectual property is one of the core subjects for pharmaceutical industry. Generally patents last for 20 years. In developed markets the substitution process is smooth-running. Generics take the freed place almost right after the patent expiration date. The scheme is not so well-working in emerging markets, because the competition is not so strong. Some countries (such as Brazil, Argentina or India) implement the idea of medicines availability by restricting the patent practices to weaken the rivalry between companies and to make medication more affordable.

Many countries have peculiarities with distribution system. While in developed countries all the important information could be easily found on the Internet in developing countries feedback is often hampered or deformed. It is one of the main problem in India. Most people live in rural areas (about 70% of 1,2 bln population) and the process of delivery is complicated. GSK company came up with an idea that solved the problem of contacting with the population of the locations that are hard to reach. Today (in 2015) the company covers 20.000 villages directly using sub-distributors or women-representatives depending on the village size [3, 35].

Africa is an ambiguous region. On the one hand, this area is developing, but not strong enough. On the other hand, it has a great potential and definitely cannot be ignored. Many companies prefer to leave the development in this region for a better time or use it to promote themselves in terms of corporate social responsibility. GSK company, in contrast, considers investing in this region as very important and brings into action several activities orienting on the long-term effect. It is going to create the world's first Africa Non-Communicable Diseases Open Lab, to expand existing facilities in Kenya and Nigeria and build new factories in other regions. It will also train 10.000 healthcare workers in three African countries.

## Conclusion

To sum it up, all the regions cannot be evaluated by the same scale. Nevertheless they are affected by the same world tendencies, individual ones also take place. All countries can be divided into three categories in dependence to the development of the pharmaceutical market there. Generally the trends differ in these categories. Not only trends are different, but special aspects of each area. These special aspects may belong to various sides of economic life — from government regulations in intellectual property protection to the complications with feedback receiving. All of them should be kept in mind in order to achieve the company's prosperity.

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# NEUROMARKETING — THE MODERN METHOD OF MANIPULATING CONSUMERS

## Abstract

*Neuromarketing — the modern area of research, which stands at the intersections of two areas: neuroscience and consumer behavior studies. The main characteristics of neuromarketing are presented in details. Various technics of studying a consumer behavior are reviewed in the article, as well as the conclusion of the appropriateness of certain ones. The impact of the neuromarketing on trade is also analyzed. In conclusion the article underlines significance of neuromarketing in the marketing communications.*

***Key words:*** *Neuromarketing, Neuroscience, consumer behavior.*
***JEL codes:*** *M11, M21, M31*

Every day people face different situations when they schould choose one alternative from many. Making daily choices people are guided by their emotional feelings that shift their decisions toward unconsciousness. Thus, understanding how emotions influence our behavior and making choices process is very significant, due to the fact that it will help to predict one's choices in the future. Thanks to Neuroscience, insights to the issue of how brains act are possible.

Research in Neuroscience is a great tool in studying consumer decisions that allows scientists to answer different questions and reduce gaps regarding customer cognitive processes. Investigations relating to the issue provide researchers with information of how consumer decision-making relies on his memory, emotional responses, and attentional engagement as well. Though it is possible to imagine intuitively how emotions and memories influence our choices, mainly it is not easy to understand how one's brain really reacts. Neuroscience does give researchers possibility to determine cognitive abilities which contribute to the decision-making process, particularly to the consumer's one. Using this insightful information, brands have more opportunities to be remembered, effectively capture customer's attention and elicit a positive emotional response.

Therefore, we are moving toward Neuromarketing. It can be defined as the modern area of research, which stands at the intersections of two areas: Neuroscience and consumer behavior studies. Neuromarketing is a new side of marketing research that studies consumers' sensorimotor, cognitive and affective response to marketing stimuli. It is a new step of marketing research and the most effective method of reaching customer intelligence. Therefore, the main aim of Neuromarketing is to understand how consumers behavior is driven by their emotions and, consequently, to predict their purchasing decisions in the future.

Though the notion «Neuromarketing» was coined in 2002, when it was used by the Nobel Prise for Economy winner Ale Smithdts, the term was in use much earlier. Up to 1900's there were a paradigm that firstly people think, secondly they feel and only then act. However, with the beginning of studying how emotions influence our behavior there was created a new paradigm that replaced the old one and that sounds as «Feel-Act-Think».

As it was mentioned above, emotions play a great role in controlling our mood. Nearly 95% of all our choices are made at a subconscious level (Gerald Zaltman). That is why more and more brands today are being positioned to enhance certain feelings. Thus, this powerful concept attracts the attention of business in regard to the issue of the importance of analysing emotions.

The goal of Neuromarketing research is to interpret brain activity and predict consumer preferences. To measure how brain works driven by emotional feelings, scientists use various technologies, such as Functional Magnetic Response Imaging (fMRI), Electroencephalogram (EEG) and Eye Tracking.

**Functional Magnetic Response Imaging (fMRI).** This technology provides researchers with a clear picture of brain areas activity, when human emotions are affected. The concept of the fMRI is quite simple. When people are excited and experience positive feelings, particular brain areas activate and blood flows to them, and as blood has some magnetic properties, the fMRI can pinpoint activated brain areas and inactivated ones. This technology is an invaluable tool for registering such brain areas that control our abilities to remember positive or negative experiences, attentional engagement and emotional responses. Main advantages of the fMRI are 80%[1] accuracy in predicting behaviour, assessment of a wide range of emotions, suitable for different Marketing campaigns and low Marketing risk.

**Electroencephalogram (EEG).** The EEG is another helpful and useful technique for registering brain activity in real time. Work of the EEG method differs from one of the fMRI method: the EEG detects the electrical activity that arises at the brain surface and register various types of brain waves. This waves can be interpreted as an index of interest, excitement and engagement towards a particular experience. The results of the EEG allow to measure how consumer perceive products value and their quality. Marketing risks are also low, especially if combine the EEG with eye tracking.

**Eye tracking** is a technique that captures how eyes move around a visual scene with the help of a small and specialized camera. Regard to this technology, it is possible to investigate how long eyes are focused on a particular spot or how they

[1] https://www.trueimpact.ca/science/research-technologies/

move from one spot to another. Such research gives scientists an opportunity to understand what captures one's eyes, what is attractive for people and what arouses their interest. Eye tracking is easily conducted, but, unfortunately, an extent of behavior predictability, relying on the method, is low.

Apart from this technologies there are others as Steady State Topography (SST), that also studies brain activity, and special sensors measuring physiological state, or biometrics. All this ways of studying human brain and body allow researchers to learn why customers make particular decisions.

Neuromarketing research is expanding rapidly in both academic and business spheres. Big companies aimed at predicting consumer behavior have their own laboratories, scientists and partnerships with academia. For instance, Google, CBS, Frito-Lay, A&E Television and others use Neuromarketing research to understand how people react on their advertising and, consequently, how to attract more consumers.

Microsoft is mining EEG data to understand users' interactions with computers including their feelings of "Surprise, Satisfaction and Frustration."

Google made some conclusions when it coupled with MediaVest on a "biometrics" study to measure the effectiveness of YouTube overlays versus pre-rolls.

Daimler employed fMRI research to inform a campaign featuring car headlights to suggest human faces which tied to the reward center of the brain.

The Weather Channel used EEG, eye-tracking and skin response techniques to measure viewer reactions to three different promotional pitches for a popular series.

Frito-Lay has been studying brains of women to learn how to better appeal to female audience. Findings showed the company should avoid pitches related to "guilt" and guilt-free and play up "healthy" associations.

Besides, Frito-Lay hired in 2008 a Neuromarketing firm to determine how consumers respond to Cheetos. Using EEG technology on a group of willing subjects, the firm found out that consumers respond strongly to the fact that eating Cheetos turns their fingers orange with residual cheese dust. That data in hand, Frito-Lay moved ahead with an ad campaign called "The Orange Underground," featuring a series of 30-second TV commercials in which the Cheetos mascot, Chester Cheetah, encourages consumers to commit various uncommon acts with Cheetos. The Frito-Lay campaign got in 2009 a Grand Ogilvy Award from the Advertising Research Foundation.

In fact, marketers are just beginning to use the possibilities offered by results of different brain and body research when people are involved in seeking, choosing, and buying a product. These research should be continued and developed by companies, due to the fact that marketers can design products and communications to better meet "unmet" market needs, connect and drive consumer desire to buy. For big corporations Neuromarketing is a means to an end goal — sell more stuff.

Taking into consideration that Neuromarketing is a young area of science and marketing, many experts in and out of marketing have raised concerns about the reliability and ethicality of neuromarketing.

Some customers consider that neuromarketers are making them buy unnecessary goods and enjoy useless services and create unhealthy and irresponsible addictions and cravings. What is more, consumers may believe that idea to give advertisers information of human subconsciousness undermines one's privacy.

Next, Neuromarketing still suffers from the issue it is trying to overcome: the artificiality of market research. Brain activity in a lab may not be equivalent to brain behavior in the shopping malls where the buying choices are consummated.

Then, the cost of reasearch conducting today is too expensive and, that is why, they are prohibitive for many companies.

In my view, Neuromarketing, first of all, helps marketers understand how various emotions and feelings influence our choices, and how they should build their marketing campaign to attract more consumers. Nonetheless, thinking that companies control human mind is not wrong, because even if the main goal of corporations, which study brain and body activity under the enfluence of emotions, is to stimulate purchases and increase demand on the products or services, companies, anyway, manipulate consumers buying-decisions by pushing the «pleasure button» of byers.

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# SUSTAINABILITY REPORTING IN UNBALANCED GLOBAL ECONOMY

## Abstract

*This paper examines the role of the sustainability reporting and its features in European countries and in Russia. Using the open sources of the Global Reporting Initiative (GRI) the informationabout the indicators of sustainability report is collected. In particular, the influence on financial indicators of companies by indirect factors such as working condition is measured. Sustainability reporting creates real opportunity for unbalanced economy to diversify risks of companies' performance, reduce costs and improve efficiency.*

***Key words:*** *Sustainability reporting, Global Reporting Initiative, non-financial indicators*
***JEL codes:*** *G10, G20, Q56*

Unbalanced global economy is influenced by such factors as forced and compulsory labor, internal frauds, wasting of energy resources and discrimination of particular groups. Sustainability reporting is a recent development that promotes the principles of fair trading, investing in new technologies and scientific researches.

Pressures of increasing population, overgrazing, overcultivation have a strong influence on the future performance of particular companies. A life cycle of a company that cuts down trees and doesn't care about reforestation can't be considered as long-term and perspective. Eventually, fertile topsoil may be entirely destroyed, leaving only dust, bare rock and no perspectives for doing business and money in the future.

Company should be aware of any possible risks on financial markets. In this case financial reporting provides the company and investors with full information about the rate of liquidity, relations between liabilities and assets and other financial indicators. Financial reporting includes Balance sheet, Income statement, Profits & Losses statement and Cash flow statement. These statements have been proved to be reliable for a really long time until the economy became global and other factors appear to have great influence on the profits and losses of a particular organization.

Business is trying to create strong reputation in order to make investors confident about the future performance and its role in financial markets. Share prices are volatile so that their price could stay at the level of «junk bonds» because of any reported allegation in news according to fundamental analysis.

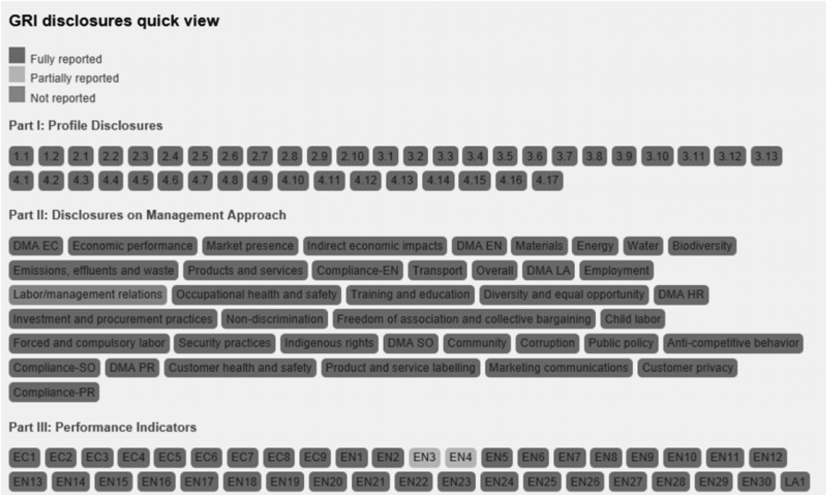
Sustainability report is an obligatory report for companiesin Europe and America that provides potential investors and other users with data and information about performance of particular business. [3] Companies publish a sustainability report that deals with economic, governance, environmental and social impacts caused by its everyday activities. The organization values and governance model are presented in sustainability report. The recent researches demonstrate that companies presented systematic sustainable reporting could lessen the impact of crisis in 2008. The high quality of sustainable report made investors more confident about the future perspectives of a particular firm. A. T. Kearny examined profits and losses of a diversity amount of companies and came to the conclusion that sustainability reporting helps firms to increase theircapitalization up to $650 million. [1]

This year non-financial statements have been presented by prominent companies in different areas. BP (energy sector), Morgan Stanley (financial sector), Apple and IBM (computer science technologies) have released a fully disclosure of impact of their activity on social and environmental area. International companies are as conscious about their reputation in a business society as small firms are. It is commonly known that Tabacco is doing a huge harm to our health and as a result of the obligatory sustainability reporting the biggest Tobacco company British American Tobacco (BAT) released a non-financial statement where the new technologies in cigarette manufacturing are presented. Obligatory sustainability reporting made BAT renovate cigarette manufacturing process and create a technology that is twice as less harmful as it was previously.The number of non-financial statements increases from 2149 in 2010 to 4155 statements in 2013 year.

The main reason why there are increasing numbers of companies reporting non-financial statement is possibility to measure risks of their performance. Social, governance, economic and environmental operations are presented in non-financial statements. These four key areas play a huge role in building strong connections between a company and investors. It is a regular monitoring of sustainability performance that makes investors confident about the future of a particular firm. The global economy combines long term profitability based on ethical behavior and social justice that is why sustainability reporting is a vital resource for managing change inside the company performance and structure.

There are no strict rules and requirements about how the sustainability reporting should be produced although Global Reporting Initiative (GRI) set a number of indicators that should be disclosed. [5] Global Reporting Initiative was founded in 1999 and since then it has been developing and promoting the reporting system that enables organizations to measure risk of their everyday performance. GRI services don't pass and verify the quality of the disclosures although they help company with preparing non-financial reports by releasing official guidelines. The step-by-step instruction is available on the on-line resource. The requirements to the high quality sustainable statement are presented on the official website. There main indicators could be found.

GRI insists on organization revealing the information about training and education costs, presence of freedom of association inside the company and equal opportunities for women and men, absence of child labor and other essential indirect economic factors. [5]



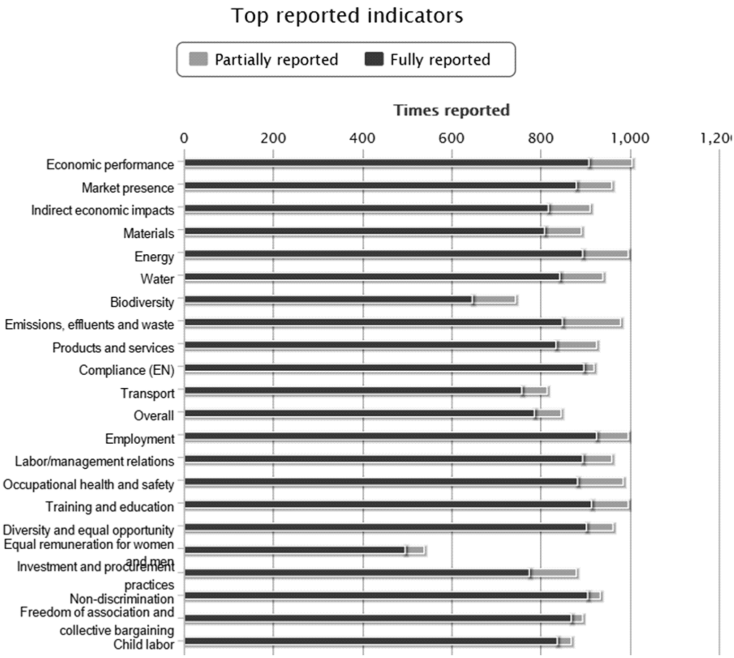

***Pic. 1.*** GRI disclosures quick view

The organization is advised to reveal the information about raw materials that are used in manufacturing goods. This information demonstrates investors how the company is anxious about environmental system and if there is anopportunity for any government to raise taxes because ofgas emissions and water polluting. There is a strong connection between environmental performance and *Earnings Before Interest, Taxes, Depreciation, and Amortization* (*EBITDA*) *which is the main reason why European investors examine under scrutiny non-financial statements.* [4]

Concealed indicators can immediately reveal weaknesses of a particular organization and investor has a chance to anticipate future profits and losses. According to official GRI statistic the indicator «Equal remuneration for women and men» is being concealed in 17% and the other indicator «Child labor» wasn't disclosed in 15% of all disclosures.

Analyzing the background of companies that didn't disclose the «Child labor» indicator shows us that indirect economic impact has huge influence on the goodwill of companies and their revenue. Using child labor isn't allowed in the world although several companies hire children at the age of 12 or even 10 years old. A huge fine system is created by the government.In some countries there is also a possibility for a law to prohibit the performance of such organizations. Financial statements don't reveal the information about employees while non-financial statement does. It is very important for investor to be aware of the fact that the performance of the organization is legal. In 2013 Apple refused to do business with Chinese company «Guangdong Real Faith

Pingzhou Electronics» that had been using Child labor. The company was fined a huge amount of money. In 2014 Samsung ceased to cooperate with Chinese company «Dongguan Shinyang Electronics» that had employed children to do a hard job. Investors lost a huge amount of money because of the public scandal and the absence of clients for those Chinese companies. The necessity to reveal full information about employees and education, health and safety costs make companies improve the conditions for workers in general. [6]




*Pic. 2.* Top reported indicators

According to GRI official statistic firms don't report the data about the amount of energy and water used in the manufacturing process and itarises a question: «Does the company have new technologies to reduce raw material costs or it wastes the resources and invested money?» The answer should be given. Firms don't want to create a reputation of a company that doesn't concern the future of nature so they renovate their technologies. Promoting sustainable reporting helps investors to anticipate future cash flows. [4]

There are internal and external benefits of sustainable reporting for companies. Increased understanding of risks and opportunities, improving efficiency, reducing costs are the key internal benefits for business. Assessing sustainability with respect to performance standards and laws has created a strong base for making contacts with private and government sector. External benefits of sustainability reporting include improving reputation and brand loyalty, increasing the price of intangible assets namely Goodwill and forecast a possible relation between profits and lossesof a company.

Sustainability reporting in Russia is not compulsory. Companies don't worry about environmental system and social rights. This policy undervalues possible risks andmakes foreign investors unconfident about their savings. Absence of information about government relations is one of crucial reasons why investors are not interested in building long-term connections with Russian companies.

In 2012 the Directive about obligatory sustainable reporting was released by the PresidentV.Putin. It states that companies are obliged to report non-financial statements in 2016.The Directive also states to create a governance structure with a respect to Global Reporting Initiative. [2] This structure should create special requirements that comply with Russian features. In future Russian non-financial system will integrate with Global Reporting Initiative so that the amount of foreign investments increases.

The economy is unbalanced because of different factors. The key problem is meaningless and unconscious attitude to environmental, social, governance and economic system. Sustainability reporting makes business reveal the information about the influence on these factors. Because of the willingness to have a strong reputation companies are keen on improving their system. Sustainability reporting can help the whole world to reduce destructive and ruinous impact on environmental and social sphere.

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# FACTORING AS AN ALTERNATIVE TOOL FOR TRADE FINANCE

## Abstract

*Any dynamically developing company, increasing its sales, may have to attract extra financial resources. One of the most popular ways which the company nowadays often resort to for their successful operation is factoring which can serve as alternative source of credit. Many small and medium-sized businesses have learned that factoring is an effective financing tool that promotes dynamic growth of the companies. However, the creation in Russia flexible factoring sector can be a time-consuming process.*

***Key words:*** *factoring, factor, receivables, loan, bank.*

## Introduction

Factoring is one of the most promising mechanisms for financing business. Traditional forms of external financing cannot be suitable in all cases. Factoring can actas an alternative sources of finance for enterprises because it is able to satisfy the needs for working capital.

Analyzing the issues related to factoring, it's worth starting with the implication and characteristics of these operations.

Factoring is a complex of services provided by the bank or a factoring company to its customer in exchange for the assignment of receivables. The term "factoring" origins from the English word «factor», which is translated as an intermediary agent. Factoring operations were based on commercial credit. It provided purchasers as a deferred payment for goods. However, the need to accelerate the turnover of funds forced suppliers to seek out new ways to reduce accounts receivable. This became possible thanks to the introduction of financial agent which may be represented by a bank in the chain of payments — that has made it possible to solve this problem for the benefit not only for the seller, but also for the buyer.

## History of factoring

The first factoring operations were used abroad in the 50-th years of XX century by American banks such as "Bank of America", "The first national bank of Boston" and "Trust company of Georgia". However, they were formally legalised in the USA in 1963, when a government organization — the controller of money circulation- decided that factoring operations represent the legal form ofbanking. [1,6]

Nowadays factoring became widespread in the West. Europe remains the largest zone with 60% of business, whilst Asia is now approaching 30% of its volume. The largest traditional market remains the UK and Ireland at €330bn but the asset- based lending approach in China is estimated to have grown to approaching €378bn. [2]

The development of factoring depended on the Convention on international factoring operations (UNIDROIT Convention or the Ottawa Convention), which contributed to strengthening of the world trade integration.

This Convention was developed by the specialists of the International Institute for the unification of private law and proposed to the international community for consideration and accession. The Convention establishes a special legal regime, which should be adequate to the tripartite relations in factoring.

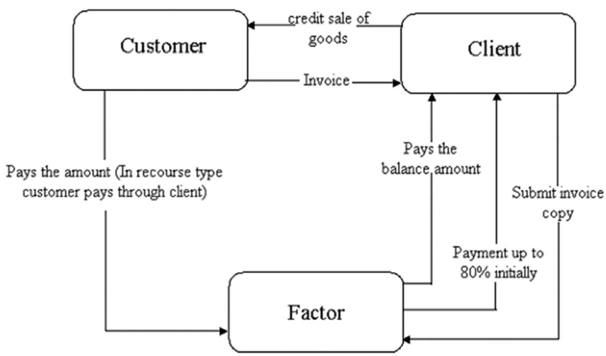
## Mechanism of factoring operations

Article 824 of the Civil Code contains a definition of factoring as “accounts receivable financing requirements.” [3]

There are 3 parties involved in factoring transactions:

1) afactor intermediary. As a rule, a commercial bank or its subsidiary branches;
2) a bank customer –the supplier that provides goods and services;
3) a debtor — the buyer undertakes to repay the vendor claims.

The essence of factoring is that the supplier of goods and services gives factor its rights to demand and receive payment from its counterparties for goods and services.




Mechanism of factoring

International factoring implies a set of a commissions and intermediary services provided by factor to its supplying customers in the implementation of the last payment for goods and services. It may be noted that the factoring services have become an independent high-tech industry.

## Advantages and disadvantages of factoring

Factoring has several advantages compared with the credit. So, factoring does not require collateral and paperwork. It only requires notification of customers about changes in the details of payment for supplies. Recoverability of the loan is incorporated in its nature. This requires the supplier to accumulate and withdraw from circulation the respective amounts of financial resources.

The advantage of factoring is the fact that factoring means refunding of money by the buyers. The amount of the loan is determined immediately, but the size of the financing in factoring is not limited and can be increased with an increase in sales of the client.

So, taking everything into account factoring has certain advantages for customers. However, in this field, as in any other field, there are some problems.

First, *the cost of factoring services*. Often factoring is considered one of the most expensive forms of financing, but that's not always true. Factoring costs more, when we compare the discount rate factors charge against the interest rate banks charge. But if a company can't qualify for a loan, it doesn't matter what the interest rate is.

Second, *possible harm to a customer.*Selling company gives the charge of collecting invoice to the factoring company and pays more attention to money collection methods which impairs company's relationship with their customers.

Third, *company image distortion*. In the past, factoring was considered a sign of the financial difficulties of the company. However, in recent years this perception has changed and it has been considered a normal way of doing business. Finally, some customers might want to deal directly with the selling company instead of dealing with factor.

Thus, weighing the advantages and disadvantages of factoring, it looks like bank financing is preferable over accounts receivable factoring, but only if banks can provide all the funds a business needs. On the other hand, if a business doesn't qualify for a line of credit large enough to pursue growth opportunities, accounts receivable factoring proves to be a perfect alternative financing option to supply the needed cash flow.

## Impact of the situation in Ukraine on factoring

In view of recent events, namely, the growth of political tensions between Russia and the West on the background of the situation in Ukraine, we cannot but touch upon the problem of how the sanctions from the West have influenced the volume of factoring transactions. As a result of the fact that foreign consumers are now less willing to purchase Russian goods, we can only suppose that the demand for export factoring will reduce.

According to experts, the situation in Russia is rather specific because the geopolitical problems connected with theUkrainian crises, are the main reason for the decline of factoring transactions. This reduces the stability of the business environment, which has a direct impact on the development of international trade and international factoring market in particular.

In general, the situation is not critical. Due to the nature of the Russian economy the share of international factoring in the portfolio of Russian banks is small. The decline of Russian businessparticipation in international factoring does not play a significant role in economic terms, as factoring is not yet well developed, and its turnover is calculated in small amounts.

Despite the fact that, factoring was primarily used in the garment and textile industries, today, it is widely used by all types of businesses that extend credit to credit worthy commercial customers.

## Major trends

The International Factors Group (IFG) has published its Global Industry Activity Report (GIAR) 2013. It examines development of the worldwide factoring Industry drawing on input from more than 60 countries. According to the report the global factoring industry volume in 2013 increased by around 3% to reach a record level of €2.2trn.The industry continues to be highly concentrated, with the top five providers in each market averaging over 80% of the volume. Bank-owned factoring businesses continue to dominate the markets. The largest traditional market remains the UK and Ireland at €330bn but the asset- based lending approach in China is estimated to have grown to approaching €378bn.

## Conclusion

Summing up, it can be noted that factoring can be considered as an alternative source of credit. Factoring is an emerging industry that dynamically develops worldwide. Many small and medium-sized businesses have learned that factoring is an effective financing tool that promotes the active growth of companies. However, the creation factoring sector in Russia is a time consuming and lengthy process, due to the specifics of the Russian economy and the lack of experience in this field.

Therefore, factoring will flourish with the development of a competitive market of services and banking operations, which is directly connected with the improvement of legislation in this area, and experience of leading countries on the factoring market.

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# THE IMPLICATIONS OF THE UKRAINE CRISIS FOR RUSSIA — EU ECONOMIC RELATIONS

## Abstract

*Today's situation on the world political arena calls into question the further prosperity of economies of the developed countries. The Ukrainian crisis strongly undermined the economic relations between Russia and some of its traditional allies, particularly the European Union. For decades these two countries had had close trade relations. However political affairs had a strong impact on the economic sphere of the countries that in turn brought huge losses for both parties.*

***Key words:*** *Ukraine crisis, sanctions, Russia, EU, trade relations*

## Introduction

In response to the Crimean crisis and the accession ofthe Crimea to the Russian Federation, some governments and international organizations, led by the United States and the European Union, imposed sanctions on Russian individuals and businesses. The Russian government responded in kind, with sanctions with a total ban on food imports from the European Union, United States, Norway, Canada and Australia.

The Ukraine conflict is having serious consequences for the EU-Russian relations and has strongly struck the economies of both countries. In Russia, the costs of the conflict are estimated to be in the tune of 1% of GDP in 2014–2016, primarily on account of increased investment risks. A rough estimate of economic effects owing to lower GDP growth yields a Russian GDP loss of close to EUR 20 billion in 2014 and more than EUR 30 billion in 2015.The effects on the individual EU countries differ depending on their exposure to the Russian market. In absolute figures, Germany might lose around EUR 3 billion, followed by Italy (EUR 1.4 billion), France, Great Britain and Poland (EUR 0.8 billion each). Austria could lose close to EUR 300 million in this scenario.[1]

## Trade between Russia and the European Union

It`s worth mentioning, that trade exposure between the EU and Russia is hugely asymmetric. According to the Eurostat statistics, in 2013 the EU was Russia's main trading partner accounting for 53% of Russian exports and

39% of Russian imports. In 2013 trade between the two nations reached 268 EUR billion. EUexports to Russia in 2013 accounted for EUR 213 billion, and imports from Russia — EUR 123 billion.[4] EU exportsto Russia predominantly such items as machinery and transport, manufactured goods and chemicals products. EU imports from Russia is presented by 5 key branches, such as mining and quarrying, coke and refined petroleum products, chemicals and chemical products, basic metals, wood and paper. Russia mainly provides Europe with oil and gas. It is common knowledge, that Russia is the main supplier of raw materials to Europe.

## The Russian food embargo

It is important to notice, that food embargo caused severe damage on the economy of the EU, which became Russia's response to the measures adopted by the EU. As the European Parliament stated in Brussels, Russian market is the second largest supplier of products in Europe. Naturally, the loss of a partner is a painful blow to manufacturers. It is known that at the moment, the loss amounted to about EUR 155million and it is only from suppliers of vegetables, peaches, oil, nectarines and cheese.

If we consider the whole picture, we should refer to last year's data. In 2013 the European Union earned EUR 11.3 billion from exports ofagricultural products to Russia. Thus, the embargo will cost Europe not less than EUR 5.25billion.[8]

## The consequences of the sanctions for the major European countries

Perhaps we should also point out the fact that for each country the damage done by sanctions is measured in colossal figures. Under the data, Germany suffered mostly from mutual sanctions among the other European countries. As Germany has the largest volume of trade of any European state, it is the most entangled with the Russian economy.Trade with Russia was EUR 77 billion in 2013. As a proportion of total visible exports from Germany, goods destined for Russia accounted for more than 3%. Germany's imports from Russia are practically all raw materials, with oil and gas making up 84%, producing an energy bill of some EUR 36 billion in total. Gas imports from Russia are most critical from a German perspective, as 39% of the country's gas needs are met by Russian supplies. Moreover large numbers of German companies are active in Russia — some 6,200 of them, more than from all other EU nations put together. Exports are mainly cars, machinery, chemical products and electronics.

Obviously, it isthe nation, which hardest hit by the sanctions — both the ban on agricultural imports and the trade restrictions on arms, special installations for the energy sector and dual-use technologies. According to the Federal statistical office of Germany, in 2014 German exports to Russia amounted to EUR 20.3 billion, which is 16.6% less than in 2013 as a result of the sanctions.[9]

Although exports to Russia is about 3% of the total volume of exports of Germany, the Committee for economic Affairs is concerned about the threat for 50 thousand jobs in Germany in term of negative trends in exports.

The mood in the business community in Germany decreased for the fourth consecutive month, reflecting the poor economic performance of the Eurozone. The business climate index calculated by IFO fell to 106.3 points in August compared with 108 points in July 2014.

The tension in relations with Russia also contributed to the fall in economic output by 0.2% in the previous quarter, and this is the first reduction since the end of 2012. The German engineering sector, for example, where Russia is the fourth-largest export market, sent almost 19% fewer exports to Russia in the first half of 2014.. Exports of machinery decreased by 17.2% and exports of chemical products by 5.9%.As for food market, the volume of imports of German products in Russia in 2013 amounted to EUR 1.6 billion, which is 14% lower compared to 2012.

However, other countries are also faced with enormous challenges in terms of Russian embargo. For examples, companies from Poland, the Baltic States, Finland, the Netherlands and Spain also need to find alternative destinations for their fruit and vegetables — if that's even possible at such short notice. European vegetable growers, particularly Holland and Poland, were perhaps those who suffered most from the sanctions. European farmers, whose annual exports to Russia was total 16 billion euros, were seriously affected by the sudden imposition of sanctions on exports. That loss in food exports was followed by Ireland, whose cheese exports to Russia was total 4.5 billion euros a year. While Russia was able to obtain those products from other sources, particularly Turkey, European sellers' losses have not yet been compensated. France, for its part, is bound to suffer under the embargo on future arms shipments and Britain's financial sector will feel the effects of the sanctions against Russian banks. If the sanctions remain as they are, the negative impact on European growth will be manageable.[2]

Moreover, many western companies have taken a hit as the conflict in eastern Ukraine drags on and the sanctions imposed by both sides start biting. Here some of the biggest brands affected.

- Carlsberg warned that profits would fall as Russian economy stalls.
- Adidas scaled back its operation in Russian.
- Total owns a stake in Russia`s energy giant Novatek. There will be a drop in profit
- Societe Generale`s profits in Russia fell 36% in the second quarter
- Volkswagen reported 8% drop in car sales in Russia the first six months of 2014
- Renault reported a slowdown in Russia
- Danone said its results were hurt by a decline in the ruble.

- BP owns a stake in Rosneft, Russia`s biggest oil company, which is taking a hit due to the western sanctions.

## The Russian economy under the sanctions

Now I suppose, it`s time to concentrate on the Russian Federation. The sanctions have undoubtedly augmented the negative economic developments in Russia resulting from the combined effect of the deteriorating investment climate, ruble depreciation. In April 2014, the volume of Russia's trade with the European Union decreased by 3.4% compared with April of 2013 and accounted for USD 103.2 billion. The volume of Russian exports declined by 2.7% and amounted to USD 91.2 billion and Russian imports fell by 5.0% to USD 38,9 billion compared with April 2013.[10]

**Trade between Russia and the EU**

| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | April 2013 | April 2014 |
|---|---|---|---|---|---|---|---|---|
| EU | *382,4* | *236,3* | *307,0* | *394,0* | *410,3* | *417,7* | *134,8* | *130,2* |
| Growth rate | *35,1* | *–38,2* | *29,9* | *28,3* | *4,1* | *1,9* | — | *–3,4* |
| The EU's share in total foreign trade of Russia | *52,0* | *50,4* | *49,1* | *47,9* | *48,4* | *49,0* | *49,6* | *49,2* |

Source: Ministry of Economic Development of the Russian Federation http://economy.gov.ru/

Significant decline was recorded in the trade of Russia with the support anti-sanctions European countries — Great Britain (–19,6%), France (of –16,7%), Poland (–15,8%) and Finland (–14,4%).Trade with other EU countries has declined more slowly. For example, the volume of trade with Italy decreased by 8.8%, with Germany by 6.7%, and the Netherlands — 2.7%. The Russian finance minister Anton Siluanov said at an international financial and economic forum in Moscow, that western sanctions cost the Russian economy $40 billion this year.

## Conclusion

To draw the conclusion, one can say that, the Ukrainian crisis and the subsequent reciprocal sanctions played a crucial role in the development of EU-Russian economic and trade relations. In terms of the aggravation of the situation on the political arena, it is important to maintain economic ties between Europe and Russia at the same level, in order to avoid immeasurable losses to both sides. That`s why it`s not surprising that many European politicians have begun to discuss the possibility of easing sanctions against Russia, with the aim of restoring the previous trade indicators.

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# EMERGING MARKETS: IS THE STORY OVER?

## Abstract

*Nowadays emerging markets are slipping into recession: Chinese growth rates decelerate, Brazil suffers from stagflation, Russia's economy is suffocated by sanctions and South Africa is exposed by government inefficiency. In addition, the Fed announced the narrowing of the program of quantitative easing. Local currencies of emerging countries plunged significantly and yields on local government bonds rose sharply. This paper examines obstacles which impede sustainable growth of emerging countries, comparative analysis of current crisis and the Asian crisis in the 1990s as well as proposes the strategies to overcome the slowdown.*

***Key words:*** *emerging markets, quantitative easing, recession, the Asian crisis, BRICS*
***JEL codes:*** *F 290, H 870.*

Emerging Markets (EM) are the source of concerns. Currency fluctuation, inflation growth, and political unrest caused investors to worry about the possibility of the EM crisis repeat. On average, EM economies grew by about 4¼ percent annually during 2000–2012 — one percentage point higher than on average in the 1990s. However, in 2013–2014 economic growth in EM declined to just 3¼ percent, with notable slowdowns in the largest EM (Brazil, Russia, China, India, and South Africa (the "BRICS")). EM as a whole, as measured by the MSCI Emerging Markets Index1, retreated 6,49% in 2014, adding to the 2,60% loss for 2013. What led to this slowdown?

The Fed's quantitative easing (QE) program entailed massive liquidity in the global markets over the past several years. This monetary inflow helped fuel the global recovery. However, the announcement of tapering QE program in December 2013 led to market decline. Tighter money means higher global interest rates, which translate into higher borrowing costs for EM countries and more difficult funding growth. So, investors began leaving the market. The capital inflow to the emerging economies turned into a capital outflow. Local currencies dropped considerably, yields on local government bonds rose sharply. It is worth to mention that most of EM countries are subject to foreign capital inflows, and withdrawal of investors disrupts EM economies.

The central banks in these countries tried to conduct policies to stem capital flight and defend their currencies. The central banks in Turkey, South

[1] The MSCI Emerging Markets Index captures large and mid-cap representation across 23 Emerging Market (EM) countries. With 836 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

Africa, India, and Brazil rose rates to control inflation and prevent currency undervaluation. However, all efforts entailed currency depreciation.

Political turmoil adds to EM investors' unease — particularly in Turkey, Ukraine, and Thailand. Possibility of war, tax increase, loss of subsidy, change of market policy, excessive government intervention, inability to control inflation, all these factors facilitate high political risks.

Less robust global growth is the subject of great concern in EM. Decelerating growth in China, and stagnating demand for materials and commodities restrain global economy. Slow growth in China coupled with the country's transition from an infrastructure- and export-based to a service- and consumer-based economy have adverse effects on commodities-driven economies: Australia, Indonesia, Russia, and Latin American countries (Brazil and Peru). Moreover, cheaper Japanese exports suppress manufacturers across Asia.

All EM can be divided into five groups based on challenges confronting countries. One group includes of economies like Argentina, Ukraine and Venezuela. These countries suffer political and economic instability; they share an insufficient management of internal politics that makes them vulnerable to increased volatility. The second group consists of countries with large current account deficits. Turkey, South Africa, Chile and Peru, whose currencies experienced deep depreciation this year, would be members of this group. The third group is formed by Eastern European countries, such as Hungary and Romania, which are sensitive to renewed instability in the peripheral euro zone countries due to their strong financial ties to the euro area through their banking sectors. The fourth group composes of the BRICS countries (Brazil, Russia, India and China), with internal structural problems of a different nature. For instance, in Brazil the combination of an inflation rate close to 6% and reduced growth leads to monetary tightening by the central bank. In China, the potential destabilization caused by "shadow banking" and the incomplete reorientation of growth towards domestic demand threatens to weigh on Chinese, as well as global recovery. In the fifth and final group, we include the countries like Korea, Mexico and Poland, which have solid economic prospects, a lack of internal imbalances and financing structures that are less dependent on global liquidity. These countries are the best positioned to deal with the effects of tapering.

These events in the emerging markets reflect the situation in the mid-1990s. In 1997, after years of robust growth, Asia was suffocated by the currency crisis. The impetus came from Thailand, when the central bank decided to allow the Thai Baht, which had been pegged to the US dollar, to float freely. As a result, the currency plunged by almost 20%, triggering a panic capital flight. The crisis affected the neighboring countries (Indonesia, Malaysia, the Philippines, Singapore and South Korea). The countries of "fragile five"1 are highly dependent on foreign capital. In the past, thanks to extremely loose

[1] The countries with high inflation and sharply negative current account balance are also known as the "fragile five" (Brazil, India, Indonesia, Turkey and South Africa).

monetary policy, primarily in the USA, this was not a problem. Huge amounts of capital flowed into the world's emerging economies. Cheap money promoted lending, facilitated economic growth and raised standards of living. However, too much liquidity from debt-driven growth can also be harmful as we observe today. So, what steps will help EM overcome economic drop?

Adequate infrastructure (ports, roads, urban infrastructure, communications) are prerequisites for the development EM to sustain their growth. Almost all major EM, including China, have a poorer quality of infrastructure than developed peers (Table 1). Inability to transport products efficiently to market, supply a dependable source of electricity for industrial development or offer a communications network worthy of a world class services sector seriously impedes EM to yield income from distributive sources.

*Table 2*

**Infrastructure needs sizeable in Emerging Markets**

| Percentile ranking of infrastructure assets | US | Germany | Brazil | Mexico | China | India | Russia | South Africa | Turkey |
|---|---|---|---|---|---|---|---|---|---|
| Quality of overall infrastructure | 89% | 95% | **26%** | 43% | 56% | **32%** | 41% | 65% | 47% |
| Quality of roads | 92% | 96% | **17%** | 50% | 62% | 35% | **22%** | 70% | 59% |
| Quality of railroad infrastructure | 87% | 96% | 35% | 46% | 79% | 84% | 76% | 72% | 48% |
| Quality of port infrastructure | 90% | 96% | **8%** | **29%** | 59% | **30%** | 43% | 63% | 34% |
| Quality of air transport infrastructure | 85% | 97% | **24%** | 58% | 44% | 50% | 34% | 81% | 59% |
| Quality of electricity supply | 87% | 95% | 56% | 35% | 49% | **19%** | 51% | **24%** | 37% |
| Telephone lines | 89% | 98% | 53% | 49% | 65% | **20%** | 71% | **32%** | 60% |
| **Total** | **94%** | **99%** | **41%** | **49%** | **65%** | **46%** | **56%** | **64%** | **50%** |

Source: [2, 3]

As evidenced in a recent IMF study, there is a strong statistical relationship between higher GDP growth and a dependable legal framework. Strong property rights and the ability to enforce contracts are important conditions to healthy development of market-based, value added economic activities that help promote private investment and entrepreneurship as well as foster financial sector development.

Moreover, there is a strong correlation between years of education and a country's GDP per capita. Education geared towards exploiting a country's competitive advantages is not only capable of producing higher returns relative to similar investments in the developed world, but is necessary to attracting the investment and technology required to escape the middle income trap. While most EM successfully exploit a model of high volume (non-qualified labor, low value-added operations). Improving both the quality and availability of tertiary education to all potential members of the labor force will become perhaps as important as allocation of capital to research and development.

Prudent macroeconomic policy is the key to achieving sustainable growth. The policy should be focused on, among other factors, low inflation, elimination of trade restrictions, manageable public sector debt, avoidance of credit bubbles, as well as encouraging domestic savings. Transparent and clear legal and banking frameworks will attract foreign investment, foster internal growth.

Deep, liquid domestic capital markets are essential for investments aimed at maximizing productivity and reducing dependence on foreign markets. Liquid, functioning domestic markets provide both public and private sector issuers with access to long-term local currency funding while reducing dependence on foreign sources of finance. In many cases, local banks lack the scale and ability to provide long-term financing for private sector investments and public infrastructure.

Emerging markets today drastically differ from those of the past. Today's EM economies are stronger, their companies' balance sheets are cleaner, and their political infrastructures are more transparent. EM now account for approximately 40% of global GDP, significantly more than 15-20 years ago. That is why the current situation will not translate into EM crisis of the 1990s. Upward growth trend in emerging markets remains intact, and EM equities should continue to provide attractive funds. Nevertheless current volatility will exist over a short term.

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# THE HIGH COST OF DEFLATION

## Abstract

*This paper is devoted to a growing concern of deflation as inflation is falling around the world. Nowadays inflation is below 1% across industrialized countries. At first sight a general decline in prices sounds tempting but when deflation takes place, it can at least dull an economy. Declining prices may have several negative impacts on economy and can create a deflationary spiral that is turned hard to get rid of. In Euro-zone economies the risk of long-lasting deflation is more of a worry than elsewhere. In other words, the global economy is slowing down again.*

***Key words***: *deflation, deflationary pressure, low inflation, global economy, unemployment, the European Central Bank*
***JEL коды:*** *E310, E580*

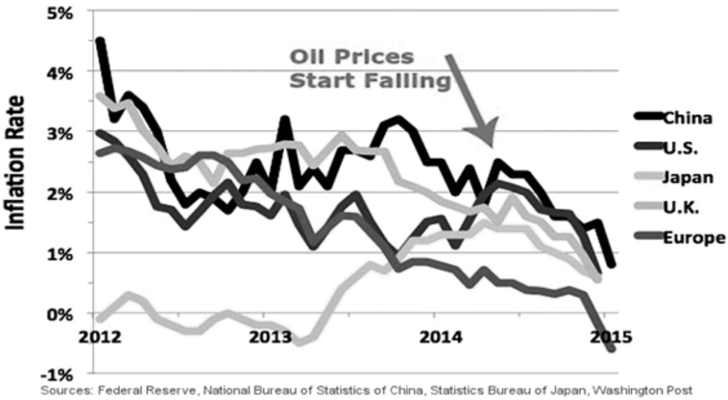
For central banks of industrialized world, "two" is a magic number. If annual price increase amounts to 2 %, most shoppers can more or less disregard this upsurge. This level of inflation is very beneficial: it gives bosses an incentive to opt for investing their earnings in something that returns more or give it back to the shareholders as dividends. Moreover, it keeps economies away from deflation and the unwanted, depressive behavior and choices like hoarding cash, delaying purchases. In spite of the professed adherence to the 2% price stability mandate, the period of falling prices is on the cards.

So what does deflation mean? Deflation is defined as a fall in the general price level. It is a negative rate of inflation. This phenomenon means that the value of money increases rather than decreases. This allows shoppers to buy more goods with the same amount of money over time. Deflation is not necessarily bad, however several periods of deflation or just low inflation can lead to high level of unemployment, stagnation of economy and deflationary spiral. Deflation can be both short-term and long-term. For example, Japan had a period of deflation lasting decades starting in the early 1990's.

It is worth noting that "deflation" is often confused with "disinflation". As it is mentioned deflation represents a decrease in prices for goods and services while disinflation represents a situation of slowing inflation. Disinflation is not considered to be as problematic as deflation because prices do not actually decline.

The whiff of deflation is everywhere as inflation is below 1% across industrialized countries. Even in America, Canada and Britain — all growing at more than 2% — inflation is below target. The UK registered the lowest inflation rate (0.5 percent) since 2000, while US inflation slacked to 0.8 percent, the steepest monthly slowdown in six years. Japan's 2,4% rate is set to evaporate, as Japan is projected to fall back into deflation. But it is the Eurozone that is most striking. It slipped into negative inflation in December 2014 (-0.2 percent). Today 15 of the area's 19 members are in deflation. The highest level of inflation registered in Austria amounted to 1 %.

Inflation is below 1%




***Graph 1***

A sharp decline in oil prices resulted in a significant slowdown in inflation of advanced economies. A barrel of Brent crude cost $110 a year ago, whereas its present price is less than $60. Most economists agree that the sharp oil prices drop is caused by decreased demand. This fact underwrites energy and transport prices decline allowing economies provide more goods at lower prices. Also there was a decrease in non-energy industrial and durable goods. For many industries falling prices are already a commonplace thing. In euro zone the prices of computers, phones and cameras have been falling for a decade. For instance, in Spain telephone equipment is 90% cheaper than ten years ago. So it is obvious that deflation is not surprising for shoppers. Even in Japan there is little evidence that purchases are being put off.

Experts identify several reasons for observed situation in Europe.

First of all it is a significant increase of unemployment since 2008, with the unemployment rate now amounting to 11,3%. In Greece it is close to 26%. It will take years to overpass the situation. Even if Spain, praised for its 2% growth rate, keeps current growth of economy it will take eight years for unemployment to attain pre-crisis rate. And this fact makes the risk of long-lasting deflation more of a worry than elsewhere.

The practice of devaluation also played a role. The least developed countries of the Eurozone, which became uncompetitive in the boom period, can not devalue their currency to regain competitiveness. The only possible solution for them is to pursue internal devaluation. This means reducing costs and therefore prices in the economy primarily by cutting wages. That's how southern Europe can make their exports more competitive and at the same time reduce the purchasing power.

What is more, the fundamental cause of falling prices is weak demand within the Eurozone. Fiscal austerity to try and reduce budget deficits that was pursued by several countries — spending cuts and tax increases — caused a significant drop in demand. And because of the relatively tight monetary policy, and strong Euro, demand could not be spurred by other sectors of the economy.

So inflation is falling rapidly around the world and this is happening despite the unprecedented efforts of the European Central Bank, the US Federal Reserve and other central banks around the world to reverse this trend. But what is the danger of falling prices and what are the effects?

At first sight a general decline in prices sounds tempting. But even low inflation can at least dull an economy especially the most fragile countries in the current environment. So declining prices may have several negative impacts on economy. They are as follows:

— *Discourage consumer spending.* When there are falling prices, this often encourages people to hoard cash and delay purchases because they will be cheaper in the future. This in turn creates more deflationary pressure in the economy. That is why the boost to purchasing period of falling prices is welcome.

— *More difficult for relative prices and wages to adjust.* While deflation/lower inflation in highly indebted countries is painful to them, at least it improves relative prices, and hence exports and current account sustainability. Unfortunately, when inflation turns low everywhere in the euro area, each unit of deflation/low inflation endured by indebted countries delivers less price adjustment relative to the surplus countries. In other words, each point of relative price adjustment must be bought at the cost of greater debt deflation.

— *Real wage unemployment.* Labour markets often exhibit 'sticky wages'. In periods of deflation, real wages rise. This could cause real-wage unemployment.

— *Increased real debt burden and the real interest rate that borrowers pay.* If falling prices endure, then debts, fixed in nominal terms, are harder to pay. A recent study by McKinsey, a consultancy, tracked total debt—government, household and corporate—between 2007 and 2014. Euro-zone economies lead the charge, with debt up by 55 percentage points of GDP or more in five troubled "peripheral" states and three "core" ones. If incomes consistently fall those debts may become impossible to pay.

Very low inflation may benefit important segments of the population, notably net savers. But in the current context of widespread indebtedness problems, it is a growing problem in a modern economy. Governments around the world should prop up aggregate demand through an appropriate fiscal response. The Bank of Japan is committed to as much Quantitative Easing as it takes to get inflation back to 2%. Now negative interest rates as a new and radical policy is becoming fashionable, with Nordic central banks following the ECB in adopting it. Going forward, the expectation is that the Eurozone will remain in price decline for the whole of 2015, despite the expanded QE adopted by the European Central Bank. In other words, it seems the global economy is slowing down again.

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# INVESTMENT CLIMATE IN RUSSIA: UNSETTLED PROBLEMS AND NEW CHALLENGES

## Abstract

*Being one of the top destinations for foreign investment, Russian economy has been suffering post-soviet difficulties for a long time preventing investors from considering our country as a target destination for their assets. Furthermore, recent events and political and economic segregation of Russia from the world community have put significant obstacles in the way of new investment. But while some international companies discontinue doing business in Russia, other large corporations are still participating in new investment projects.*

***Key words:*** *investment climate, foreign direct investment, political and economic segregation, international companies, investment project.*
***JEL code:*** *F21*

Supposed to be one of the top destinations of foreign investment, the Russian economy has been suffering post-soviet difficulties for a long time preventing investors from considering our country as a target destination for their assets. Furthermore, recent events and political and economic segregation of Russia from the world community have put significant obstacles in the way of new investment.

## Attracting foreign capital as one of strategic priorities

Countries seek for FDI (Foreign Direct Investment) as they give many benefits. Russia views foreign investments as a driver for:

1. Accelerating economic and technical progress
2. Revamping and upgrading production facilities
3. Mastering advanced production management methods
4. Ensuring employment, training personnel capable of responding to the challenges of a market economy

Russia is interested in an inflow of enterprise capital rather than borrowed capital because in this case the country's external debt does not grow, and the cooperation with foreign companies provides Russian businesses with new technologies, management methods and direct access to global markets with competitive products, real investments are the impulse the economy needs to ensure healthy economic growth.

## Advantages of investing in Russia

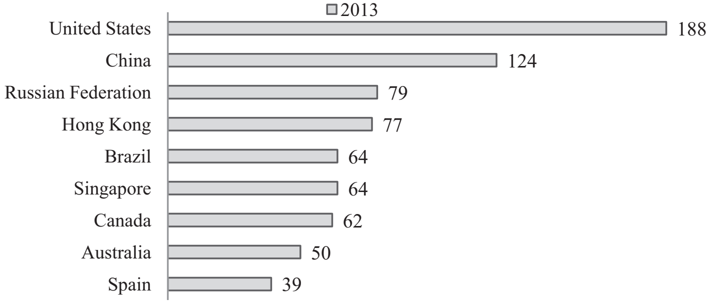
The Russian Federation is found among the nations that have a great potential as a target for foreign investment. The country offers certain advantages that promote investment to the economy, some of them are the following:

- Rapid economic growth and technological development — since 1999, GDP (Gross domestic product) growth has averaged about 7% per year, average world economic growth being 4-5%. Russia also possesses huge scientific potential that builds a base for technological and scientific research and cooperation with research institutes abroad.
- Favourable geographic position –Russia is a connecting link between Europe and Asia, has a maritime boundary with North American continent that makes the country the centre of transportation network, including marine, land and air.
- Vast natural resources — the Russian Federation is a world leader by resources per capita, among which there are natural gas, oil, minerals, metal, energy, forest and fresh water.
- Large-scale consumer market — with a population of 140 million people and persistently growing income per capita Russia represents a vast market. There is a gap created by large internal demand for all types of goods and services and insufficient supply from domestic sources that is filled up mostly through importing.
- Highly qualified human capital — Russia enjoys intellectual economy, well-skilled labour force, strong scientific and research base, as well as extensive R&D facilities.

Considering all the advantages, investment climate in Russia seems to be rather favourable.

## Russian investment climate assessments

The UNCTAD (United Nations Organization on Trade and Development) ranks Russia as the third top FDI destination in 2013.




***Graph 1.*** FDI inflows: Top 10 host economies (billions of dollars)[3]

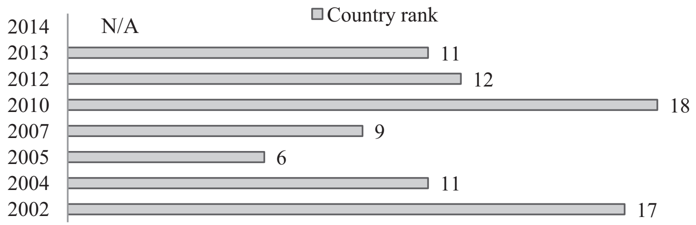
Unfortunately, most of these capital investments come from the offshore zones, and the real situation is not so positive.

Though there are so many advantages and motives for investing in Russia, our economy still has enough obstacles preventing investors from targeting their assets to it, and investment climate in Russia upon assessment of the experts of international organizations is stated as comparatively negative. Pursuant to the ranking of "Doing Business-2015"[1] report (the World Bank) Russia stands 62$^{nd}$ by the ease of doing business and 143$^{rd}$ among economically free countries according to the Index of Economic Freedom [2] (Heritage Foundation) — rather unfavourable indicators for a country pretending to be economically developed. It is strongly connected with corruption and bureaucratization of Russia, which stem from the Soviet planned economy, as well as intransparent legislation and observance, heavy taxes and high trade barriers.

Understanding the existing difficulties but still unable to struggle against them, Russia has appeared to face new defiance arising from heightened political tensions.

## New challenges

Investors are constantly monitoring the existing geopolitical conditions. According to newly issued by the UNCTAD the World Investment Report [4], the volume of FDI to Russia has fallen sharply, by about 70% to $19 billion. The UNCTAD attributes the decline partly to the Ukraine conflict, Western sanctions on Russia, and resulting raised investor concerns. Though, last year the Russian Federation was not listed among 25 most attractive FDI destinations for the first time in over a decade.



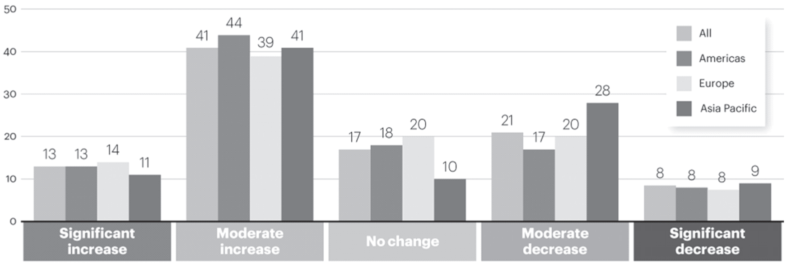

***Graph 2.*** Russia's position in the FDI Confidence Index [0]

During 2014–2015 due to sanctions, sharp currency fluctuations and non-lucrative continuation of a business many foreign companies marked their intention to quit the Russian market and closed many or all their affiliates throughout Russia's territory. This fact refers to many retail companies such as EM&F Group, New Look Group, that totally abandoned Russian market, Adidas Group, that plans to close 200 stores located in Russia, and also such well-known brands as, for example, Samsung, that abridged its presence at the market significantly, and McDonald's, that cuts its 2015 expansion plan.

CNN is planning to quit the market, General Motors discontinues production in Russia and radically curtails the lineup.

## New investment prospects

In spite of this, the Russian economy is still able to attract foreign investment. According to preliminary A.T. Kearney Foreign Direct Investment Confidence Index 2015 results, half of investors still see Russia as a viable operating environment in the medium term.




***Graph 3.*** Change in FDI to Russia and its neighbours in 2015 if geopolitical tensions eased (% respondents) [0]
Note: Figures may not resolve due to rounding

Many companies abroad decide to mitigate foreign exchange risks by localizing production in Russia. This mostly refers to the manufacturing sector. In support of this fact, Volkswagen concern is investing in engine producing plant in Kaluga and has already invested about €250 million in the project. The second stage of a factory is going to be built by Claas, a German producer of agricultural machinery, in Krasnodar. They plan to implement the project with the overall cost of €120 million in Krasnodar. Also, SAP, one of the world's largest corporate software producers, made an offer to invest in the Russian technology sector against reservation of a right to work on state orders. It should be mentioned, that among SAP largest clients in Russia are Gazprom, Lukoil, Rosneft, Russian Railways.

Continuing investment processes in our country are also connected with the fact that many European companies consider sanctions discontinuation inevitable and are acting in their medium- and long-term interests. Europe has already felt the sanctions itself, as it is, along with the USA, one of the top investors in Russia.

To conclude, despite Russia's internal problems with legislation and trade barriers, as well as external difficulties in the form of economic and political sanctions, advantages of investing in Russia still exist and prevail. The European business is preparing to terminate the sanctions, as otherwise, if they continue, it would affect not only the Russian economy, but the economy of Europe as well. And it is not what the world community should allow.

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# COLOR PSYCHOLOGY: SCIENCE OF FUTURE OR PRESENT?

## Abstract

*"Colors, like features, follow the changes of the emotions" — said Pablo Picasso. Who knows better than Picasso. Recent studies have found out that color is a powerful communication tool and can be a signal, influence mood, and cause physiological reactions. Different colors can have different effects. In the first part of this paper the questions what color psychology is and how colors affect us are considered.Thenthe power of color and brand in modern society is analyzed.And the final part presents examination of color policy in Russian banking sector.*

***Key words:*** *banks, marketing, colors,brandpersonality, logo design*
***JEL codes:*** *M31, M37*

## Introduction

One of the most important aspects in creating a corporate identity is the choice of corporate colors. Color has a very strong effect on our mood and can perceive different emotions. Different colors can be a sign of prestige, as well as affect perception of product. What is more, marketers use color to evoke associations. Colors can alter the meaning of the situations. Sometimes if consumers lack motivation, information or ability to evaluate a product they may use signals such as shape or color to make a decision. Moreover in today's world with enormous amount of options and products branding and colors are becoming more and more important.Therefore, the corporate colors are the brightest identifier of the company.

## Color psychology

Almost ninety percent of our knowledge about the world we become though our vision. So it is not a surprise that marketers are creating brand trying to appeal to its visual characteristics, especiallyto name and logo. However, more and more attention is being now paid to corporate colors. According to the National Bureau of Standards human eye is able to perceive almost 10 million different colors. Almost everyone is affected by color, but there are no two people who has exactly the same reaction to a particular color or their combination, though certain general reactions exist [8].

Till 19th century scientists denied the fact that color can affect our choice. But recent studies have proved that color affects the way we feel. [7]

Corporate color — it is one of the key elements of corporate symbols. Together with the brand colors have become one of the main tools used by companies to differentiate. Bright colors and a recognizable brandhelp companies to stand out among a great number of competitors and to more effectively attract the attention of clients.One of the Beeline image-makers John Williams once said: “The one who controls colorsis saving half of the advertising budget.”

## Brand and colors

Like a carefully chosen brand name, color becomes a central place in the brand’s identity, it increases brand recognition [3], and contributes to the desired image [4]. Through color a brand can establish an effective visual identity, form strong associations, and with the help of brand company can position itself among competitors. Thus the brand loyalty may decrease in response to changes in a brand’s color scheme [6]. Recently almost all discussions about color psychology have generally lead to anecdotes [5]. On the other hand, managers have often relied on the recommendations of consultants, whose judgments based on their own past experience rather than scientific data. In 1997 Gorn et al. [5] having interviewed 12 creative directors found that most of them are not familiar with color psychology and their decisions are based mostly on good feeling or past experience. But nowadays color is one of the main variables in corporate and marketing communications. It has become an important variable in the marketing literature, as it can induce emotions, influence choice and help producers differentiate from one another. Sonowadaysmarketers and advertisers do realize that colors can affect consumption.

## Colors in Russian banking sector

Banks were one of the first in Russia to understand the importance of carefully chosen color scheme. In the mid-90s the main idea of all banks was leadership in the economy.[1]Bank’s marketers have chosen advertising policy that corresponded with this idea. 1998 crisis has crushedbanks’ reputation and changed the advertising strategy to recovery of lapsed power and trustworthiness. According to MDM-Bank vice-president Ilya Razbash, “afterthe deposit insurance system advent the reliability of credit institutions is no longer so relevant for as before. What is more, in fact, bank are not differentiate from each other in product lines, conditions and quality of services. So now it is important to understand what exactly and in what form should the products be offered.”In today’s competition circumstances financial organizations are paying much attention to brand recognition, what I mean, they use name, logo and corporate colors to stand out. According to experts, it is not a coincidence: the client is influenced not only by the parameters of products, but also by the brand color scheme and brand’s personal perception. I have chosen leading Russian banks to investigate the banks’ color strategy.

Bright colors are preferred, when it comes to the development of the retail business. For example, the bank “Renaissance Credit” has chosen crimson color.

Another example is Bank of Moscowgraduallogo restyling. After 10 years of successful work the Bank of Moscow from a relatively small has become a universal bank, one of the leaders in Russian financial market. The main bank’s clientsare young people aged from 25 to 35.Thus in 2003 the bank decided to design a new modern logo. There is no much difference between old and new logos. The letter “M” has just changed the shape. According bank’s presidential adviser Mikhail Kamensky, new logo isa sign ofstrength and stability, as the quintessence of hard work and success.

Banks usually choose calm and solid color palette, if it is building long relationships with corporate clients. For instance, Sberbank has chosen green color as a corporate one not accidently: the analytics of the bank have found out that 87% of consumers associate green with money that by far increase brand attractiveness. Furthermore, if we look at Sberbank’s logo we can see yellow as a symbol of sunlight, the image of hope and trust. Moreover, much attention is paid nowadays to the growth conception. The Sberbank managers usually use images of different plants, pyramids and other figures built from money.

The main corporate colors of VTB Group are blue and white. These colors used to be corporate colors when it was established. During re-branding in the second half of 2000s VTB marketers wanted to save the bank image by leaving these colors as corporate ones. Moreover, the colors have not been chosen accidently: they correlate with bank strategy, its mission and values: blue as a sign of credibility and white as a sign of openness. Red is also a corporate color in some parts of the bank such as in VTB24, that provides services to private clients. What is more, the combination of red and blue means safety and strength. White color brings “peace” in the red-blue combination.

General for all banks nowadays both for advanced and developingis enrichment of color palette that correspond with bank’s strategy and missions.

## Conclusion

Color has become very important as more companies go global. Companies use colors to stand out. Colors can alter the brand’s perception Moreover, knowing one’s color preferences consumer behavior can be predict. That is why it’s extremely important to choose the right color.

To conclude with, Pablo Picasso said: “Colors, like features, follow the changes of the emotions.”

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# GLOBAL BANKING ENVIRONMENT: IMPENDENT COLLAPSE OR INESCAPABLE MODIFICATION

## Abstract

*Nowadays there are a lot of issues connected with instability of global banking system. In this research I have analyzed not only the overall situation but dwelled specifically upon banking environment of several countries, defining precisely the objective reasons for current banking crises all over the world. Accordingly, the research outlines both theoretical causes as well as practical outcomes of banking crises.*

***Key words:*** *banks, banking crises, financial crises, interest rates, government regulation, shadow banking*
***JEL codes:*** *E58, F01, G20*

## Introduction

Currently, financial crises are more likely to appear as a fairly and ordinary permanent feature of the economic cycle. However, it is extremely crucial to distinguish the term "banking crisis" from the financial one. There is a great definition of «major banking» crisis by professor Charles Calomiris from the Columbia Business School as «time when a huge amount of failure going on in the banking system or when banks aren't closing but people have stopped making payments to the bank, which forces the banks to look for another way to make payments on the loans people can no longer pay. In the end, the bank is usually closes» [1, 16]. In other words, it should be distinguished that banking crises can consist either of constant bank failures which usually have a negative impact on aggregate net worth of these institutes (in excess of 1% of GDP) or moments of panics about noticeable or unnoticeable aggregate shocks. The major difference between banking and financial crises is that unlike financial one, banking breakdowns cannot be determined just as an inevitable outcome of human activity or the liquidity transforming structure of balance sheets of a bank. Moreover, even severe macroeconomic environment is separately from other possible causes not sufficient enough to provoke banking crises.

One of the reasons to do a research of this kind was to understand why some countries have a stable banking system whereas the majority of others, including the USA, remain to be unstable?

Here is a quotation of Charles Calomiris, who said: «*You are living in the middle of the worst pandemic of global banking instability the world has ever seen.*

*There's no period in human history that is even close. If you look around the world since the 1970s, we've had over 100 major banking crises»* [1,37]. Unfortunately, it should be admitted he is right. Although, not every advanced country went through banking crises. For instance, let's have a deep look at two strong and solid superpowers such as the USA and Canada. Canada has plenty of banks and financial institutions and in the 20$^{th}$ century it experienced a major shock. Major shock means there time, when prices for basic commodities rose sharply and made everything too expansive for people to buy or even sell. As a result, both import and export industries suffered because they had problems with brining in foreign goods. When this has occurred in Canada, there was no banking crisis. In contrast, the USA had 17 banking crises despite being less dependent on exporting staple commodities than Canada. Practically, it means that Canada should have experienced much more shocks. That is a puzzle. Analyzing all potential causes for this puzzle will help to identify objective reasons for any banking crisis.

## Interconnection of politics and banking crises

Undoubtedly, politics plays a vital role when speaking about economic development and perspectives. According to Charles Calomiris, countries with higher incomes tend to have more credit than countries where incomes are poor. Namely, Japan and the U.S. have good proceeds, high credit and also have stable democracies. On the other hand, there are stratocracies like the Democratic Republic of the Congo and Chad that, in their turn, have low income, low credit as well as constantly fluctuating banking system. As an outcome, it can be seen that democracies are more likely to have strong banking spheres.

However, even banking systems of countries, which have the democracy as a political state system, can be ruined by an irrelevant or inaccurate government respond. To illustrate, there was a wise respond from the British government in the 19$^{th}$ century, when the government made a reform that was able to stop the bust cycles and booms that had attacked the economy for several decades. In contrast, counterproductive tools that had been taken by the US government in the same 19$^{th}$ century leaded to financial instability and further problems.

Thus, political environment and measures that are provided by the government influence critically the further development of the banking system as well as improving current instability in case of a need.

## Basic principles of banking crises

While preparing this research, I have indemnified four main principles of banking crises that are dependent on each other and create a circle.

1. Repetition

Banking crises have a tendency to happen after the lapse of periods of time. Economists normally refer them to declines in prices of assets and rises in the liabilities of failed firms. It is an interesting fact, that waves of bank failures are traceable to large drops in the values of bank loans which reflect decreases in the fortunes of borrowers.

2. Rarity

Historically, banking crises occur rarer than financial breakdowns. Nevertheless, it is a common fact that nowadays there are much more government interventions, that there was a century ago, designed to sustain stability of the banking system in various forms such as lending from the central bank or providing government-backed insurance of deposits etc.

3. Coincidence

Banking breakdowns can either coincide or cannot. Namely, in 1920s the USA experienced a wave of agricultural bank failures without systematic banking panic, while at other times bank failures may happen with such kind of panics like it occurred in the Panic of 1907. Hence, banking panics can be caused by small losses but may not result in a huge wave of failures; large losses, in their turn, could lead to severe waves of banking failures without any panics.

4. Differences in frequency

Interestingly, banking breakdowns of both kinds of crises discussed above vary in their frequency across time and across countries, and the differences in the propensities for breakdowns are dramatic. Historically, the U.S. banking system experienced an unusually high quantity of both waves and panics of bank failures. Nationwide banking panics happened in 1819, 1837-9, 1857, 1873, 1884, 1890, 1893, 1896, 1907, and 1933. The U.S. also experienced an unusually high frequency of severe waves of bank failures: in the 1830s, 1920s, and 1930s. England also suffered an unusually high propensity for banking panics in the first half of the 19th century, but experienced a dramatic change in its propensity for panics in the middle of the 19th century; banking panics occurred in 1819, 1825, 1836, 1847, 1857, and 1866, and then (with the exception of a crisis induced by the onset of World War I) there were none for more than a century. Only four countries experienced severe waves of bank insolvency worldwide in the years 1875–1913; in the period 1978–2009, in contrast, roughly 140 such episodes have occurred, more than 20 of which are more severe than any of the pre-World War I episodes in terms of negative net worth of failed banks relative to GDP.

Hence, banking crises are interconnected circle of various causes that are bound together with both political and economic environment.

## Current threats

1. Low interest rates

More than 20 central banks have already moved to cut interest rates this year as weak inflation outlooks have provided many economies with the room to ease monetary policy. But the OECD warns about an over-reliance on these “exceptional measures” to stimulate global growth, noting that low rates had failed to revive investment and heightened the risk of asset price bubbles.

*“Excessive reliance on monetary policy alone is building-up financial risks, while not yet reviving business investment,* said chief economist at the OECD, Catherine Mann. *“A more balanced policy approach is needed, making full use of fiscal and structural reforms, as well as monetary policy, to ensure sustainable growth and public finances over the longer term”*[5]. In other words, interest rates of this kind can push both economic and political stability to breaking point if Central Banks carry on providing the same policy.

2. Expansion of shadow banking

Despite witnessing the world economy and global financial system experiencing a total meltdown and despite multiple pledges from policy makers all over the world to ban shadow banking procedures, in fact, no steps have been taken at all. In fact, the world of shadow banking continues to expand and the total size of the shadow banking sector is expected to reach 100 trillion USD before the end of this decade (and very likely even sooner).

3. Inappropriate policy of Central Banks

In the beginning of this February, plenty of Central Banks have eased their monetary policies. For instance, Sweden’s Riksbank slashed its main rate into negative points. In doing so, it became the 14th central bank to ease monetary policy so far this year, but the first to actually take its “repo rate” below zero to –0.1pc. This means Sweden is actually charging its banks to lend money. In Britain, the same interest rate currently stands at a historic low of 0.5pc, but could be cut further. Switzerland and Denmark have already sent their deposit rates to –0.75pc to prevent currency appreciation and defeat deflation. Faced with the twins threats of deflation and economic stagnation, monetary policymakers are reaching for their interest rate levers and digital money-printing tools in a bid to stave off recessions and debt deflationary dynamics.

Here is breakdowns of the consequences that could emerge from these actions.

## Possible outcomes

1. International currency wars

“Competitive easing” among central banks has stoked fears of a return of international currency wars. The announcement of unprecedented monetary stimulus from the ECB and the Bank of Japan has led to the respective weakening of their exchange rates and prompted dramatic responses from the smaller central bank players. In Europe, the Swiss, Danish and Swedish authorities have all moved to impose punitive negative interest rates in a bid to prevent their currencies from rocketing in value. Denmark meanwhile, has been forced to lower rates four times in three weeks and purchase €32bn in foreign exchange to prevent the krone from developing into a safe haven for investors. Hence, these wars could ruin interconnection of banking systems and their relationships between each other. Separation is the critical thing to have in current unstable situation.

2. Divergence

The expectation of a normalisation of monetary policy by the Federal Reserve has resulted a sustained rally in the US dollar. Such strength in the world's reserve currency has simultaneously applied pressure on economies pegged to the greenback. Meanwhile rate hikes from the Fed — which are expected to begin later this year — will naturally leader to tighter monetary conditions in economies everywhere from Mexico to Hong Kong.

It is this divergence in the actions of the world's major central banks which could lead to a new global liquidity crisis, which means complete catastrophe.

## Conclusion

As it can be seen, the world is going to get to go through a tough crisis like in 2008, but I believe that this wave is going to be even worse than the previous one. Banking crises are not the same as financial ones, because in case there is a breakdown in financial system, banks are the first to maintain stability in the country. In contrast, if there is a banking crisis, everything becomes to look like a mess.

We are going to be in for quite a bumpy ride if governments and Central Banks all around the globe do not provide necessary measures and practices as soon as possible. There should be efficient collaboration of countries in order to get through it. So hold on tight and get ready.

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# JAPAN'S PUBLIC DEBT DYNAMICS

## Abstract

*The three-arrow strategy adopted by the Government of Japan in 2013 presents great interest for investigation. Each of the arrows of strategy should stimulate economic growth and reduce public debt of Japan. Japan's gross public debt has risen from 74% of GDP in 1992 to more than 245% today, and many experts forecast it over 250% of GDP in 2015. The article analyzes the dynamics of public debt and other economic indicators in Japan.*

***Key words:*** *gross debt, the three-arrow strategy, GDP growth, deflation*

## Introduction

Nowadays, many countries have a problem with a gross public debt. Japan is not an exception. More than that, Japan is the country that has one of the biggest public debts. Very high public debt is a serious problem for the government. Besides, a large primary deficit of the country, low growth and deflation make Japan lose market confidence. A sovereign debt crisis in Japan would be an important source of instability for the world economy. Japan's national debt service is ¼ of the total budget. For example, the expenditure on national debt service in 2014 was planned to reach the level of 24.3% of the total expenditure of budget [4]. The aim of the Japanese government is to reduce the budget deficit and boost nominal GDP growth to prevent the risk of debt growth. It can be achieved with the help of the three-arrow strategy announced by the new government in 2013 — flexible fiscal policy, structural reforms to boost trend growth and a higher inflation target — could help to reduce the debt over the medium term.

## Japan's gross public debt

As you can see at Figure 1, the growth of public debt and GDP has an inverse negative relationship. It means that with the slowdown of economic growth, the growth of the public debt of the country increases.

Japan's gross public debt has risen from 74% of GDP in 1992 to more than 245% today, and many experts forecast it over 250% of GDP in 2015 [1, 5]. Government debt (as a percent of GDP) is used by investors to measure a country ability to make future payments on its debt.

The increase in the debt over the past two decades is due to a combination of high primary deficits and high real interest rates relative to real GDP growth [2, 5]. The highest growth rate of public debt was in the year of 2009 when public debt increased by 9.6%. At the same time there was a decline of Japan's GDP by 5.5%. Since 2011 the rate of growth of public debt has started to decline, while Japan's economic growth has started to increase.

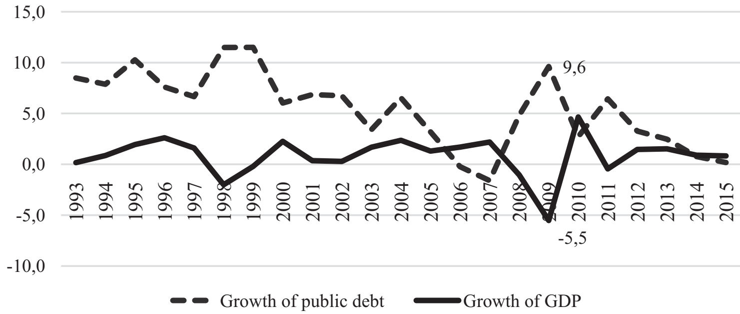


***Figure 1.*** The rate of growth of public debt and GDP growth

## The first arrow of strategy: the flexible fiscal policy

Japan's government announced the three-arrow strategy to reduce public debt. First, they want to have a more flexible fiscal policy. The main instruments of fiscal policy are the revenue and expenditure of the state budget. For Japan government the primary balance of budget amounting to 7.5% points of GDP would help to achieve the necessary consolidation of the budget [1, 7].

Government budget is an itemized accounting of the payments received by government (taxes and other fees) and the payments made by government (purchases and transfer payments). Budget deficit means that the government spends more money than it takes in. Due to it, the country has a very high public debt. At Figure 2, we can see Japan's budget deficit dynamics.

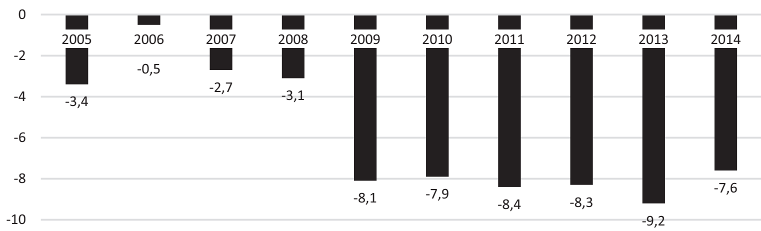


***Figure 2.*** Japan's budget deficit dynamics

Japan has run a primary budget deficit for 20 years. One fundamental factor behind structural deficit has been demographics, as population ageing tends to increase social spending and reduce tax revenue [1, 6].

Japan's budget deficit has risen from 3.4% of GDP in the year of 2005 to more than 7.5% today. The largest deficit of Japan's budget was in 2013, it was about 9.2% of GDP. For comparison with Russia it should be added that in 2013 Russia's budget deficit was at level of 0.5% of GDP [5].

## The second arrow: structural reforms

The second arrow of strategy presents structural reforms boosting trend growth. If the country has a faster GDP growth, it can reduce the growth of public debt. It directly increases the denominator of the debt-to-GDP ratio. Higher participation reduces the budget deficit and the rate of increase of the numerator. At Figure 3, we can see how budget deficit influences on GDP growth.

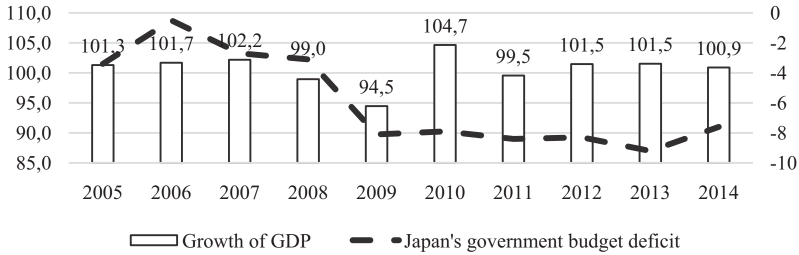


***Figure 3.*** The rate of growth of GDP and budget deficit of Japan

As we can see at the Figure 3, with the increase of the growth of budget deficit, the growth of the public debt increases too. For example, after financial crisis in 2008, budget deficit of Japan increased to 8.1% of GDP and at the same time the GDP decline to 94.5%.

## The last arrow of strategy: the end of period of deflation

The third arrow of the government's strategy is to end the period of deflation and target 2% inflation using monetary policy measures. Deflation is a decrease in the general price level of goods and services. Many economists believe that deflation is a problem in modern economy because it increases the real value of debt.

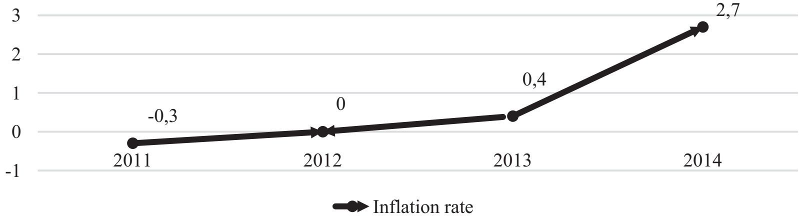


***Figure 4.*** Japan's inflation rate dynamics

As we can see at the figure 4, inflation rate was at the level of 2.7%. It was mostly achieved with the help of increase of sales tax from 5% to 8%. The inflation rate in Japan was recorded at 2,4% in January of 2015. Inflation rate in Japan averaged 3,2% from 1958 until 2015, reaching an all time high of 25% in February of 1974 and a record low of -2.5% in October of 2009. Inflation rate in Japan is reported by the Ministry of Internal Affairs & Communications [3].

## Conclusion

In conclusion, it should be mentioned that high gross public debt is a serious problem in any country. The governments need to deal with rapid rise of debt as it may prevent the growth of the national economy. As for Japan's public debt, many experts believe that the three arrows of the government's strategy could be successful in preventing the rise of public debt. Since 2011 the rate of growth of public debt has started to decline and Japan's economic growth has started to increase. Nevertheless, Japan's public debt would likely be above 200%.

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# THE IMPACT OF SANCTIONS ON THE ECONOMIC SITUATION IN RUSSIA

## Abstract

*In 2014, Russian economy experienced several negative shocks. In January and February the ruble exchange rate slightly decreased due to the fact that the program of quantitative easing of the US Federal Reserve began to reduce. Accession of the Crimea to Russia in March caused an immediate response from countries such as the USA, Japan, Canada and countries of the EU in the form of sanctions. These were the major reasons for the economic instability.*

***Keywords:*** *Russian economy, ruble exchange rate, quantitative easing, sanctions, economic instability*
***JELcodes***: *D740, H500, H 870.*

## Introduction

The annexationof the Crimea to Russia in March 2014, as well as the Russian government's assumed support of separatists in eastern Ukraine served as some kind of trigger for the United States and the European Union to introduce the first series of sanctions against Russia. The US government initiated the introduction of sanctions with the intention of internationally isolating Russia, and the EU had no choice but to join the US under the risk of incurring economic losses. Sanctions have also been supported by the Group of Seven — G7 (former G8) and some other countries, the partners of the US and the EU.

The EU and the US have ratcheted up sanctions several times, tightening restrictions on major Russian state banks and corporations. They have blacklisted dozens of senior Russian officials, separatist commanders and Russian firms accused of undermining Ukrainian sovereignty.All the people named on this list are now subject to Western asset freezes and travel bans.

Sanctions mainly target Russia's state finances, energy and arms sectors. Russian state banks are now excluded from raising long-term loans in the EU, exports of dual-use equipment for military use in Russia are banned, future EU-Russia arms deals are banned and the EU will not export a wide range of oil industry technology. Three major state oil firms are targeted: Rosneft, Transneft and Gazprom Neft, the oil unit of gas giant Gazprom. Yet the gas, space technology and nuclear energy industry are excluded from sanctions (for now), but there is a possibility that new EU sanctions may affect the supply of equipment for the gas industry. Still, the question is, how exactly have sanctions influenced the Russian economy and the lives of its citizens in general?As a matter of fact, sanctions have become one of the causes of the financial crisis in Russia and with no doubt it has had a significant negative impact on the Russian economy.Since autumn 2014, the ruble has been devalued by 50 percent against the US dollar, capital outflows have amounted to 51 billion dollars and, consequently, inflation has risen. Another contributing factoris the falling oil prices, which have now fallen so much that Russia's total export revenues this year will be two-thirds of what they have been before. That means that Russia will have to cut its imports by half. According to economic forecasts, the Russian economy will go into recession this year [2].

In January 2015 , the international rating agency Standard & Poor's (S & P)has lowered its long- and short-term ratings of Russia on foreign currency obligations from "BBB- / A-3" to "BB + / B", giving the country the level of non-investment rating with a negative outlook. Thus, for the first time in 11 years the country's rating reached a non-investment grade. Moreover, in the late February, the international rating agency Moody's downgraded Russia's sovereign rating to "Ba1" from "Baa3". Hence, the country's rating dropped to so-called "junk" level. Also, at the beginning of 2015, the international rating agency Fitch downgraded Russia's sovereign rating to 'BBB-' from 'BBB' with a negative outlook as well [4].

As for other economic consequences, Russian federal budgethad to be adjusted due to sanctions and economic slowdown. The government was forced to increase spending to support companies affected by the sanctions. The National Welfare Fund and pension savings of the citizens are the main sources of funds for the struggling companies [1].

## Implications for military and space industry

In general, beneficial effects of sanctions on the industry may be noted. In particular, new solutions have been introduced; standardization measures are performed at higher speed.The imposition of sanctions also accelerated the process of import substitution in the space industry. The government is now planning the production of such final products as launch vehicles, boosters and spacecraft. Under the terms of sanctions, Russia will buy the missing microelectronic components and tools from reliable suppliers in China, South Korea, India, Singapore and other Asian countries.

The situation with the military industry looks less promising. Alas, Western countries used to be the main suppliers of crucial details for production of Russian weapons, which significantly complicates modernization of Russian military production [3].

## Implications for the fuel and energy complex

Because of sanctions Oil Company "Lukoil" had to reduce its investment program, and also Lukoil's net profit decreased more than by half to the fourth quarter of 2014 compared to the previous year.The oil company "Rosneft" requested the government to provide financial aid in the amount of 1.5 trillion rubles to maintain liquidity.

Gas Company "Gazprom" was forced to optimize its pricing policy and geographically diversify its markets. The company also suffered from the ban on technologies that were needed for the production of oil on the Arctic shelf.

As a result of the sanctions, reduction in oil production in Russia can reach 7 percent per year [3].

## Tourism

It has not been a good several months for Russia's travel industry. Moscow has "advised" officials not to travel abroad, and in July 2014 banned public servants from travelling overseas on tickets paid for by foreign entities. As a result, demand for foreign travel fell by more than 50 per cent, estimated 4-5million foreign journeys by government employees have been cancelled, and a number of Russian travel agencies have gone bankrupt. Holidaying in Crimea has been suggested by the Kremlin as an alternative.

The number of tourists travelling abroad (especially in European countries) has dropped significantly, with some destinations' tourist flow having slumped between 20% and 50% against 2013. Experts see two reasons for this: reluctance to put up with outbreaks of Russophobic sentiment and the ruble devaluation against the euro [3].

## Citizens' income

This year could see the first decline in real incomes in Russia since President Vladimir Putin came to power with a social contract that promised rising wealth at the expense of full political participation. According to forecasts, GDP per capita will fall to $8,000-$10,000 in 2015, down from $14,000 in 2013. That, added to rising inflation, will mean ordinary Russian citizens start feeling an undeniable pinch in their own pocket.The imposed food embargo doesn't help either. It was introduced in August 2014 as a response to Western sanctions. Russia imposed a ban on agricultural imports from the EU, US, Norway, Canada and Australia. The embargo does not include New Zealand, Japan and Switzerland. The ban applies to imports of meat, dairy products, seafood, fruit and vegetables.

The total annual volume of imports, which fell under the sanctions, estimated at US $ 9 billion [3].

## The way out?

The Russian economy will have to endure a difficult period of adaptation to the new environment. For at least a year, economic growth rates will be negative while the possibility for a recovery will be highly dependent upon how soon a new equilibrium point is reached. If energy prices remain low while geopolitical instability and sanctions persist, negative economic dynamics will continue in the coming years.

There are some steps which Russia can take in order to improve current economic situation, or at least not to worsen it. First of all, what should be done is authorities should rethink and adjust its international policy. It is important to understand that despite the fact that mutual sanctions have been introduced against the US and European countries, the tension that exists between Russia and Western countries first and foremost backfires on Russia and its economy. Secondly, Russia should solve the problem of import substitution. By developing its own economy, the country will be less dependent on imports of goods and services from other countries.

Experts say that the current economic model in Russia is tied to world oil prices, and is only able to reproduce itself and crises. The suggestion is that Russia should use positive experience of other countries, such as, for instance, our partner China or Japan, to build a new economic model and change existing economic policy.

Summing up, it is clear that the problem is much more comprehensive and goes above and beyond temporary sanctions. Raising the country's economy to a new level and building industry is what Russia should aim for in long term run.

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# ECONOMIC COOPERATION BETWEEN GERMANY AND CHINA IN 2005–2013: THE EXPERIENCE OF QUALITATIVE AND QUANTITATIVE ANALYSIS

## Abstract

*This article concerns some aspects of economic cooperation between Germany and China. We compare the economic parameters of Germany and China as the actors of bilateral relations and give an assessment of the nature of economic cooperation between Germany and China in 2005–2013 through the analysis of the dynamics of trade turnover between them. Our research is based on the methods of qualitative and quantitative analysis.*

## Introduction

In our opinion, of all the more than 20-year old history of the modern system of international relations the most relevant for the study of the relations between Germany and China is the period, beginning with the year 2005. It was at this time, that the development of rapidly increasing world economy in the new millennium was interrupted, naturally but suddenly, by the global economic crisis of 2008, the effects of which continue to appear nowadays.

In this paper we compare the economic parameters of Germany and China as the actors of bilateral relations and give an assessment of the nature of economic cooperation between Germany and China in 2005-2013 through the analysis of the dynamics of trade turnover between them.

The research is based on the methods of qualitative and quantitative analysis.

## A comparison of the economies of Germany and China

At the beginning of 2013, Germany and China had the most powerful economies in their regions. Germany was the first economy in Europe and the fifth in the world and China was the first economy in Asia and the second (after the USA) in the world [1]. Both countries were at the top three by the volume of foreign trade turnover: China occupied the first place and Germany — the third [2].

According to the data, presented in Table 1 [3], we will make a more detailed comparison of both economies in 2012.

*Table 1*

**Key economic parameters of the FRG and the PRC in 2012**

| Parameters | FRG | | PRC | | Ratio |
|---|---|---|---|---|---|
| | Value | Rank in the world | Value | Rank in the world | PRC/FRG |
| Area | 357022 km$^2$ | 63 | 9596961 km$^2$ | 4 | 27 |
| Population | 81147265 | 16 | 1349585838 | 1 | 17 |
| Population density | 227 pers/km$^2$ | 36 | 141 pers/km$^2$ | 55 | 1/1.6 |
| Population growth | -0.19% | 211 | 0.46% | 154 | |
| GDP (PPP) | $ 3123 bln | 5 | $ 12380 bln | 2 | 4 |
| GDP (PPP) per capita | $ 38486 | 29 | $ 9173 | 122 | 1/4 |
| GDP growth | 0.70% | 171 | 7.8% | 18 | 11 |
| Inflation | 2% | 35 | 2.6% | 59 | 1.3 |
| Export | $ 1492 bln | 3 | $ 2050 bln | 1 | 1.4 |
| Import | $ 1276 bln | 3 | $ 1817 bln | 2 | 1.4 |
| Foreign trade turnover | $ 2768 bln | 3 | $ 3867 bln | 1 | 1.4 |
| FDI inflow | $ 6.6 bln | 40 | $ 121 bln | 2 | 18 |
| FDI outflow | $ 66.9 bln | 6 | $ 84.2 bln | 3 | 1.3 |
| FDI Confidence Index | 1.52 | 5 | 1.87 | 1 | 1.2 |
| HDI | 0.920 | 5 | 0.699 | 101 | 1/1.3 |

China has one of the largest territories in the world, exceeding Germany's territory by 27 times. The number of China's population, which occupies the top place in the appropriate rating, was 17 times more than the number of Germany's population. Because of the relatively large area, despite the enormous number of the population, population density of China was 1.6 times less than population density of Germany. Both countries have problems with population growth. In Germany, death rate exceeds birth rate. On the contrary, China has to restrain population growth, because, despite of the average rate of population growth, the population of China, because of its huge amount, is growing rapidly from year to year.

China's GDP at purchasing power parity (PPP) was 4 times more than German's GDP (PPP), but in per capita terms, we observe the reverse situation. Real economic growth in China was also visibly higher than economic growth in Germany — by 11 times. As for the levels of inflation, they were both low and almost equal: they varied 1.3 times in favor of Germany.

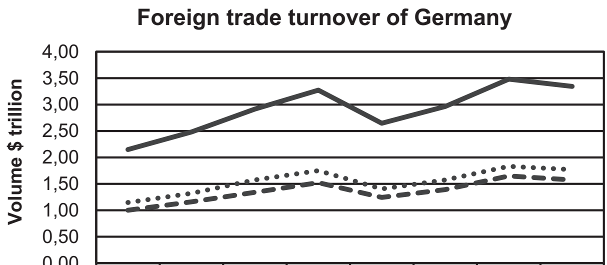
Both countries had the volume of export more than the volume of import, but both export and import of China was 1.4 times more than export and import of Germany.

In 2012, the inflow of foreign direct investment (FDI) in China was 18 times more than the volume of FDI, received by Germany. In the same year, China as an investor hold the third place in the world, exceeding Germany in the volume of outflow of FDI by 1.3 times. Both countries were reliable recipients of FDI, differing in the value of FDI Confidence Index by 1.2 times in China's favor.

Finally, the Human Development Index (HDI), as measure of the standard of living of the population, was considered very high for Germany and average for China.

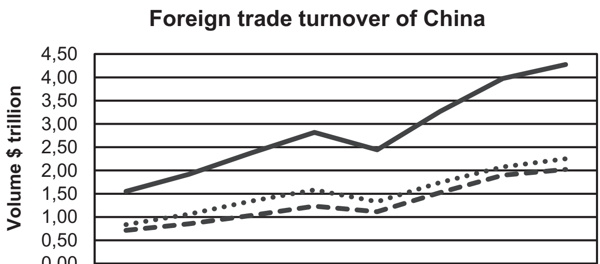
To compare the dynamics of foreign economic activity of Germany and China in 2005-2012, we will take their foreign trade turnover as the indicator.

We can see the qualitative nature of the development of foreign trade turnover of goods and services in the period under review in the graphs that are given in the corresponding figures (Fig. 1 for Germany and Fig. 2 for China) [4].




| | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|
| Export | 1,15 | 1,32 | 1,57 | 1,75 | 1,40 | 1,57 | 1,83 | 1,77 |
| Import | 1,00 | 1,16 | 1,34 | 1,52 | 1,24 | 1,39 | 1,65 | 1,57 |
| Sum | 2,15 | 2,48 | 2,91 | 3,27 | 2,65 | 2,96 | 3,48 | 3,34 |

***Fig. 1.*** Graphs of foreign trade turnover of Germany in 2005-2012




| | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|
| Export | 0,84 | 1,06 | 1,34 | 1,58 | 1,33 | 1,74 | 2,08 | 2,25 |
| Import | 0,71 | 0,85 | 1,03 | 1,23 | 1,11 | 1,52 | 1,90 | 2,02 |
| Sum | 1,55 | 1,92 | 2,38 | 2,82 | 2,44 | 3,27 | 3,98 | 4,27 |

***Fig. 2.*** Graphs of foreign trade turnover of China in 2005-2012

After having analyzed these graphs, we can say:

1. In both countries, after the global economic crisis of 2008, there was a decline of foreign trade turnover, but the fall of turnover for China was visibly lower than for Germany.
2. From 2009 to 2011, both in Germany and China, we can see the rise. China's turnover was growing faster, Germany's turnover — slower.
3. After 2011, when the second wave of the crisis started, the rise of China's turnover slowed, and turnover of Germany began to fall again.

Obviously, China's foreign trade turnover, compared with Germany's foreign trade turnover, has shown greater resilience towards the global economic crisis.

## Some aspects of economic cooperation between Germany and China in 2005–2013

As of 2013, Germany was the largest trading partner of China in Europe and the sixth trading partner in the world, and China was the most important trading partner of Germany in Asia and the third trading partner in the world [5]. In 2013, the volume of trade turnover between Germany and China was \$ 187 billion: goods were exported from Germany to China by \$ 89 billion, from China to Germany — by \$ 98 billion [6]. Germany imported from China mainly data processing equipment, electrical and optical goods, clothing, electrical equipment, equipment for machinery and metal products, while China imported from Germany mainly cars and spare parts, machines, data processing equipment, electrical and optical products, electrical equipment and chemical products. Germany was also the largest investor in China, taking the first place among the EU countries and the second place in the world after the USA in the investment volume in the Chinese economy. The investment volume of German companies in China greatly exceeded the investment volume of Chinese companies in Germany: at the beginning of 2012, the ratio was € 35 billion of German investment against € 1.2 billion of Chinese investment [7].

Leaving outside our investigation other aspects of economic relations between Germany and China, we will focus on the study of the dynamics of their economic cooperation, beginning with 2005. As a quantitative indicator, reflecting the dynamics of economic cooperation, we will consider the dynamics of trade turnover between the countries. For a better understanding of what has happened for the last nine years, we will take into account the dynamics of trade turnover between Germany and China, beginning with 2000.

The graphs, showing the dynamics of trade turnover, are presented in Fig. 3 [6].


| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Export | 8,66 | 10,8 | 13,8 | 20,6 | 26,0 | 26,3 | 34,6 | 41,0 | 50,1 | 52,2 | 71,2 | 90,2 | 85,7 | 89,0 |
| Import | 17,0 | 17,8 | 20,2 | 29,1 | 40,8 | 50,6 | 62,8 | 77,4 | 88,8 | 79,2 | 102, | 110, | 100, | 97,4 |
| Turnover | 25,7 | 28,7 | 34,0 | 49,8 | 66,9 | 76,9 | 97,4 | 118, | 138, | 131, | 173, | 200, | 186, | 186, |

*Fig. 3.* Graphs of trade turnover volumes between Germany and China in 2000-2013

Basing on the nature of these graphs, we can say:

1. The potential for the development of trade turnover between Germany and China in 2005–2013 was laid at the beginning of the new millennium. Despite the waves of the global economic crisis in 2008 and 2011, the trend of growth of the trade turnover volume, which had taken place before 2005, had also remained for the next nine years. For both of the time intervals — 2000–2004 and 2005–2013 — the trade turnover between the countries has grown equally — by 2.6 times. In absolute terms, for the years 2000–2004 the trade turnover has grown by $ 41 billion, and for 2005–2013 — by $ 126 billion.
2. Both waves of the global economic crisis affected the trade turnover volumes between Germany and China. In 2009, there was a decline by $ 8.3 billion, and in 2012 — by $ 15.4 billion. The decline in 2009 was replaced by rapid but not long growth in 2010: during the two years the trade turnover increased by $ 74 billion. Germany had made a greater contribution to declines because of the decrease of its purchasing power, and a greater merit in the growth belonged to China, the purchasing capacity of which was higher.
3. The volume of trade turnover between the two countries in 2013 remained practically at the level of 2012. The volume of Germany's export (China's import) slightly increased, while the volume of Germany's import (China's export) slightly decreased.

## Conclusion

The main conclusions of our research are the following:

1. At the beginning of 2013, the FRG and the PRC were the most influential actors in their regions: Germany in Europe, and China in Asia.
2. In 2012, despite the multiple superiority of China's economy over the economy of Germany in many parameters, the standard of living in Germany was significantly higher than the standard of living in China.

3. During the global economic crisis of 2008, China demonstrated greater stability than Germany.
4. From the analysis of the export-import dynamics of goods through 2005-2013, it follows that, as a whole, the trade turnover between Germany and China kept developing, despite some temporary regress caused by the global economic crisis. The regress was due to the decrease of purchasing power of Germany, and China made a greater contribution to the growth.

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# THE ROLE OF REAL OPTIONS IN UNBALANCED ECONOMY

## Abstract

*The report considers the connection between types of real options and project risks. The most important risks in unbalanced economy were pointed out. Sector analysis of project risks and real options was provided. Empirical evidence for the results of the real options theory was analyzed as well. The report will be useful for people interested in investment planning.*

***Keywords:*** *real options, decision analysis, risk-management.*
***JEL codes:*** *G300, G310.*

## Introduction

The ability to change investment decisions according to new information can add value to the project. In these situations such valuation criteria as net present value and internal rate of return can undervalue some investment projects. Traditionally managerial flexibility can be valuated with the help of real option models or with the help of decision trees.

Managerial flexibility generates value in the situations when uncertainty is high. Managerial flexibility can be found in R&D projects, in oil and gas sector, in energy sector, in information technology, in agriculture, in building industry. Also real options should be considered during valuation of the innovation projects.

The goals of the report include the analysis of the connection between real options and project risks, sector analysis of real options and the overview of the empirical studies of the existence of real options.

## The basic concepts of real options

Operational flexibility is the ability to react on project risks and to change project plans according to them. Such opportunity can be considered as an option. Many strategic business decisions contain the features of the real options.

"A financial option is the right but not the obligation to buy or sell a certain security at a certain price at a certain moment" [4, 30].

A real option is the right but not the obligation to change investment decision according to new information [4, 30]. The investor executes a real option when the investment decision is changed. Both financial and real options have similar functions, as they help to hedge project risks.

The value of real option can be considered as the difference between active net present value of the project and its passive net present value. Active net present value is the NPV of the project, including the ability to change investment decisions and react on risks. [7, 20] Passive NPV of the project is the NPV, which doesn't include the ability to react on project risks. [7, 25] The value of the project is increased, because the investor is able to manage the uncertainty.

Financial options can be valued with the help of such methods, as analytical formula, introduced by Black and Scholes [4, 35], binomial trees introduced by Cox, Ross and Rubinstein [4, 37] or by imitation modelling. These methods have their strong and weak points. For example, analytical formula are complex, but they give the most exact estimation of the real options value. Imitation modelling is not so exact, but much more flexible.

In some cases the tools of financial option valuation are not able to evaluate real options correctly, because not all preconditions of financial options remain in the case of real options.

For example, real options may include several sources of uncertainty. Such options are called rainbow options and should be valued by special formula for rainbow option valuation.

Real options in multistage projects should be valued as compound real options. Compound option is an option on an option. The first formula of compound option valuation was introduces by Geske [3,10]. Compound and rainbow options can be valued by modifications of analytical formula and binomial tress, but the most common method used to value financial options is imitation modelling. The examples of compound option valuation can be found in the works of Cassimon [3, 15] and Sereno [9,17]. Shcwartz has built the model which valuates R&D project as a rainbow option [10, 9]. Multistage projects including operational flexibility can be considered as dynamic programming models [1,5].

However, the models of real option valuation are not widely used because their application in practice can be connected with some problems.

Firstly , the models of the real option valuation can be too complex. The computations may be too complicated or the result of the estimation can be difficult to interpret.

Secondly, the lack of available data can make the estimation impossible. Low quality of available data can make the result of the estimation unstable. This makes it difficult to take correct investment decisions.

## Real options and project risks

Project risks can be divided into external and internal ones. External project risks include such risks as macroeconomic risks, market risks and state regulation risks. Market risks can be divided into price risks, market requirement risks and risks connected with competition. State regulation can also influence on market requirements. Internal risks include risks, connected with project performance, costs risk and human resource risks.

Very often different project risks can be interconnected and generate several real options.

Risks can be also divided into positive and negative ones. Negative risks include the decrease of the project net benefits according to stochastic factors and positive risks include some new project opportunities.

Different types of real options can be used to hedge these project risks. The main types of real options will be discussed in this part of the article.

An option to abandon considers the ability to kill the project. For example, the project can be abandoned in the case of low demand for production. This option can help to manage such project risks as market requirement variability and project performance variability. The option to abandon exists when there are no log-term contracts with customers.

An option to defer investment considers the ability to wait and to observe the market situation. It can help to react on the changes of demand, on price changes and on changes of market requirements.

The options to expand and to contract the project according to the fluctuations of demand on production can hedge market risks. The scope of the project can be changed according to new market conditions or due to changing macroeconomic situation.

The option to switch considers the ability to change the technology of production either the type of the product sold, or turn to the other suppliers of raw materials. It gives the opportunity to optimize production costs or to react on changing market requirements. The option to switch exists when the technology is flexible or when the equipment is multifunctional.

The option to temporarily stop the project, for example, according to decrease in demand can be very important during the time of economic crisis. The option to stop the project commonly is considered together with the option to restart.

The options to pilot and to stage can help to hedge the risks of uncertain project performance, particularly, technological risks. They give the investor the opportunity to resolve some sources of uncertainty when the project is realized, to find the strong and weak points of the project and to improve the situation.

Unbalanced global economy leads to increase of macroeconomic and political risks. International markets for commodities become unpredictable due to fluctuations of currency rates. Market requirements also change, particularly as a result of political situations. This makes important the option to abandon, the option to stop, the option to expand and to contract.

On the one hand, rapid technological development takes place. On the other hand, the markets for technologies suffer because of administrative barriers, asymmetric information and political conflicts. This leads to increase of technological risks. As a result such real options, as the option to pilot and to stage become vital for some investors.

Switching options become important as a result of increasing market and technological risks.

## Sector analysis of real options

Oil and gas industry is characterized by two main sources of uncertainty: the uncertainty of oil and gas prices and uncertainty of oil and gas reserves [8,10]. The projects in this industry can be divided into three stages: exploration, development and extraction. Geological uncertainty is resolved after the end of the first stage. The option to abandon is important because of this type of uncertainty. The options to defer and to stop can help to manage the risk of price fluctuations.

These real options should be considered while project planning, because price uncertainty has increased due to current economic situation.

The projects in information technology can be characterized by project performance uncertainty and market requirement uncertainty. The ability to divide project into manageable chunks, to stage and to pilot can help to hedge these risks. They allow the manager to improve It -service if it has serious drawbacks. The option to stage can also deal with such risks, as changing market requirements, as well as the option to defer. But the risk of competitors' preemption decreases the value of an option to defer [2, 20].

R&D projects can be characterized by uncertainty of project performance, demand uncertainty and costs uncertainty. The options to defer, to abandon and to switch can manage project risks in R&D, as well as the options to stage and to pilot. The sources of uncertainty in research and development projects and their influence on project value were studied by Huchzermeier and Loch. [7,10]

Projects in agriculture can be characterized by cost uncertainty, demand uncertainty and product performance uncertainty as well. Product performance uncertainty has increased nowadays because of climate changes. Market requirements can be changed due to state policy. The projects in this sector are characterized by the option to expand, the option to contract and the option to switch.

## Empirical evidence of real options

The empirical analysis of real options is provided in figure1.

There has been found an empirical evidence of the results of the real options theory in natural resource sector and in information technology. Moel found, that the decisions to open and close gold mines are influenced by the dynamics of gold prices [5, 10]. This result can be explained by the real options theory. The existence of real option to defer in oil and gas sector was found by Sabet [8, 17]. He tested the impact of oil and gas prices volatility on firms' value. The evidence of the options to switch, to stage and to pilot in information technology was found by Benaroch [2, 5].

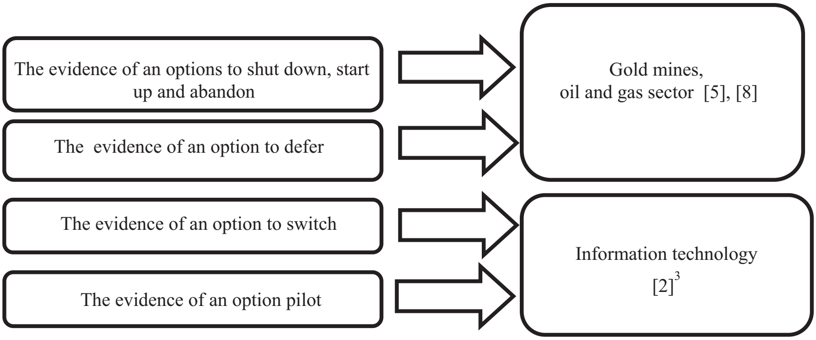


***Figure 1.*** Empirical evidence of real options in different sectors

Few studies test the results of the real options theory empirically and not all of the results can be tested directly, as a result of the complex models and the lack of the available data. Case studies can be more useful in analyzing the work of real option models in practice.

## Evidence for further research

The opportunities for further research can be pointed out according to provided sector analysis and overview of empirical studies.

For example, the empirical analysis of options to switch and to change the scope of the project can be provided. The analysis of these options in agriculture can be made with the help of the case studies.

Behavior of large multinational companies which open and close subsidiaries in different countries can be discussed from the position of the real options theory.

Different models of real option valuation can be built, for example models considering multistage projects as compound options. The impact of signals on the execution of real options can be studied.

## Conclusions

The ability to change investment decision according to current situation can add value to the projects, because it helps to react on changes and effectively manage them . This flexibility is the right but not the obligation and can be valued as an option.

Real options can be considered as the instruments of hedging project risks. The role of real options is increasing as a result of increasing project risks in unbalanced global economy. Types of real options in different industries depend on specific sector risks. The fact that real options create value can be observed empirically.

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# DOES INFLATION TARGETING MATTER?

## Abstract

*Today inflation targeting is the state of the art of monetary policy in many countries. By now researches have reached the consensus about the lowering impact of inflation targeting on inflation. Implications for growth, however, are less clear-cut. Starting with the brief overview of theoretical and empirical literature the estimations of inflation targeting impact on the output growth are presented. Several methods, including general method of moments (GMM) for dynamic panel data and propensity score matching, were used in estimation. Strong beneficial effect of inflation targeting on the output growth in advanced economies and no significant impact in emerging economies were found. Peculiarity of this paper is to avoid all technical complications of the methods employed and to focus on the intuition behind the estimation technics.*

***Key words***: *monetary policy, economic growth, inflation targeting, panel data*
***JEL codes:*** *C23, E52, O42*

## Introduction

Most modern central banks incorporate some version of price stability among its objectives. Sometimes an explicit target for the inflation rate is set and the monetary authority is responsible to follow this target.

Inflation targeting is a framework rather than a rigid set of rules for monetary policy. To be more precise, the famous inflation targeting policy consists of the following elements [4]:

1. Price stability is explicitly recognised as the main goal of monetary policy.
2. There is a public announcement of a quantitative target for inflation.
3. Monetary policy is based on a wide set of information, including an inflation forecast.
4. Transparency.
5. Accountability mechanisms.

Of course, when the central bank makes the decision to start the transition to inflation targeting, the question about possible consequences for the economy arises. By now consensus among economists about the lowering impact of inflation targeting on inflation is reached. Implications for real economy, however, are less clear-cut. Subject to different samples and methods employed researchers came to sometimes opposite results.

In November 2014 the Bank of Russia officially stopped pursuing the policy of managable floating exchange rate and formally let the ruble float freely. By doing so, our central bank started the transition to inflation targeting regime.

The question of whether the starting date of this transition was chosen correctly is left beyond this paper. However, understanding the expected consequences of this policy is an extremely topical issue for Russia.

In the existing literature one of the most popular analysis concerning the effects of the inflation targeting is the investigation of how this regime influences inflation and output growth.

Of course, there are reams of papers that try to analize other possible consequences of inflation targeting, such as its impact on variability of mentioned variables, expectations, exchange rate volatility and long-run interest rates [3].

Some researchers propound, as well, the considerable charachteristic of each monetary policy regime — its duration [5]. As for inflation targeting, this regime has undoubtedly withstood the test of time. In fact, no country so far, that adopted the inflation targeting, has abandoned it. The absence of any obvious international costs of such remarkable policy should be pointed out: inflation targeting countries have lower exchange rate volatility, less frequent «sudden stops», no specific international reserves or current accounts [7].

The apparently most important linkage of IT regime with output performance, especially concerning its growth, has not been investigated fully due to several reasons. First and foremost, this type of policy has been implemented in some countries only for a considerably short period. The first country that chose to target inflation was New Zealand in 1989. At the beginning of 2000 there were only 15 countries in the world with such monetary policy regime, most of them have just implemented it. That is why the room for empirical researches at that time was very restricted because of unavailable data. Secondly, the researchers have not reached the consensus about such a topical question so far.

## Theoretical mechanisms

From the theoretical point of view, the DSGE model is the most widespread framework for analysing this question. According to many papers, the effect of inflation targeting on output growth is positive, though there are also some counterarguments for such conclusions.

Here are some mechanisms of beneficial impact of infaltion targeting on growth. Annicchiarico, Pelloni, Rossi consider New Keynesian model with endogenous growth [2]. They find that the nominal volatility is detrimental to growth, as it causes the inflation fluctuations that raise the firms' uncertainty about expected price level. As a result, to mitigate this uncertainty firms increase the price markups and the output and investments fall. Inflation targeting has positive effect on growth through elimination of nominal volatility.

Annicchiarico also proposes another mechanism in New Keynesian model with endogenous growth and knowledge spillovers [1]. The positive production shocks in the economy, where the central bank is strictly focused on inflation targeting and ignore any output deviations, lead to increase in investments on the one hand. On the other hand, households increase the working hours in order to stimulate growth-enchancing activities, especially at the first stages of transition to new equilibrium. Both factors increase the economic growth.

## Empirical technique

Empirical literature on this topic is more controversial. Notwithstanding, while the final conclusion might still be debatable, the partial consensus apparently suggests that inflation targeting has different impact on the developing and developed countries. Using different methodologies and samples researches found the variety of conclusions concerning the impact of inflation targeting on the output growth.

In this paper, the crucial and still topical question of inflation targeting impact on the output growth is discussed. This issue is worth to consider at least due to availability of new data.

Theoretical literature reveals the existence of the mechanisms and channels through which inflation targeting, having the monetary nature, might affect the real economy. Empirical investigations provide the instruments and methods that can be employed to find the effects of inflation targeting. They are:

1) Ordinary Least Squares on cross-sectional data
2) General Method of Moments for dynamic panel data
3) Propensity score matching

All these methods were used to estimate the impact of inflation targeting on the output growth. One should distinguish between advanced and developing economies because of large differences in initial conditions and trends in inflation rates and output growth rates between these two groups.

## Results

The simplest econometric method for estimation of casual linkages, in this case the impact of inflation targeting on the output growth, is the Ordinary Least Squares (OLS) method. Regressions with GDP growth as dependent variable on dummy variable of inflation targeting and other controls were run. Consideration of two periods (for robustness of results) 2001-2011 and 2002-2012 leads to the following conclusions. Inflation targeting policy is beneficial for growth in advanced economies. However there is no evidence on any significant impact of this policy on the output growth in emerging countries.

Two issues must be highlighted here. Firstly, the quality of models on cross-sectional sample of countries, that are undoubtedly hugely heterogenous, is not very high. The sample of advanced economies contains only 34 observations, very few for reliable model. The goodness of fit that regression models have on the sample of emerging economies is also low. Secondly, due to aforementioned heterogeneity (countries differ in many aspects), the estimated coefficient of inflation targeting regime might mean completely different effect, for instance the level of central bank independence. That is why data with more complex structure and more sophisticated methods must be applied to the issue of inflation targeting.

Next method that was used to estimate inflation targeting impact on the output growth is General Method of Moments (GMM). The detailed description of GMM is very complicated; GMM is sometimes referred to as the black box method — a few researchers fully understand how this estimation actually works. This method implies the following idea. OLS minimizes the sum of the squared errors. 2SLS (Two Stage Least Squares) can be implemented via OLS regressions in two stages. But there is another, more unified, way to view these estimators. In OLS, identification can be said to flow from the assumption that the regressors are orthogonal to the errors; the inner products, or moments, of the regressors with the errors are set to zero [6].

However, an ambiguity arises in conceiving of 2SLS as a matter of satisfying such moment conditions. What if there are more instruments than regressors? If we view the moment conditions as a system of equations, one for each instrument, then the unknowns in these equations are the coefficients, of which there is one for each regressor. If instruments outnumber regressors, then equations outnumber unknowns and the system usually cannot be solved. The specification is then overidentified. Because we cannot expect to satisfy all the moment conditions at once, the problem is to satisfy them all as well as possible in some sense. To measure the deviation of the system one uses special metric.

Why is it necessary to use such overcomplications? The model is specified so that the dependent variable — output growth — is regressed on its own lag. So the assumption here is that it is more likely that country with high growth last year, say 7–8%, will also have high growth this year, say 5–6% but not 1–2%. This specification implies that commonly used methods for panel data such as models with fixed and random effects give inconsistent estimators and more complex methods have to be applied.

The results that give the GMM estimations are in line with the cross-sectional analysis for advanced economies. Inflation targeting policy is beneficial for growth, however it is worth mentioning that this positive impact appears only in three years after adoption. In emerging economies threre is some evidence that inflation targeting policy might negatively affect the output growth.

Finally, the propensity score matching methodology was implemented. This approach was adopted from the unfamiliar to economists fields where one can conduct experiments and use control groups, such as medical drug trials or job-training programs. One can think of the adoption of inflation targeting regime as a treatment applied to a group of countries at different times. In order to reveal the effect of such treatment on the output growth, one can construct a group of "control" countries and years — countries and years that had similar characteristics to countries that adopted inflation targeting in the year they adopted it, and as a result had similar probability of adopting inflation targeting regime, but did not adopt the regime. Then growth outcomes for treatment and matching control groups of countries can be simply compared.

At the first glance it appears that adoption of inflation targeting increased GDP growth rate in advanced economies from the average growth 3 years prior to average growth 3 years after policy adoption by about 1.2 percentage points and did not make much different in GDP growth rate of developing economies (Figure 1). Such simple comparisons, however, can be misleading, because many other factors affect GDP growth.

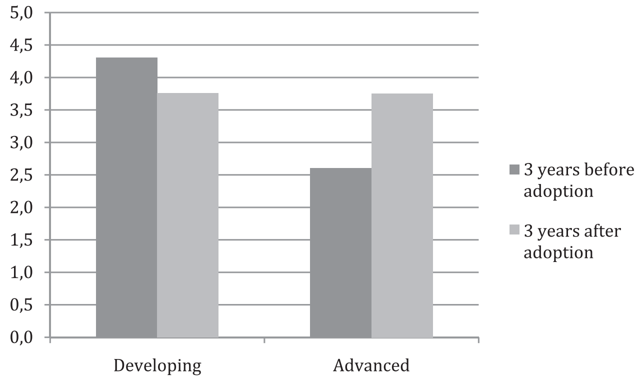


***Figure 1.*** GDP growth in countries that adopted inflation targeting

Figure 2 shows the results of propensity score matching implementation. It presents changes in GDP growth rate from the average rate in three years prior to the inflation targeting adoption (or non-adoption, for the control group) to the three years following the adoption, in percentage points.

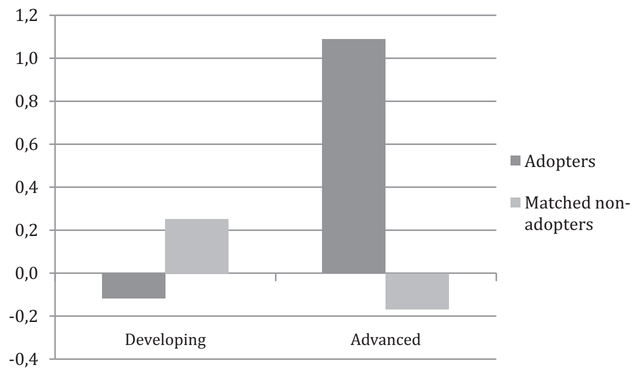


***Figure 2.*** Change in GDP growth rate from 3 years before to 3 years after the adoption

For advanced economies that adopted inflation targeting, there was a substantial increase in the GDP growth rate, while there was no change for the control group. The effect was much less pronounced for the emerging economies: developing economies that chose to target inflation observed even a decrease in the output growth. However, statitiscally speaking, this contraction in GDP growth cannot be counted as negative — it is simply insignificant or cannot be distinguished from zero.

## Conclusion

This paper presented the estimation results of how the inflation targeting policy might affect the output growth. Three methods were used to evaluate this effect: OLS, GMM and propensity score matching. The results, consistent with the literature, suggest that in advanced economies inflation targeting policy not only helps to tame the inflation but also stimulates the output growth. However, in emerging economies the analogous favorable effects of this policy are not pronounced. One possible explanation lies in the contractionary nature of inflation reduction that brings to nought benefits for real economy that arise from inflation stability and reduction of uncertainty associated with inflation targeting regime.

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# EUROPEAN BANKS WIN FROM THE CRISES IN EMERGING MARKETS

## Abstract

*One of the most crucial problems that European banks are facing now is emerging-market risk. It can materialize through different channels, but the most possible ones – are geopolitical risk and the global economic slowdown. Geopolitical risk arises, due to the fact, that a lot of European banks have subsidiary banks in such emerging countries, as Russia, Ukraine, Turkey and China. The uncertainty in economic development and political instability in these nations influence negatively the activity of European banks. The forecast of the global economy reveals, that despite the support from some accelerating factors, the rate of the economic growth in the Euro Area will decrease in 2015 by 0,2%. This economic slowdown and the impact of the emerging countries both have a negative effect on the banking sphere of the European Union. However, various crises in above mentioned countries have a positive influence on the economy of the European Union as well, as depositors prefer more stable European banks and investors select European bond market.*

***Key words:*** *emerging-market risk, geopolitical risk, asset quality, outflow of funds, euro depreciation.*
***JEL codes:*** *F 29, G 21*

## Introduction

In January 2015 the European Banking Authority published a report about risk assessment of European banks. The European Banking Authority is an independent organization, the aims of which are to maintain financial stability in the countries of the European Union and to preserve the efficiency of the functioning of the banking sphere. Despite the fact that EBA is independent, it is accountable to the European Parliament and the European Commission [9].

It is common knowledge, that banking sector in all countries is usually subject to various types of risks, for instance, credit, operational or systemic risks. The European banking sector is not an exception. The major risk for the European banking system in 2014, according to the EBA, is the emerging-market risk. This was acquired from the result of the survey of both European banks and market analysts. The survey, conducted by the European banking Authority reveals, that over 45% of responders admitted, that they consider the emerging-market risk the most important risk for their institution in the next 6 month. Furthermore, the number of banks, agreed with this statement, increased within the period from June to December of 2014 [2, 7]. The survey reflects, that as of December 2014 the most possible channels through which this risk can materialize are geopolitical risk and risk of the global economic slowdown. In order to better understand the mechanism of the emergence and development of the risk, it is preferable to study the influence of these two channels on the European banking system separately.

## Geopolitical risk

Considering the most serious geopolitical problems of nowadays, one can come to the conclusion, that they are connected with such countries, as Russia, Ukraine, China and Turkey. All of these countries have experienced an economic slowdown or, as in case of Ukraine even a crisis. This assumption is based on the following facts. Russia is weakened with financial and technological sanctions and also with lower oil prices. Ukraine is under the threat of the civil war and in order to survive, it runs into debts, asking the tranches of credits from the European Union, the Word bank and the International Monetary Fund. If we look at China we can see, that the economic slowdown in it is a planned step of the Chinese president. His aim is to implement a consumer-driven economic model, that demands lower, but more sustainable rate of economic growth. As far as Turkey is concerned, there is an unstable political situation in the country. It was caused by a mismatch in the policies pursued by the president and by the prime-minister [7]. Of course such unstable political situation has a negative impact on the economic sector. Because all the above mentioned countries referred to as emerging economies, are engaged in international trade, it is obvious, that the geopolitical risk for such active market participants, as the members of the European Union, stems from uncertainties in the developing countries.

Now let us turn to the nature of the risk itself. All types of banking risks can be classified into three groups based on the underlying indicator involved in the risk. These groups are: capital, liquidity, funding and environment risks. As far as the geopolitical risk is concerned, it belongs to the category of the capital risks, because of the bank capital risk exposure [1, 4]. In order to better understand the influence of the capital risk upon the activity of a bank, it may be further subdivided into such banking issues, as the asset quality and the volatility of decreasing market liquidity. Asset quality, according to the results of the survey of banks and market analysts, remains the most important issue. Increasing imbalance in the economy of emerging markets and lower growth rate prospects in the European Union only intensify the problem. The second issue for banks is the market volatility, which arises when as both banks and financial markets are vulnerable to asset price alterations and to decreasing market liquidity. Despite the fact, that the asset quality is determined as a high level indicator with a stable trend and market volatility is referred as a medium-leveled risk, the second index, unlike the first one, has an increasing trend and may be in the nearest future it will pass the factor of the asset quality. Given the foregoing, we can arrive at the conclusion, that the geopolitical risk affects such important indicator of the bank activity, as capital.

### Negative impact of emerging-market risk

It is a well-known fact, that each issue has both a positive and a negative impact. In reality every theory is far more complex than just black and white. On the one hand, the increasing instability in emerging markets cause grave problems for European banks, because many of them have established subsidiary banks in emerging markets. So if the economic situation in a country is unbalanced it immediately leads to the problem of bad loans. A loan can be qualified as a bad one, if repayments are not made as originally agreed between the borrower and the lender and if there is a threat of non-payment [3]. So due to the reasoning above, these institutions suffer more if geopolitical tensions increase. More than that, political relationship between different states can dramatically influence the performance of a bank. Best of all this statement is illustrated by the example of economic sanctions imposed on Russia by the United States of America and the European Union. On the March, 6 2015, the United States of America froze assets of three Russian banks. The whole sum of assets amounts to 640 million dollars [6]. If Russia in response to these actions freezes the assets of American and European banks, the European, especially French banks, will suffer the most. The reason for this assumption lies in the fact, that French institutions have invested about 51 billion dollars in Russia in the form of a credit and an acquisition of securities. One can assume, that Italian banks are in the similar situation as French ones. The banks of the Apennine Peninsula have invested 28,6 billion dollars in Russian securities. Taking into account, that absolute indicators are not so representative, because banking sectors in individual countries have different size and capacity, it is better to study relative ones, that are represent the proportion of investments into Russia, compared to the total amount of assets in a banking sphere of each particular country. The share of all banking assets of Austria located in Russia is approximately 1,4%. The banking sector of France is larger, that is why the share of assets invested in Russia is only 0,5% [5]. For other stable European countries risks, that are connected with the Russian Federation, are very small and amounts to only about 0–0,2%.

Considering the European banks investments in the Russian economy, it should also be noted that in addition there is a systemic risk as all assets are deposited with the limited number of banks. The similar condition can not be only connected with the situation in Russia. European banks have invested their assets in other emerging markets too.

### Positive impact of the crises in emerging markets

On the other hand, as it already been mentioned, the crises in developing countries can also have a positive impact on the economy of the European

Union, as depositors prefer more stable European banks and investors select European bond markets. This statement can be proved with the facts, that, firstly, within the 2014 year there was an outflow of 1,9 billion dollars from the funds, investing in the securities of the Russian Federation. What is more, according to the statistics, only in the first week of January 2015 2,7 billion dollars were withdrawn from the funds of emerging markets. It is a very representative example of how investors leave developing countries in a such short period of time. Speaking about the 2014 year the outflow of capital from emerging market funds amounted to 25,8 billion dollars [4]. As is known, Asian countries suffered the most. All the capital, withdrawn from the emerging markets, that afterwards became temporary available funds, could be and most likely was invested in the European bond market. More than that, it is necessary to add, that financial markets in emerging economies are not so developed and sophisticated, as in the European countries. Most foreign investors on the Russian security market pursue the aim of gambling rather than any long-term go. Secondly, the total amount of assets and loans in the banking sphere of the European Union increased from December to June 2014. Stability of the European banks attract depositors from all countries around the world.

## The risk of the global economic slowdown

As far as the other channel, through which the emerging-market risk can materialize, it is concerned with the global economic slowdown. According to the IMF report on January, 20 2015 the global growth forecast for 2015 year declined by 0,3%. Despite the lower oil prices, further monetary policy easing, the euro depreciation and more neutral fiscal policy the rate of the economic growth in the Euro Area in 2015 will decrease by 0,2% and by 0,3% in 2016 [8]. It is indicative, that the only country that has a positive forecast is Spain.

Speaking about emerging markets and developing economies the growth rate is even worse: –0,6% for 2015 and –0,5 for 2016 [8]. The reasons for this worsening situation are the slowdown of investments to China and the weakness of Russian economy. Naturally, the decline in the economic growth rate of a country has a negative impact on the banking sector of a state. As the result of the world economic instability, the IMF also predicts a decline in the investment activity in the Europe. This fact may be supported by the example, that was given speaking about the withdraw of funds from the emerging markets in 2014. So no one can forecast, whether this future slowdown in investment activity will be caused by the refusal of the European investors to put money in their own economy or by the desire of the non-European investors to invest their money in the economy of the United States of America.

## Conclusion

In conclusion it is necessary to say, that the European Union suffers a lot of problems. They are connected with the indebtedness of the Southern European countries. Moreover, unstable situation outside Europe adds to the inner problems. Considering both positive and negative effects, one can understand, that benefits outweigh minuses. Assuming, that European banks have billions of dollars, invested into the Russian Federation in the form of a credit or an acquisition of securities, the risk of losing these funds will only arise, if Russia freeze the foreign assets. But it is unlikely. On the contrary, the inflow of the capital from emerging markets amounts to a rather significant sum. The major part of investors, individuals and business entities prefer stability, that is why they put their temporary available funds into European banks. These banks do not provide very high rates, but they guarantee that money will be safe. It is not so important, how big the risk is. What is much more important, whether adequate actions are undertaken in order to struggle against it. The European Union has all possibilities to fight. There is only the issue of the use of available options.

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# RECENT DEVELOPMENTS AND PROSPECT FOR ENGINEERING IN RUSSIA

## Abstract

*The article examines the aspects associated with prospects of engineering in the Russian Federation. The results of analytical research in the Russian engineering market are considered. Recent developments of engineering are analyzed. The major factors confirming prospects of significant growth of the Russian engineering market are defined. The structure of the Russian market in the context of engineering service methods, main suppliers and market segments are evaluated.*

***Key words:*** *engineering market, fields of engineering, prospect of engineering in Russia, innovation, modernization, industrial design.*
***JEL codes:*** *D 490, L 100, L 800.*

Advances in engineering have been central to human progress since the invention of the wheel. In the past hundred and fifty years in particular, engineering and technology have greatly transformed the world we live in, contributing to significantly longer life expectancy and increased quality of life for many people. This is why engineering deserves our attention. Nevertheless the term "engineering" itself is quite new for Russia. That doesn't mean however, that the idea of engineering, engineering processes and professional engineers is something new and unknown. The engineering movement in Russia has evolved since the middle of the nineteenth century, through consolidation of the scientific community, the formation of domestic engineering corporations and through representatives of business (industrialists and entrepreneurs) interested in accelerated development of domestic production. However the problems connected with organization of engineering activities and related ones have become especially important in our country during the last few years. It has become a hot topic of concern not only for players of engineering market but also for government.

The aim of this paper is to examine the aspects associated with prospects of engineering in the Russian Federation.

The major tasks are as follows:

- making an overview of different definitions of the term "engineering";
- describing the fields of engineering;
- analyzing Russian engineering market;
- considering recent developments of engineering in Russia;
- defining the major factors confirming prospects of the Russian engineering market significant growth.

Engineering is indeed a deep and diverse topic, and this article is an attempt to illustrate it and to shed light on the most important aspects of this phenomenon.

As a result, it will be useful not only for professional engineers and specialists in related spheres, but also for those students who are just choosing their future carrier.

There is a great number of definitions of the term "Engineering". The most widespread are given in the table below.

*Table 1*

**Definitions of the term "Engineering"**

| № | Source | Definition |
|---|---|---|
| 1 | Draft European Standard EN 16311 | Engineering (from Latin ingenium, meaning «cleverness» and ingeniare, meaning «to contrive, devise») is the application of scientific, economic, social, and practical knowledge in order to invent, design, build, maintain, research, and improve structures, machines, devices, systems, materials and processes. |
| 2 | The American Engineers' Council for Professional Development | Engineering — the creative application of scientific principles to design or develop structures, machines, apparatus, or manufacturing processes, or works utilizing them singly or in combination; or to construct or operate the same with full cognizance of their design; or to forecast their behavior under specific operating conditions; all as respects an intended function, economics of operation or safety to life and property. |
| 3 | UK Standard Industrial Classification of Economic Activities 2007 | Engineering is the process of envisioning, inventing, creating and building the world around us. |
| 4 | Engineering UK 2011, G. Gereffi | Engineering, the application of science to the optimum conversion of the resources of nature to the uses of humankind. |

To have a better understanding of engineering and its place in modern world, the relationships among science, technology and engineering should be analyzed. They can be described as shown in the figure below.

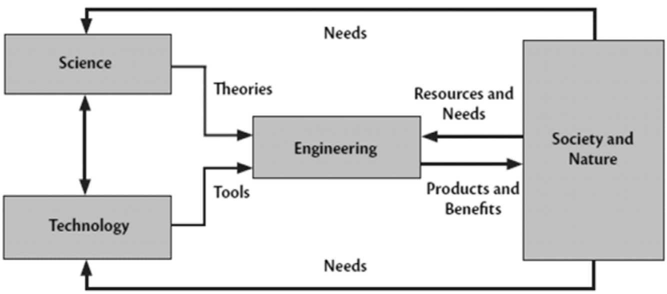


***Figure 1.*** Engineering and science

As you can see in the chart, the role of engineering and science in the knowledge society and economy cannot be underestimated. Science and engineering are essential parts of the same range of activity. Engineers use both scientific knowledge and mathematics on the one hand to create technologies and infrastructure to address human, social and economic issues, and challenges on the other. Engineers connect social needs with innovations and commercial applications. Technological change and innovation are the major drivers of economic, social and human change, so engineering, technology and social sciences are closely connected.

A diverse and increasing range of areas, fields, disciplines, branches or specialties of engineering could be outlined [2,3]. They developed as knowledge developed and differentiated as subjects subdivided, merged or new subjects arose. Emergence of new branches of engineering is usually indicated by the establishment of new university departments, new professional engineering organizations or new sections in existing organizations.

To illustrate the scope and diversity of engineering, it is useful to present the list of engineering branches as a diagram (Figure 2).

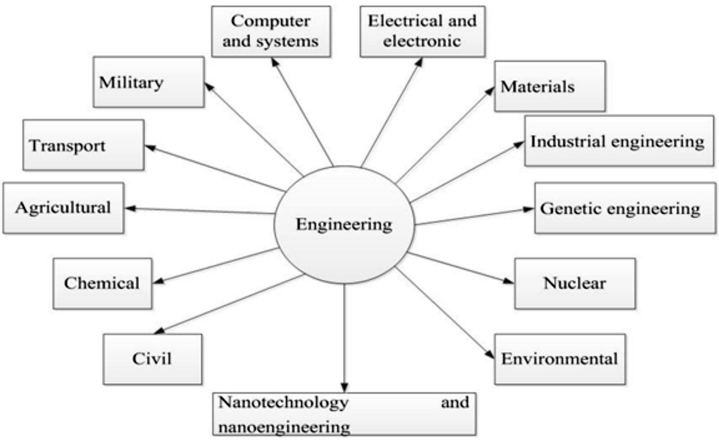


***Figure 2.*** Branches of engineering

The modern Russian market of technological engineering is characterized by considerable lag from the European one compared to the level of development. It could be considered as “fast growing market at the beginning of its formation”. High risks, the long investment period and large volume of initial investments place barriers for entering this market.

According to the analyzed materials [2,3,4], the capacity of the Russian market can be estimated at less than 1% of the international market of engineering services. The capacity of the Russian market in 2013 was 1,5 trillion rubles.

However, it should be underlined, that there are some difficulties with calculations of capacity and other market indexes because engineering in Russia is not allocated as the certain sphere of economy, that is why engineering service is not a unique unit of a statistical assessment. In this regard the Russian market of engineering services is at the stage of the formation now.

The **factors confirming prospects of significant growth** in the engineering market are the following:

- implementation of programs of the Government of the Russian Federation for modernization of economy and energy efficiency;
- implementation of the plan of measures ("road map") in the field of engineering and industrial design;
- assessment of investments, necessary till 2020, of more than $400 billion for development of the energy sector, being today one of the main consumers of engineering services.

According to the forecast carried out by KPMG [2] a growth rate of engineering services in Russia during 2014-2018 is predicted at the level of 15% annually. The actual and expected market capacity of engineering services in the Russian Federation is shown in figure 3.

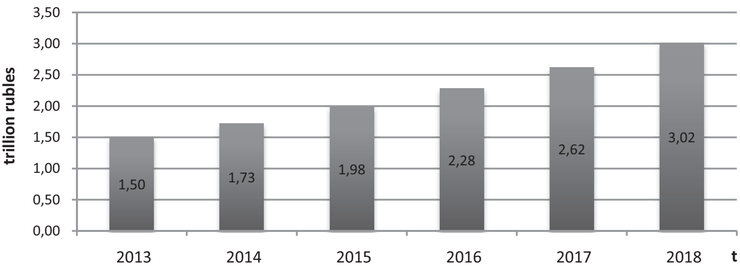


***Figure 3.*** The actual and expected market capacity

The structure of the Russian market of engineering is analyzed below. In figure 4 the structure of engineering services in types, according to classification of the Economic Commission for Europe of the UN (UNECE) is presented.

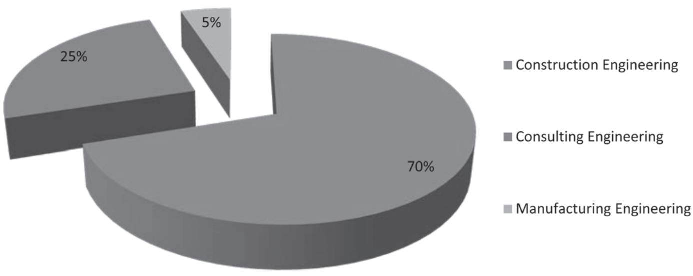


***Figure 4.*** The patterns of engineering services in the Russian market of engineering

Construction engineering has the main market share (up to 70%), consulting engineering has 25% and technological engineering accounts for 5%.

Engineering services in Russia are provided by special engineering consulting firms, and also industrial and construction companies. The main players on this market are private professional companies and large corporations, though the share of large corporations has reduced during the last years as a result of serious competition. The structure of the Russian companies providing engineering services of various types is presented in figure 5. It should be noted that many of them are large diversified holding companies, for example JSC Group E4 and Rusinzhiniring Holding.

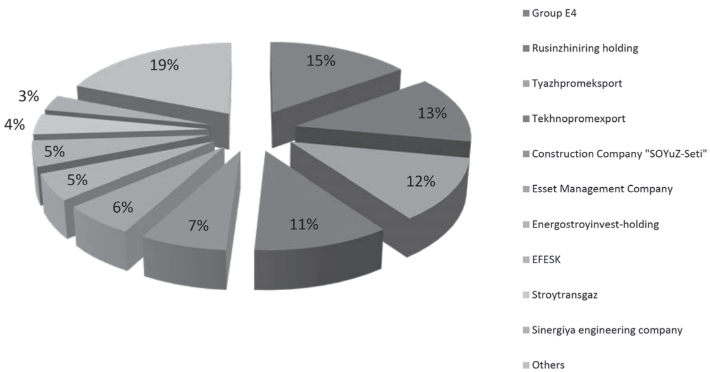


***Figure 5.*** Main players of the Russian market of engineering services

Though the major players on engineering market in Russia are E4 Groups, the Rusinzhiniring Holding and Tyazhpromeksport, there is a large number of small engineering companies on the market which total share does not exceed 19%, such as: VEB Engineering, Sevzap NTTs, Giprotruboprovod, VNIPIgazdobycha, Giprogaztsentr", Velesstroy, KMUS-2, Neftegazengineering, RusGazEngineering Group, etc.

The structure of consumers of engineering services by branches of economy is presented in figure 6.

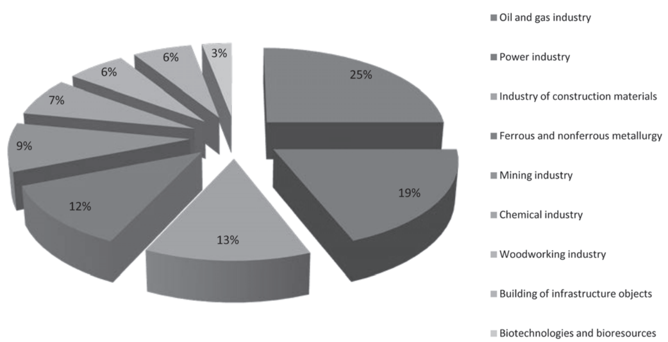


***Figure 6.*** The structure of the Russian market of engineering services by branches of economy

The greatest share is occupied by oil and gas industry, including technologies for production of liquefied gas and development of the sea shelf, power industry and the industry of construction materials. It should be noted that active revival of engineering (in modern understanding of this word) began with implementation of the investment program in the energy sector started by RAO UES.

To sum everything up, the main results of the paper are the following:

1) an overview of different definitions of the term "engineering" is presented;
2) the fields of engineering are described and classified;
3) the carried-out analysis of the market of engineering services showed that the capacity of the Russian market in 2013 is 1,5 trillion rubles, growth rate of engineering services in Russia, during 2014-2018, is predicted at the level of 15% a year;
4) recent developments of engineering in Russia are outlined;
5) the major factors confirming prospects of significant growth of the Russian engineering market are defined.

The current economic crisis presents challenges on the one hand and opportunities for engineering on the other hand. However, there are encouraging signs that the leaders of our country recognize the importance of engineering, science and technology and the fact that their development may provide an opportunity to economic recovery and sustainable development of our country.

To make a conclusion, it is engineering in fact, that drives social, economic and human development. It is a major factor in innovation and the rise and fall of civilizations.

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# PPP IN A CHALLENGING ENVIRONMENT OF VENTURE CAPITAL FUNDING: UNFAVORABLE SELECTION MODELLING

## Abstract

*The article studies PPP in a challenging environment on the basis of asymmetric information and its accuracy. The task is twofold: firstly, to provide a research of venture funding specifics in Russian challenging environment, and secondly, to build up a model of unfavorable selection principle for venture capital funding. The research is provided by a system method of the analysis along with economic and mathematical modelling.*

***Key words:*** *PPP (Public Private Partnership), asymmetric information, unfavorable selection, venture capital, modelling*

## Introduction

The basic aim of the article is to study unfavorable selection principle on the example of venture capital funding. The task is twofold: firstly, to provide a research of venture funding specifics in Russian challenging environment, and secondly, to build up a model of unfavorable selection principle for venture capital funding on its basis. The research is provided by a system method of the analysis along with economic and mathematical modelling.

## The concept of PPP in a challenging environment

PPP or Public-Private Partnership could be defined as a government service or private business venture, which is funded and operated through a partnership of government and one or more private sector companies.

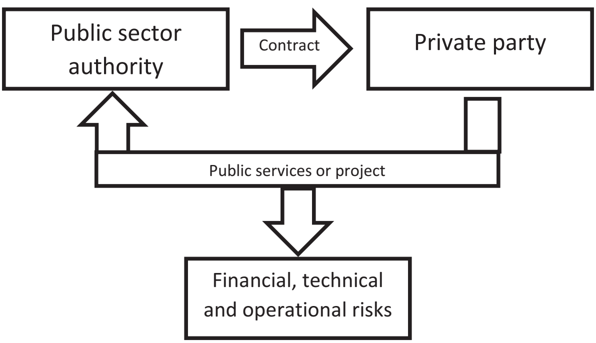


***Figure 1.*** The concept of PPP

To clarify the situation with PPP in Russia under the conditions of sanctions it is necessary to highlight that some economists believe that new sanctions imposed in Russia will lead to complete termination of contracts due to foreign investors leaving the Russian market.

Head of infrastructure and project of PPP department of Herbert Smith Freehills Company Olga Revzina stresses that even at the stage of partner selection for organizing, consortium foreign partners should firstly open the sanction list to find out the prohibited Russian partners. [1]

However, in practice, if we look closer, these limitations could be minimized in terms of infrastructure railroad development. There are still a lot of PPP for rail-road infrastructure, for example PPP-project of Pulkovo reconstruction in St. Petersburg.

Pulkovo airport in St. Petersburg ranks third in Russia in terms of passenger turnover. Nowadays, within the PPP project, broad-based reconstruction is taking place in accordance with the legal scheme № 552-64 'Participation of St. Petersburg in PPP projects' 24 of October 2000 (accepted in 2006).

This Pulkovo reconstruction will bring benefits in both social and economic areas. In addition, international commercial banks demonstrate an active interest to the project, as a result,the banks investment exceeded twice firstly planed the budget funding of the project.

Overall, PPP of Pulkovo has illustrated a long-term banking collaboration (15 years) in PPP projects in Russia and has become a textbook example in PPP involvement. This project is included in the first 100 global high-innovative city projects.

Let us shed light on the problem from the other angle. According to the Ernst and Young consultant, there is no limitation for PPP development in the current situation in Russia under sanctions. [1] According to him, it is a myth that foreign investors are leaving Russian PPP market because of sanctions. They are leaving the market because they don't see the project that could be profitably implemented under current conditions. Thus the basic problem in the challenging environment of PPP is the right project selection because of information asymmetry.

That is why it is vitally urgent to analyze uncertainty of economic processes increasing risks and information asymmetry.

## Venture capital as the basic form of innovation in finance

The theoretical basis for this research starts with the research of 1970 G.Akerlof "The Market for Lemons: Quality Uncertainty and the Market Mechanism" that firstly describes unfavorable selection as an economic phenomenon. [6]

The concept of this economic phenomenon is — there is asymmetry of information on the market between the Principal and the Agent.

The Principal is better informed about the quality of a manufactured goods or range of services. The Agent does not have precise and accurate information about the product at the moment of purchasing. Thus, the Principal has the incentive to overrate the product and to sell it at a higher price. Because of information asymmetry the Agent has no right trade off to buy the product of low quality at higher prices. As a result, the market of low quality products is expending. This phenomenon is called unfavorable selection.

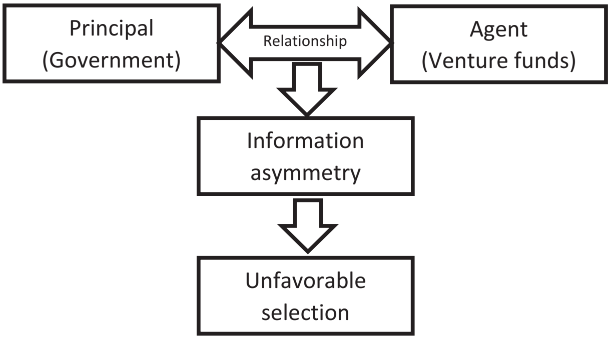


***Figure 2.*** Unfavorable selection principle

Despite the success of some Russian projects implemented with the help of venture investments, it is necessary to note that venture investments present sector-wise inequality and the priorities are given to short-term investments. This trend impedes Russian economic development and requires adjustments.

In order to understand the problem let us address venture capital entrepreneurship in Russia. The history of this phenomenon in Russia is over 20 years. Because of the 20 years of development, we can see that the number of venture funds increased from 11 regional venture funds in 1994 to 105 companies of direct and venture investment in 2009 and today's turnover of venture investment is more than 2 bln $.

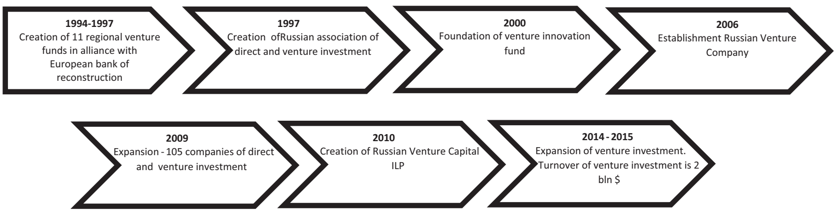


***Figure 3.*** Venture capital in Russia: 20 years of success. Time-line analysis
Created by the author on the basis of [5]

## Information asymmetry and its effect on decision-making in project selection

According to the Principal-Agent relationships, project information presents some asymmetry as entrepreneur knows his business much better and investor does not have accurate information about the business itself, the company, advanced technologies, research and development basis.

As a result, the entrepreneur has the motivation to use this competitive edge information at the sacrifice of the investor.

Knowing this, the investor makes his/her decision by averaging the discount rate for every project. As a result, conflicts of interests occur because entrepreneurs of quality projects with high potential do not want to participate in the market because of overrated discount rates. Conversely, non-quality projects entrepreneurs strive to participate because of underrated discount rates presenting market failures.

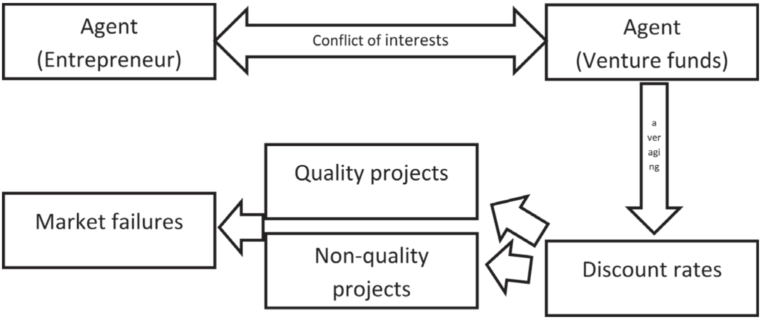


*Figure 4.* Conflict of interests in decision-making process
Created by the author on the basis of [3], [4]

## The basic criteria for effective project evaluation

Nowadays there is a great variety of research concerning criteria of project effectiveness:

- NPV (Net Present Value);
- PI (Profitability Index)
- IRR (Internal Rate of Return)
- MIRR (Modified Internal Rate of Return)
- PP (Payback Period)
- DPP (Discounted Payback Period)
- ARR (Accounted Rate of Return)[7]

You can see from the table that there are two basic criteria NPV and IRR. The rate such kind of methodology is approximately the same in the US and Great Britain.

*Table 1*

**Preferences in criteria choice**

| | USA | UA | Netherlands | Canada | Australia | China |
|---|---|---|---|---|---|---|
| NPV | 75 % | 80 % | 89 % | 1 | 94 % | 49 % |
| IRR | 76 % | 81 % | 74 % | 2 | 81 % | 89 % |
| PBP | 57 % | 70 % | 79 % | 3 | 90 % | 84 % |
| ARR | No data | No data | 2 % | No data | No data | 1% |

Source of information: [7]

Ernst and Jang made a research based on opinion poll of the funds presenting investments in Russia. There are 36 international funds the total assets for which is over 4,7 billion $. 3 billion $ is invested in Russian bonds and shares. [7] *According to this research* there is no unique methodology

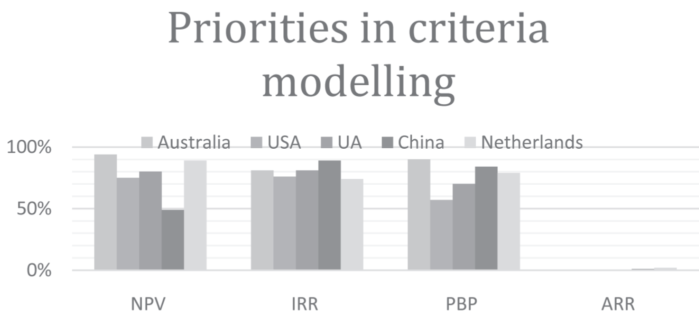


***Figure 5.*** Priorities in criteria modelling
*Created by the author on the basis of [7]*

Unfavorable selection modelling for venture financing of investment project

According to the research of author, you can see the tasks of the model. We introduce following designation:

- $b$ — the share of the Principal in the project profit
- $(1 - b)$ — the share of the Agent in the project profit
- $\theta$ — type of Agent project, $\underline{\theta}$ — lowest level of Agent project type, $\bar{\theta}$ — highestlevel of Agent project type
- $F(\theta)$ — distribution function of Agent project type
- $y$ — effort of Agent
- $H$ — function of project income
- c — cost of project realization of Agent
- $U(\tilde{\theta})$ — function of Agent utility
- $W^p$ — function of Principal utility
- $h(\theta)$ — hazard rate

As mentioned above, the Agent does not invest his own funds and expects to get surplus from the project. Assuming these we can see limitation for the Principal and for theAgent.

The final model depicts the conditions of the Principal-Agent Relationship optimization under project Venture funding on PPP market. As a result, maximizing the goal function of Principal under information rent of Agent minimization through the selection of the optimal effect.

$$U(\tilde{\theta}) = (1-b)\cdot H(y(\tilde{\theta}),\tilde{\theta}) - c(\tilde{\theta}, y) \xrightarrow[\tilde{\theta}]{} \max$$

$$W^{p} = \int_{\underline{\theta}}^{\bar{\theta}} b\cdot H(y(\theta),\theta)\cdot f(\theta)\cdot d\theta \xrightarrow[\theta]{} \max$$

## The result

After some calculations, the final result is the following:

$$y^{*} = -\frac{2\cdot(1-b)\cdot\theta^{3}}{2\theta\cdot h(\theta)+1}\cdot\frac{\partial H(y(\theta),\theta)}{\partial y\partial\theta}$$

The author's model defines optimal condition of Principal-Agent partnership for venture financing of PPP projects.

## Conclusion

The analysis allows us to draw some conclusions. First of all, *project valuation* for decision-making about venture funding should include *analysis of asymmetry*. Secondly, maximizing the goal function of Principal under information rent of Agent minimization through the selection of the optimal effect. Thirdly, the final model depicts the conditions of Principal Agent Relationship optimization under project Venture funding on PPP market. Finally, we should yield lessons for venture funding implementation. Therefore, it has become the basic requirement for innovation economy in Russia in the challenging environment.

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# THE FORESIGHT IN FUEL AND ENERGY INDUSTRY IN RUSSIA: THE IMPLICATIONS OF SANCTIONS

## Abstract

*The research analyses the importance of fuel and energy industry in Russia as well as current and possible implications of sanctions to the complex due to the present structure of the sector and the utmost importance of foreign companies in the process of extraction (mainly the equipment in the upstream segment) and their refining facilities. The comprehensive analysis will use the scenario approach in order to estimate the impact on the industry in the long term.*

***Key words:*** *energy economy, sanctions, Russia, oil prices, oil and gas sector.*
***JEL codes:*** *F 51, O 13, Q 43.*

## Introduction

While being the main source of the budget income, Energy sector is the basement of the whole Russian economy. That is why hitting it became one of the paramount goal of the sanctions' implementation. According to the adopted regulation agreements, sanctions imposed a wide range of restrictions on the energy technologies' transfer to Russia. These measures are likely to inhibit a number of strategic plans of Russian companies.

## Export restrictions of certain technologies and equipment

First of all, the sanctions are expected to create additional difficulties for the shale exploration and the extraction in the Arctic zone [1]. These projects are characterized by extremely difficult climate conditions, so they were based mostly on the usage of foreign equipment. Moreover, as Russian oil companies have a lack of experience they participated in a number of collaborative projects with the Western companies such as Exxon Mobile, BP, Statoil and so on [6]. In addition, domestic producers had contracts with the Western oilfield service companies like Shlumberger.

Now after sanctions came into effect they have to leave the Russian market. However, the oilfield service companies have found a way to bypass the restrictions. At the end of January 2015 Shlumberger – the world oilfield service leader – announced a purchase of 45,65% share  in a largest Russian drilling company called Eurasia Drilling Company [7]. Thus, it got an opportunity to continue working in Russia.

Against this background, there is a question that may be asked: “Will the sanctions really damage Russian energy sector, and if so, when will that be?” The answer is quite complex, but it seems that they will not have an immediate impact on current exploration; they will be oriented mostly on preventing the future development of the industry. Oil reserves in the majority of exploiting wells are close to their end, while there is a plenty of resources hidden in the hard-to-reach deposits, which require foreign equipment.

Nevertheless, although implemented restrictions put a huge pressure on the energy sector, it can be also considered as a driver for a sector, pushing it ahead and providing new opportunities. In such a complicated situation Russian companies started searching for the ways out [3]. Firstly, they reoriented their activities to Asia, raising the total oil & gas exports to the region up to 30%. In return, China will be able to deliver all the necessary equipment, that can substitute western prototypes. However, the change in supply will take some time, thus a number of projects will be postponed. Secondly, Russian companies may concentrate on their own development, investing money in the R&D, in other words, to work out a different and comprehensive strategy with the solemn goal of self-sufficiency and efficiency. Today many oil & gas corporations have chosen this path. They’ve started to analyze the existing trends in the world energy economy so as to highlight the technologies of their foreign competitors in order to prioritize current investment projects and to develop a sound long-term investment and R&D strategy.

## Restricted access to the foreign capital markets

The next important issue to be addressed is the limitation of access to the international funding. Russian companies, including those operating in the oil & gas sector, are highly dependent on the foreign financial resources. While external debt of the Russian economy was gradually decreasing during 2000s, companies continued to take more and more credits in the foreign banks, investing raised money in their key investment projects. Now with international capital markets closed they will have to switch to Asia again and the main problem here is the current uncertainty about possible credit terms.

## Low oil prices ($50/b or less)

Finally, Russian economy continues to suffer from the recent dramatic fall in oil prices. At the beginning of the 2015 they’ve reached the point of 50 $/b and the future changes are hard to predict [5]. The situation is similar to the one with the implementation of sanctions — the existing productions process is not threatened in the short-run, but it may have absolutely different effect in the long-run as new progressive projects become unprofitable or even impossible due to the lack of the needed technologies. At the moment Russian energy companies are thought to remain stable due to the flexible tax regime, when the rates move in the same direction with the oil prices. Additionally, their revenues nominated in rubles are supported by the national currency depreciation. In order to estimate the low oil prices' impact on the companies, operating in oil & gas industry, Fitch Ratings published a comprehensive forecast, based on the assumption that there will be no recovery in oil prices during 2015-2016 (55$ per barrel). In this case the credit burden of corporations are projected to remain acceptable with the only 23% decline in EBITDA [5].

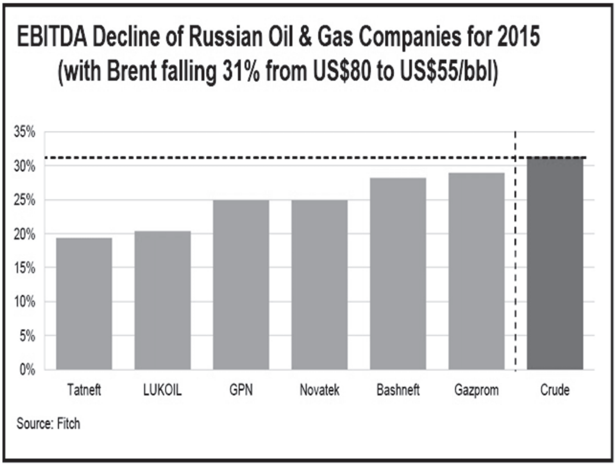


***Figure 1.*** EBITDA decline of Russian Oil & Gas Companies for 2015-16 relative to oil price dip. [5]

While constructing this scenario, Fitch Ratings took into account three factors that can affect future sector's performance. Firstly, it is a progressive tax regime mentioned earlier. Secondly, it is a relatively flexible regime of exchange rates that will cushion the impact of falling export revenues. And finally, the domestic gas prices' regulation, that go down slower than the oil prices do.

There is no doubt, sharp decrease in the oil prices made Russia's current position even more complicated. The total impact of the sanctions on the current oil & gas projects is reflected in the table below.

*Table 1*

**The impact of sanctions on the oil & gas projects**

| | **The restrictions on the Russian imports of equipment** | **Restricted access to the foreign capital markets** | **Low oil prices ($50/b or less)** |
|---|---|---|---|
| **Shelf projects in the Arctic** | **Critical**<br>High dependent on the foreign equipment and technologies | **Important**<br>The projects imply high level of financing and cannot be implemented without foreign funding | **Critical**<br>The projects remain profitable on the level of $40–100 |

| | **The restrictions on the Russian imports of equipment** | **Restricted access to the foreign capital markets** | **Low oil prices ($50/b or less)** |
|---|---|---|---|
| **Prirazlomnoe** | **Not critical**<br>The offshore drilling | **Not critical**<br>The main investments have been already made. Only operational costs are left | **Critical**<br>The production costs are high, unprofitable under the low oil prices |
| **Prinovozemelskie** | **Critical**<br>ExxonMobil participated in exploration | **Important**<br>The projects imply high level of financing and cannot be implemented without foreign funding | **Critical**<br>The production costs are even higher than that on Prirazlomnoe |
| **Black sea** | **Critical**<br>ExxonMobil participated in exploration | **Important**<br>The projects imply high level of financing and cannot be implemented without foreign funding | **Critical**<br>High cost of production because of deep-water drilling |
| **Kaspian region** | **Not critical**<br>Sanctions don't concern Kaspian sea | **Not critical**<br>Lukoil uses its own financial resources | **Important**<br>Cost of production is higher than ones for continental deposits |
| **Harder-to-reach oil in West Siberia** | **Critical**<br>High dependent on foreign equipment and technologies | **Important**<br>The projects imply high level of financing and cannot be implemented without foreign funding | **Important**<br>The production costs are high, unprofitable under the low oil prices |

Source: [2], [4]

However, the stabilization of prices would not improve the situation as the current issues lay a way deeper. Firstly, the trends on the energy market have recently changed their direction due to the development of the several factors:

- So-called “shale revolution” that implies the US to become a global centre of the hydrocarbon production;
- The rising demand for oil and gas in the Asian region.

## Conclusion

Thus, Russia has to adjust its energy industry to the new conditions based on the new rules of competition. Unfortunately, this is where internal problems come into play. The majority of the wells have already been depleted with the existing fields are going into the decline phase. Even in the USSR, particularly in the 1960–1980s, in most cases oil fields were overused in order to cover the output plans set by the government. While having huge oil & gas reserves coupled with the stable and high oil prices and relatively low extraction costs — Russia was given an opportunity not to invest money in additional technological improvements. That resulted into the progressive degradation of the whole oil & gas sector deprived from the investment needed to alleviate the depletion of the existing wells — the need for additional explorations efforts in the area as well as new technologies increasing the efficiency of the process in general.

Eventually, this short-sightedness accounted for the transformation of the oil & gas sector in Russia making it directly dependent on the foreign investors and partners. In order to revitalize the industry a lot of foreign companies and foreign experts, mostly from the developed countries, were permitted to enter the Russian market in 2000s. That is how the cooperation between Russian leading producers and foreign oilfield service companies started to spread over the industry. On the other hand, while being quite efficient at the beginning, this combination made Russia companies highly dependent on their foreign partners and, thus, made the whole sector vulnerable to the current sanctions.

Nevertheless, the dependence seems to be mutual. Although Europe is making a plenty of attempts in order to reduce its dependency on the Russian gas, to diversify its supply, the cost of such a substitution remains relatively high. Moreover, the demand for the natural gas will not go down at least in the mid-term, accounting for around 100bcm of gas up to 2030.

There is a paradox, but the sanctions may even have a positive effect on the Russian energy sector, making it more autonomous and self-sufficient. Even now a lot of leading producers have started to invest money in the R&D, to analyze the foreign companies' experience in order to develop all the needed equipment and the technologies by themselves. From this point of view, such kind of crisis, caused by the sanction implementation, can provide a lot of possibilities for innovations in the sector spurred by the eventually inevitable crisis.

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# FINANCING THE BUSINESS PROJECT WITH CROWDFUNDING

## Abstract

*The research analyses crowdfunding as a method of attracting financing. It focuses on the concept and history of crowdfunding and provides a study on different types of the largest crowdfunding platforms across the world and in Russia. The research points out the benefits and risks of this type of financing and introduces the basic reccomindations for the entreprenuers, according to which they can conduct a successful crowdfunding campaign.*

***Key words:*** *crowdfunding, crowdinvesting, financing, business project, startup*
***JEL codes:*** *O16, O31*

## Introduction

A great number of entreprenuers face a problem of choosing the financing method nowadays. Traditional types of financing are usually too expensive or inaccessible for small companies. In this way, entreperenuers call for new instruments of attracting money.

The Internet brought new opportunities for project initiators. By eliminating intermediaries and reducing costs of transactions, the global network has made the usage of small amounts of money reasonable in the context of accumulating capital. Small donations by large groups of people underlie the crowdfunding.

## Concept of crowdfunding

As for many terms, which appeared recently, there is no common definition of crowdfunding, however, all of the existing descriprion share the main idea of this method.

Crowdfunding is a novel method for funding a variety of new ventures, allowing individual founders of for-profit, cultural, or social projects to request funding from many individuals, often in return for future products or equity. Crowdfunding projects can range greatly in both goal and magnitude, from small artistic projects to entrepreneurs seeking hundreds of thousands of dollars in seed capital as an alternative to traditional venture capital investment [1].

The term «crowdfunding» can be also defined as: «The use of small amounts of capital from a large number of individuals to finance a new business venture.

Crowdfunding makes use of the easy accessibility of vast networks of friends, family and colleagues through social media websites like Facebook, Twitter and LinkedIn to get the word out about a new business and attract investors. Crowdfunding has the potential to increase entrepreneurship by expanding the pool of investors from whom funds can be raised beyond the traditional circle of owners, relatives and venture capitalists» [2].

## Historical background

In 1713 Alexander Pope set out to translate ancient Greek poems into English. It took 6 years to translate 6 parts and the result did worth it. Translation of Homer's Illiad endures to this day& In exchange for a shout-out in the acknowledgements, an early edition of the book, and the delight of helping to bring a new creative work into the world, 750 subscribers pledged two gold guineas to support Pope's effort before he put pen to paper. They were listed in an early edition of the book.

In 1783, Mozart took a similar path. He wanted to perform three recently composed piano concertos in a Viennese concert hall, and he published an invitation to prospective backers offering manuscripts to those who pledged. Alas, not all projects reach their funding goals, and Mozart fell short. A year later he tried again, and 176 backers pledged enough to bring his concertos to life. He thanked them in the concertos' manuscript

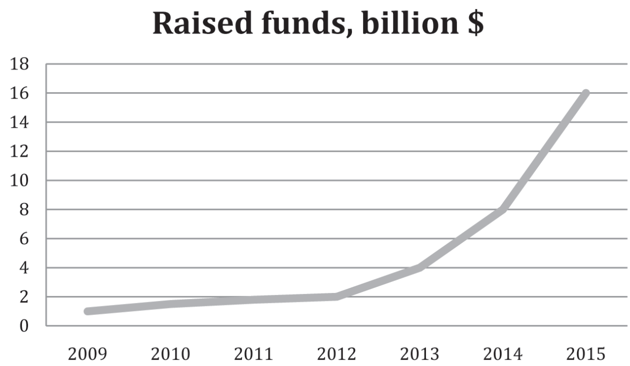
In 1885, arguably the most ambitious project of all to find funding this way began. France was at work on a statue of the Roman goddess of freedom to give to the United States to celebrate its centennial. But the Statue of Liberty had no pedestal on which to stand in New York Harbor. Joseph Pulitzer, publisher of The New York World, launched a project for the construction of one. In exchange for 1 dollar pledgers would receive a six-inch statuate of Lady Liberty. In Exchange for 5 dollars they would receive a twelve-inch one. Soon, over 120 000 people from over the world helped to raise over 100 000 dollars.

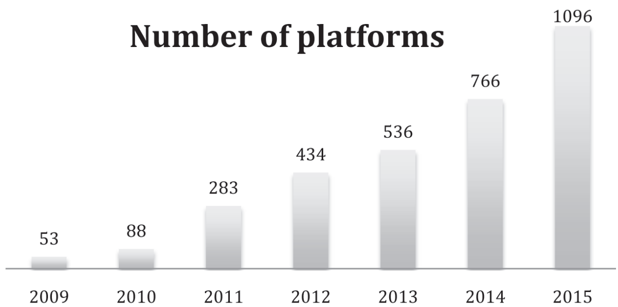
In 1997 a rock band Marillion raised money for their reunion tour over the Internet with the help of their fans. Inspired by this event, founderd of «ArtistShare» started the first crowdfunding platform for creative misicians [3].

The term «Crowdfunding» was introduced by Michael Sullivan in 2006.

## Market analysis

According to the portal statista.com, in 2012 the crowdfunding market was estimated at 3 billion dollar with growth rate at 60%. In 2009 funds raised on crowdfunding platforms were estimated 1 billion dollars and they kept growing slightly until 2012, then, raised funds amount skyrocketed and it is estimate to hit 16 billion dollars in 2015 [4].




## Crowdfunding platforms

Nowadays there are more than 750 crowdfunding platforms. Creators can choose between them according to their needs and project goals.

For example, there are services based on equity crowdfunding, such as CrowdCube or Seeders, which allow companies to issue microshares and by selling these shares they collect money. This type of crowdfunding is usually called crowdinvesting.

**CrowdCube** — the largest crowdinvesting platform in the Great Britain and one of the largest in the world. According to the platforms model, investors can buy micro-shares in different projects. Crowdcube was founded in 2011 and helped to attract almost 80 million pounds.

«Camden Town Brewery» — a project, launched by the largest brewery in London. Its aim was to raise money for a construction of a new factory. The goal of 1,5 million pounds was exceeded by 1,7 times and reached more than 2,5 million pounds.

«The Burrito Bond» is a project, launched by «Chilango» which holds a restaurant chain. The company issued bonds with 8% interest and maturity of eight years. The campaign goal of one million pounds was exceeded by two times [5].

Its worth mentioning that business of CrowdCube is approved by Financial Services Authority of the Great Britain.

**Kickstarter** — is one of the most famous crowdfounding platforms. It was launched in 2009 and since then more than 8 million people donated over 1,5 billion dollars, funding over 80 thousand creative projects. It's reward model, also known as the «Kickstarter model», presumes that people donate a certain amount of money and in reward they receive a product of a campaign or a special gift. Kickstarter is known for the most successful crowdfunding capmaigns in history.

The «Pebble» — is a project for building a smartwatch. It has raised 10 million dollars, exceeding the target amount more than one hundred times. Currently, «Pebble» is one of the most successful smartwatches on the market [6].

The «Coolest Cooler» is a multifunctional device, which includes a cooler, an audio speaker, a phone charger, a blender and a LED tourch. It's crowdfunding capmaign raised 13 million dollars, making the «Coolest Cooler» second most funded project on «Kickstarter» [7].

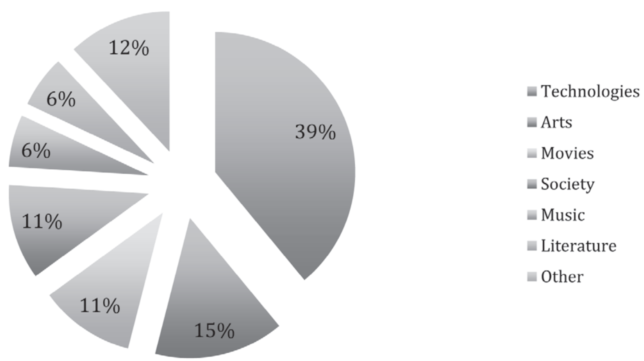
«Pebble Time» is the new version of «Pebble» and founders had raised 20 million dollars during the campaign and it has beome the most successful project on Kickstarter [8].

### Crowdfunding in Russia

In recent years crowdfunding industry has been growing fast in Russia.

Current estimation of Russian crowdfunding market, accrording to J'son & Partners Consulting is 160–180 million rubles and approximately 75% is held by Planeta.ru and Boomstarter which both are based on the reward model.

**Shares in russian crowdfunding industry**




Source: J'son and Partners Consulting

**Planeta.ru** — is the major crowdfunding platform in our country. It was founded in 2012. Planeta.ru helped to fund more than 300 projects with more than 50 millions of donations. Platforms commission is 5% from successfully funded projects [9].

A teleplay «Petrushka» is one of the most successful campaigns on «Planeta.ru». Victor Shenderovich, the initiator of the project, collected more tha 5 million 800 thousand rubles from approximately 3 thousand people.

«Mokrii Nos» — a project of a multifunctional center for animals. Founders of this project raised more than 5 million rubles and in current time the center is being built.

Another Russian crowdfunding platform — **Boomstarter** was founded on 2012. Boomstarter became «The most socially important startup» in «Startup» competition by HSE. More then 36 thousand people donated more than 50 million rubles [10].

The movie «28 panfilovcev» raised 3 million 191 thousand rubles on Boomstarter from nearly 4 thousand people. The movie is supposed to be released in 2015.

«Russian Dance Festival» — the largest dance festival in Russia. In order to organize this event, in 2014 a campaign was launched. It ended up attracting almost 3 million rubles from 267 sponsors. The festival was successfully held in 2014.

Although donations on Russian platforms are much smaller than the ones on American platforms, Russian crowdfunding industry is still growing fast.

## Advantages of crowdfunding

There are three active parties in crowdfunding process: creators, funders and platforms. Crowdfunding introduces both benefits and risks to each of them.

Benefits for creators:
- Lower cost of attracting financing
- Funders can give advices on product
- More information about consumers and demand

Benefits for funders:
- Opportunity to invest money
- Earlier access to product
- Formalization of contracts between creators and family and friends since they are usually the first to fund the project

Benefits for platforms:
- Income from successfully funded projects (4%–5% of funding sum)
- Creative products attract the attention of mass media

## Risks of crowdfunding

Although there are certain advantages for entrepreneurs, crowdfunding campaign also represents risks for these three groups.

Risks for creators:

- Project information disclosure
- Financial management due to large amount of funders
- Funders can affect project realization

Risks for funders:

- Creators' incompetence
- Probability of fraud
- Risk of loosing money

Risks for platforms

- Not all projects reach their funding goals
- Bad projects affect platforms reputation

Crowdfunding is a fast developing industry with 60% annual growth. This funding method has helped to start many creative businesses and start creative projects in music and movie industries. Even though, such projects usually impose high risk on donators, the loss of individuals is relatively small because crowdfunding operates with small sums of money, but a huge number of participants. Perhaps, in near future crowdfunding will eclipse such traditional institutions like venture funds or business angels.

## Recomendations

A crowdfunding campaign is successful not only when the core idea is creative but the whole project team has to perform properly in order to reach projects goals. During the analysis of crowdfunding, main platforms and the most successful projects, the basic recommendations for projects initiators were pointed out.

Before you start:

1. Decide why crowdfunding is best for your project
2. Figure out the basic reasons why people should fund your project
3. Make a research on hot to complete your goals
4. Make a presentation and a short film about your project

Designing your campaign:

5. Choose a crowdfunding platform
6. Design the layout of your campaign
7. Decide how you will award your funders
8. Estimate the delivery date

Launching the campaign:

9. Know your funding goal
10. Focus on social media and promotion
11. Enjoy the results of campaign

Ending the campaign:

12. Thank your funders
13. Keep updating your project
14. Focus on realization of your idea

## Conclusion

By following these steps an entrepreneur can keep everything in mind and complete goals in order to bring your creative idea to life. Crowdfunding is one of the most developing capital markets in the world. It has already helped creators to start multimillion businesses, release music albums and even shoot film. However, every creator has to keep in mind advantages and risks of crowdfunding and use the experience of many successful creative projects.

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# CURRENCY WAR: WHAT TO EXPECT?

## Abstract

*Currency war is a targeted depreciation of a national currency by monetary authorities to boost exports and cut imports. But the popularity of sanctions this year has lead to significant changes in its concept. Today a currency war means a depreciation of the enemy's currency, not national. The paper examines if a currency war will benefit the world economy or the result will be a complete failure.*

***Key words:*** *currency, war, depreciation, economy*
***JEL codes:*** *F51*

## Introduction

The global currency war is threatening to prove a silent killer.

While some economists question the existence of any conflict, arguing that falling exchange rates merely reflect efforts by central banks to spur lackluster domestic economies, other express concern.

There is a growing consensus in the market that an unspoken currency war has broken out. The reason why this is a war is that it is ultimately a zero-sum game where someone gains only because someone else will lose.

The standard view on war-mongering is that by easing monetary policy, central banks from Asia to Europe are hoping to weaken their currencies to boost exports and import prices. Trade rivals then retaliate, creating a spiral of devaluations as witnessed in the 1930s.

Just this month, the Reserve Bank of Australia Governor Glenn Stevens said "a lower exchange rate is likely to be needed" after he unexpectedly cut interest rates to a record low.[4]

According to the heads of central banks, the only way to escape deflation and stimulate growth — devalue against the currencies of trading partners. This is there «competitive devaluation» begins. Its purpose is to meet the demand for exports due to competitive prices and at the same time keep the fixed prices for imports. The problem becomes apparent when too many countries are trying to weaken their currencies. Not everyone can afford it.


## How competitive devaluation works?

The first way to make a currency unattractive is to lower interest. But what happens when the interest rate is lowered to zero? It depends on the situation. In some cases, central banks further weaken monetary policy through large-scale purchases of assets (quantitative easing), which allows to inject more money into the economy through the banking system.

Other central banks are trying to carry out foreign exchange intervention and set negative rates. The most famous case is the Swiss National Bank, which in January reduced its basic rate to 0.75%, as its attempts to provide a cheap currency at the expense of direct intervention failed miserably and the bank was forced to abandon the maintenance of a fixed exchange rate of the Swiss franc. Denmark also reduced the rate to 0.75% in order to keep the peg to the euro, and the Swedish central bank brought the deposit rate to 0.1%. This was done to mitigate the Swedish krona, to avoid increasing deflationary dynamics in Sweden.

In fact, it is clear that negative rates can not be maintained for a long time just for political reasons.

The problem of negative interest rates escalates when everyone pursuing such a policy. The Fed — the only major central bank that stops quantitative easing and approaching a tipping point, when it can raise rates; However, the market, and not without reason, is skeptical about the chances of the Fed rate hike, given that the rest of the world is mired in deflation, conjugate with reduced rates and quantitative easing.

## The current situation

Of course, central banking etiquette would never be so coarse as to actually acknowledge "currency wars". But when Mario Draghi at the European Central Bank reaches for the printing press to pump €1.1 trillion into the eurozone economy, a much weaker euro is certainly a happy coincidence.[5]

It is dangerous to generalise about individual countries but there are three broad stories going on among the cutters. Weeks or even months before Draghi pushed the button, imminent ECB easing was the elephant in the room — and the main driver behind Switzerland's move to scrap the franc's currency cap against the euro, while slashing rates even deeper into negative territory. The "anti-Draghi" faction includes the Danish central bank, which has had to cut rates twice to stem speculation that the krone's peg to the euro will be a looming casualty.

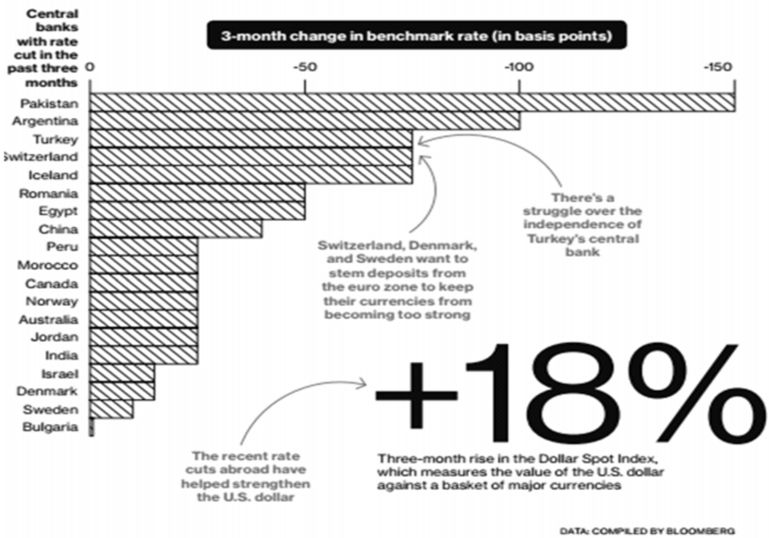
Then there are those with economies dependent on natural resources plunging in value, such as oil or metal: the likes of Canada and Australia, whose fortunes are also tied to a weakening Chinese economy. Russia — having been forced to jack up rates to defend the rouble — has cut them again as recession looms. The final group comprises those nations who usually struggle to keep inflation under control — say India, Pakistan and Egypt — which have taken the opportunity to cut rates in a tougher growth climate thanks to those low oil prices.

The average punter will cheer if his pound buys more euros on holiday in Spain. But look at the big picture. The trouble with these beggarthy-neighbour policies is that once somebody else starts cutting to hammer down their currency, you're being hurt just by standing still: so the incentive is all the more strong to follow the leader to protect your competitiveness.

Of the 53 central banks tracked by Bloomberg, 19 have dropped their benchmark interest rates in the past three months. Low rates encourage consumers to borrow and spend, increasing domestic consumption. They also devalue currencies, making exports cheaper. China has reduced reserve requirements on banks. Denmark has taken its official deposit rate into negative territory. Even the most stability-obsessed countries have made unexpected moves in this direction.

This new round of central bank activism reflects persistent concerns about economic growth. Despite a once-unthinkable amount of monetary stimulus, global output remains well below potential, with the potential itself at risk of being suppressed.

Making matters worse, weak demand and debt overhangs are fueling concerns about deflation in the eurozone and Japan. Anticipating falling prices, households could postpone their consumption decisions, and companies could defer investment, pushing the economy into a downward spiral from which it would be very difficult to escape. If weak demand and high debt were the only factors in play, the latest round of monetary stimulus would be analytically straightforward. But they are not. Key barriers to economic growth remain largely unaddressed—and central banks cannot tackle them alone. For starters, central banks cannot deliver the structural components—for example, infrastructure investments, better-functioning labor markets, and pro-growth budget reforms—needed to drive robust and sustained recovery. Nor can they resolve the aggregate demand imbalance— that is, the disparity between the ability and the willingness of households, companies, and governments to spend. And they cannot eliminate pockets of excessive indebtedness that inhibit new investment and growth. It is little wonder, then, that monetary policy instruments have become increasingly unreliable in generating economic growth, steady inflation, and financial stability.




Of course, not all currencies can depreciate against one another at the same time. But the current wave of efforts, despite being far from optimal, can persist for a while, so long as at least two conditions are met.

The first condition is America's continued willingness to tolerate a sharp appreciation of the dollar's exchange rate. Given warnings from U.S. companies about the impact of a stronger dollar on their earnings, not to mention signs of declining inward tourism and a deteriorating trade balance, this is not guaranteed. Still, as long as the United States maintains its pace of overall growth and job creation—a feasible outcome, given the relatively small contribution of foreign economic activity to the country's GDP—these developments are unlikely to trigger a political response for quite a while. Indeed, America's intricate trade relations with the rest of the world—which place households and companies on both sides of the production and consumption equation—make it particularly difficult to stimulate significant political support for protectionism there.

The second condition for broad-based currency depreciation is financial markets' willingness to assume and maintain risk postures that are not yet validated by the economy's fundamentals.

## Conclusion

So what happens next? Hard to say. Universal Currency war threatens to escalate into a war of trade protectionism, and then in a real war. The risk of such an outcome will skyrocket if China makes a fateful step and revalue its own currency — the yuan. Given that China is the world's factory, it will cause a new wave of deflation that has swept across the world.Therefore, it is likely that the currency war will continue.

The question investors are now asking: How does this all play out?

For the time being, they love it. Easier policy, low rates, quantitative easing, cheap money, weak currencies — it's all a recipe for gains in stocks and bonds, or as Kit Juckes, senior Forex strategist at Societe Generale, summed up the reaction to the ECB move: "Pretty much unalloyed joy,"[6]

However the worry is, what's the endgame?

In the 1930s when countries turned to competitive devaluations to boost growth, it backfired. The currency moves exacerbated the Great Depression by increasing trade tensions and barriers, raising business uncertainty and eventually cutting into growth.

"This currency war cannot go well. They never have," Art Cashin, director of floor operations for UBS at the New York Stock Exchange said.[7]

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# INTERACTION BETWEEN REAL AND FINANCIAL SECTORS OF THE RUSSIAN ECONOMY: GROWTH IN UNSTABLE ECONOMIC CONDITIONS

## Abstract

*The report is aimed at analyzing reasons for a distinction between real and financial sectors of the Russian economy. The main issues considered are sources of capital investments in the real sector, quantitative characteristics of the Russian financial market and possible ways of its infrastructure improvement. The research has shown that Moscow Stock Exchange should extend the access to small and medium businesses in order to support economic growth during the crisis period.*

***Key words:*** *real sector, financial market, investments, stock exchange, small and medium businesses, economic growth*
***JEL codes:*** *D 53, E 22, O 16.*

Interaction between real and financial sectors is of interest for the government and potentially represents the inducement for the growth of the national economy. The economic growth is primarily connected with investments. Investments constitute reliable driver of the economy as they determine potential for growth and improvement of production facilities, modernization processes and development of the real sector on the whole.

As follows from the official statistics, investments in fixed capital in Russia amounted to 13.5 trillion rubles at the end of 2014. It represents 19% of Gross Domestic Product [12]. This indicator is very low compared to other similar economies such as BRICS countries. For example, according to the latest data, in China investments amounted to 39% of GDP, in India — 38% [3].

Chart 1 shows that statistically the own funds of organizations is the main source of investments in fixed assets in Russia. However, these cash assets are limited and a company on a certain stage of its development tries to find out external sources.

*Chart 1*

**The Sources of Capital Investments in Russia, % to the total**

| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|
| Own funds | 39.5 | 37.1 | 41.0 | 41.9 | 44.5 | 45.2 | 48.1 |
| Budgetary funds | 20.9 | 21.9 | 19.5 | 19.2 | 17.9 | 19.0 | 16.2 |
| Funds of higher organizations | 13.8 | 15.9 | 17.5 | 19 | 16.8 | 13.0 | 12.7 |
| Bank credits | 11.8 | 10.3 | 9.0 | 8.6 | 8.4 | 10.0 | 9.3 |
| Shares issue | 0.8 | 1.0 | 1.1 | 1.0 | 1.0 | 1.0 | 0.9 |
| Bonds issue | 0.1 | 0.1 | 0.01 | 0 | 0.04 | 0.02 | 0.1 |
| Other | 13.1 | 13.7 | 11.89 | 10.3 | 11.36 | 11.78 | 12.7 |
| Total | 100 | 100 | 100 | 100 | 100 | 100 | 100 |

Compiled by the author according to the data from [4]

As can be seen from Chart 1, organizations practically do not use the possibilities of the stock market but often attract other external sources such as bank credits, budgetary funds and funds of higher organizations. But I suppose that in the following 3-4 years their role will significantly reduce. Why do I think so?

First of all, Russian companies cannot attract foreign banking capital. It is connected with economic sanctions and the speculative sovereign Russian rating BBB- with negative forecast determined by Fitch agency [3]. Moreover, domestic loans have become less available as a result of high key rate set by the Bank of Russia in the amount of 14% [2].

Secondly, the fall in oil prices has led to the need to change the funding of the planned budget expenditures. The budget for 2015-2016 was based on oil price 92$ per barrel while now the price is about 55$ per barrel [11].

Finally, I assume that head organizations will not invest in their subsidiaries due to general unstable business environment, volatility of exchange rates, high inflation (16.7% at the end of February 2015 [9]).

Thus, the analysis states that a promising source of economic growth in Russia is based on the financial sector, primarily, the stock market.

According to the IFRS statements of Moscow stock exchange its capitalisation was amounts to 385.9 billion dollars [5]. However, it is clear from Chart 2 the capitalisation of the Russian stock exchange is mainly determined by the largest companies.

*Chart 2*

**The Largest Russian Issuers at the end of 2014**

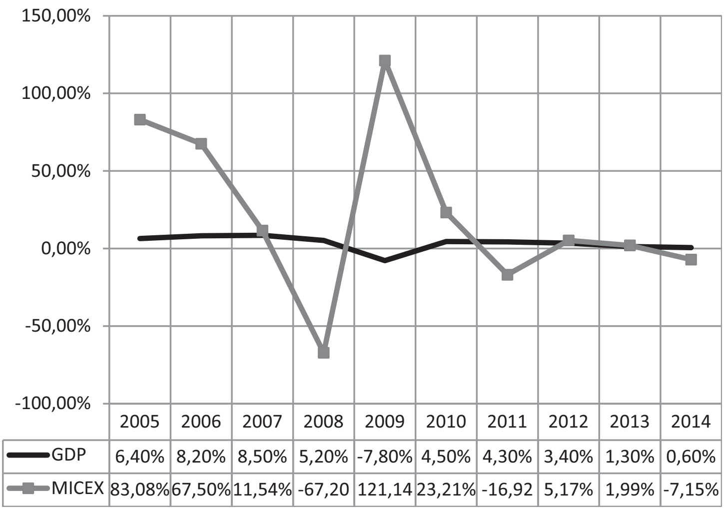
| Issuers | Capitalisation, billion dollars | % to the total market capitalisation |
|---|---|---|
| 1. Gazprom | 55.3 | 14.3 |
| 2. Rosneft | 36.8 | 9.5 |

| | | |
|---|---|---|
| 3. Lukoil | 33.5 | 8.7 |
| 4. Novatek | 23.5 | 6.1 |
| 5. Norilsk Nikel | 22.9 | 5.9 |
| 6. Sberbank of Russia | 20.7 | 5.4 |
| 7. Magnit | 16.6 | 4.3 |
| 8. VTB Bank | 15.2 | 3.9 |
| 9.Surgutneftegas | 15.1 | 3.9 |
| 10. Gazpromneft | 11.9 | 3.1 |
| Total | 251.5 | 65.1 |

Compiled by the author according to the data from [5], [10]

Thus, only 10 companies account for 65,1% of the total market capitalization which leads to separation of the real sector from the financial market. Obviously, foreign investors cannot obtain an adequate understanding of the Russian economy, focusing on public stock exchange indices. This gap finds reflection, on the one hand, in multidirectional dynamics of the growth of the MICEX index and GDP and, on the other hand, in large quantitative differences in these indicators (Picture 1).

***Picture 1.*** Dynamics of the growth of the MICEX Index and GDP, % to the previous year



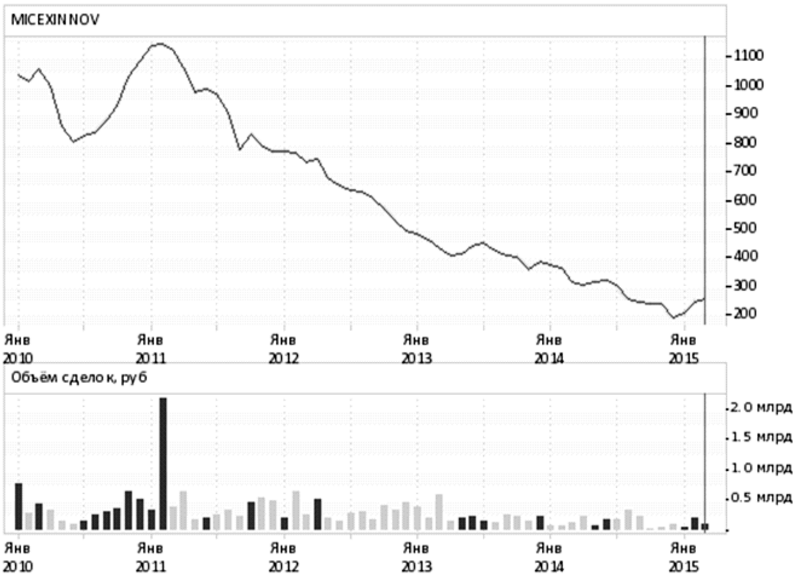

Compiled by the author according to the data from [6], [8]

I suppose that Russian financial market will represent more exactly the situation in the real sector if it becomes more available for small and medium (primarily — fast-growing!) businesses. Nowadays Moscow stock exchange (MICEX) develops innovative direction in its activities. In 2009 MICEX jointly with RUSNANO created the Market of Innovations and Investments (IIM). The main objective of it is to attract investments for development of small and medium companies. In order to get into the market a company-issuer must meet two criteria:

1) the most part of the revenues is formed through the economic activity in the industries associated with the use of innovative and high technologies;
2) capitalization is not less than 50 million roubles.

The stock exchange assists issuers; first of all, it offsets a part of the costs that are connected with the initial public offering and provides tax benefits for investors (tax capital gains at zero rate). The Market of Innovations and Investments enables high-tech, innovative companies to obtain market valuation assets, increase transparency and the value of the company, attract new investors and credit resources at reduced rates, obtain traded stocks as a tool for conducting mergers and acquisitions. The stock exchange created index "MICEX-innovations" (MICEXINNOV) that reflects the dynamics of the shares traded on the Market of Innovations and Investments.

***Picture 2.*** The dynamics of the index "MICEX-innovations" and the trading volumes on the IIM (roubles), for the entire period




Source: [7]

Unfortunately, Index shows a long-term downtrend and its short-term growth in certain periods is connected with the increase in the volume of transactions. I presume that this negative trend is due to high risks. It is obviously that investors try to act carefully and, in my opinion, it leads to low activity in the market and the fall in the stock quotes because of lack of demand. So, index goes down.

How to improve the situation? I propose several ideas.

The first is to make IIM available not only for innovative but for all fast-growing companies like it is on the similar markets — NewConnect (Warsaw), Alternative Investments Market (London), TSX Venture (Toronto), NYSE Alternext, Nasdaq Capital Market (New York).

The second is to create the stabilisation fund which for some time (5-7 months after placement) will support quotations of securities of the company at close to the cost host (to limit the downside potential). On the one hand, it will be to encourage doubters to get into paper during placement, since, the probability of its falling is weak; on the other — the company-issuer will have the time to confirm the effectiveness of the use borrowed funds and prospects of its development. The fund may be formed on the model of public-private partnership. For example, issuers applying for support should be directed by a few percent of the money received to his capital. Of course, if such a fund to appear, its activity must be due to the high number of constraints. This can be, for example, limits per issuer in absolute terms and as a share of portfolio. The representative of the fund may even be members of the board of directors of a company. Also, it is necessary a clear regulation of determination of the offering price of the shares. All these measures will allow not only reduce the risks of falling shares after the placement, but significantly improve the quality of the issuers.

The third idea is to improve promotional support for the market activities. Many private investors do not know or understand this segment and its great benefits, and the media are talking mainly about blue chips. In addition, representatives of the market may organise training seminars for students of engineering or economic disciplines and young entrepreneurs.

I believe that the Market of Innovations and Investments is one of the most important elements of the Russian innovative infrastructure. It looks like a promising platform for developing companies and their cooperation with investors and business-angels. In my opinion, it needs to be improved in order attract more perspective issuers and, as a result, to expend the understanding of the Russian economy and organize capital mobility in the real sector. Thus, development of this Market is an opportunity to improve the interaction between real and financial sectors of the Russian economy.

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# MARKETING TODAY: FRANCHISING AS A WAY OF BUSINESS DEVELOPMENT

## Abstract

*It goes without saying that starting your own business is risky. Nevertheless, there is a way to eliminate some risks — that is what is called franchising. Using the well-known brand may lead a new venture to success. Of course the entrepreneur has to pay the franchisor for it. The report which is based on factor and sector analysis would be of interest to potential entrepreneurs as well as students specializing on business.*

***Key words:*** *business, franchising.*
***JEL codes:*** *M 13.*

## 1. Introduction

"Franchising is a business relationship in which the franchisor (the owner of the business providing the product or service) assigns to independent people (the franchisees) the right to market and distribute the franchisor's goods or service, and to use the business name for a fixed period of time."[1]. So, franchising involves two parties, which agree on the terms of their partnership. Depending on the type of the franchise, franchisor gives franchisee the right to use the trademark, sell specific products or services, benefit from know-how and work according to the business-model.

Franchise agreement is the basis for the parties' cooperation. That is the contract that states the rights and the obligations of the franchisor and the franchisee. The document contains the information about the brand, the business model and the know-how shared with the franchisee, as well as the fee (initial one and royalty payments paid on the regular basis). It also restricts the duration and the territory on which the franchisee has the right to operate under the franchisor's brand. The agreement should also regulate the case when one of the parties breaks the rules or goes bankrupt.

Nevertheless, franchising is not only about the law. Of course, law is important but the other thing that is essential is relationship. Franchisor supports franchisees, franchisee sticks to the rules and commits to the increase of the brand value. This interconnection requires mutual trust and respect. That is the reason why both the selection of franchisor by franchisee and franchisee by franchisor is very important. Sometimes a person is simply not the franchisee type — he is a real entrepreneur and wants to create his own rules instead of sticking to other one's. The earlier it is found out the better because it can cause misunderstanding and opportunistic behaviour afterwards. "High level of transparency and complex partnership are both essential conditions and the advantages of franchising". [6]

The other pillar of franchising is the brand. It is practically the most important decision factor for consumer behavior. The more well-known the brand the higher the chance that the consumer opts for the particular good or service. That is based on psychology: people are more likely to trust things their brain registers most of the time. While being the most valuable asset, brand is also the most vulnerable one. Reputation is gained over time by the franchisor but actions of irresponsible franchisees may simply ruin it. That happened, for example, to "Doka Pizza" brand owned by the first Russian franchisor Vladimir Dovgan. Although the franchisor paid attention to the quality of food and services, its franchisees didn't and the brand simply lost its loyal customers. That is the reason why execution and sticking to the franchisor's rules is crucial for the brand survival. To check how franchisee is operating franchisor uses lots of methods starting from video cameras up to mystery shopping.

## 2. Franchising in Russia

### *2.1. Time-line analysis*

While the term 'franchising' dates back to ancient France and Albert Singer founded Singer Sewing Machine Company, the first franchising company, in 1851, it was not before 1990s when franchising was introduced in Russia. That has two reasons: first of all, franchising was impossible in the socialistic society and secondly, trademark institution had been practically destroyed by 1990s in Russia. The law regulating trademarks was introduced only in the end of 1992 and 1996 is believed to be the year when franchising reached Russia.

Nowadays Russian franchising market is in the phase of slow growth. At this point three main factors should be named. The information about the profitability of franchising model attracts more franchisees. Moreover, franchising serves as one of the ways to diversify the business. And last but not least large companies opt for such kind of business model to conquer new markets as new regions provide a vast range of opportunities for business development.

When compared to other ways of expansion, such as organic growth or mergers and acquisitions, franchising seems to be the most attractive for business owners. The main comparative criteria are presented in the table (see Table 1).

*Table 1*

**The comparison of the ways of business development**

| Criterion | Organic growth | Franchising | Mergers & acquisitions |
|---|---|---|---|
| **Speed** | Minimal | Average | Maximal |
| **Risks** | Minimal | Average | Maximal |
| **Investment capital profitability** | Average | Maximal | Minimal |
| **Investment volume** | Average | Minimal | Maximal |

The history of franchising in Russia may be split into 3 main periods. The first one, so called "The appearance of franchising in Russia" lasts from 1992 up to 1998 and is characterized by the foundation of the first Russian companies operating under franchising business model. Vladimir Dovgan was the first Russian franchisor. He founded such companies as "Doka Pizza" and "Doka Khleb". Moreover, that was the time when numerous foreign franchises, such as Buskin Robbins and Subway appeared on the Russian market. In 1997 Russian Franchise Association — RFA — was founded in order to support franchising in Russia. Nevertheless, robust franchise boom was interrupted by the economic crisis in 1998. The number of franchises significantly decreased afterwards.

The second period (1999-2003) may be characterized as stagnation because disregarding fast supply growth the demand remained low and franchising business transparency was extremely low. There were about 1000 franchises at that time.

The third period, so called formation, started in 2003 and continues up to now. That is the time when numerous franchising consulting companies emerged. Both demand and supply increased and so did franchising market transparency. Consistent growth was interrupted by 2008–2009 crisis which reduced the franchise number. The supply became more diversified at that time.

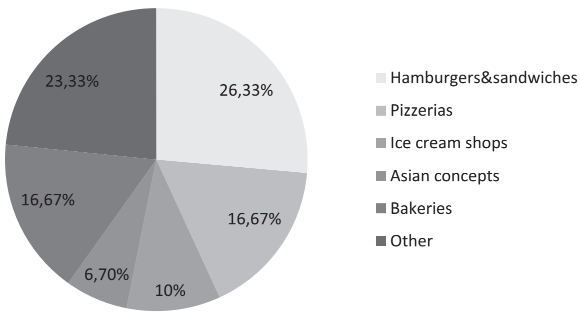
2014–2015 are also very tough for the Russian economy. Some foreign franchisors, such as Wendy's, decided to quit the Russian market but others, on contrary, provided more favorable business conditions, e.g. decreased the royalty. Moreover, economic challenges create new opportunities for Russian franchisors that benefit from the changes in consumer behaviour. Discount bar chain KILLFISH, for instance, economizes on costs but provides beverages at a lower price for young customers.

### *2.2. Fast-food franchising in Russia — sector analysis*

After examining Russian franchising business market in total let us have a look at fast-food market in particular. This choice is determined by several factors. First of all, fast-food in Russia is growing not only in terms of volume but also in terms of POCs' (point of contact) number. Second, the industry survives the crisis period better than food market in general due to the tendency to save up money on food in hard times. Finally, crisis attracts investors to real business rather than financial assets.

For the sake of research the author has gathered information about 60 fast-food franchises on the Russian market. Russian fast-food market embraces numerous concepts where traditional burgers and sandwiches are prevailing (26.3%). They are followed by pizzerias and bakeries (16.67%) and ice cream shops (10%). Asian concepts, e.g. Japan, Chinese and Korean ones, have insignificant share. "Other" category includes mobile cafes, cafes serving Russian national dishes as well as new concepts such as bubble tea or frozen yogurt cafes (see Chart 1).

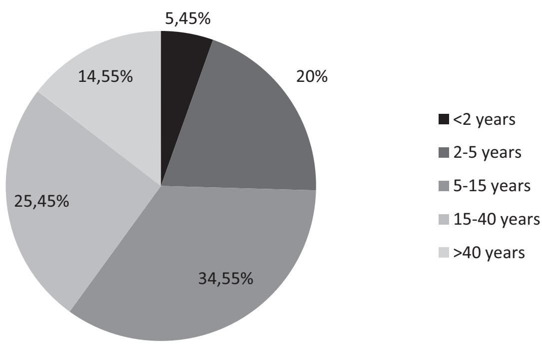
***Chart 1.*** Fast food concepts on the Russian franchise market.




***Source: Author's*** *research, 2014.*

As brand is the cornerstone of franchising the period of its existence on the market is an extremely important factor when it comes to a franchise purchase. The older the brand the more loyal customers it has. The research shows that the majority of Russian fast food franchises (approx. 95%) are more than 2 years old (see Chart 2). Moreover 40% of brands are older than 15 years old. The oldest brand is Carl's Jr operating since 1941, while BIG ONE and La Pizza Espresso which appeared in 2013 are the youngest ones.

***Chart 2.*** Fast food franchises by operating experience.




***Source: Author's*** *research, 2014.*

### *2.3. Recommendations for potential franchisees*

The next step for a potential franchisee after investigating the industry is the choice of franchise itself. The problem is that the franchise financial parameters incl. profitability and return on investment are usually exaggerated by the franchisor because it varies greatly by region and format and the main franchisor's aim is to sell the franchise. Furthermore, some franchise concepts are too young to be estimated in terms of financial patterns. So, it is crucial for the business success to track quantitative and qualitative criteria carefully. Quantitative criteria include:

- *Franchise age:* the more the age, the more known the brand and the more chance for success;
- *Number of operating franchise POCs* (The principle is not "The more the better" but "The more profitable the better");
- *Multifranchisee number:* multifranchisee owns more than 1 franchise of specific brand. E.g. ROSINTER is proud that practically all its franchisees own at least 2 franchises.
- *Contract term to payback period ratio:* if the second one exceeds the first one, franchise purchase is useless.
- Except quantitative there are numerous qualitative criteria:
- *Trademark registration*, to avoid frauds;
- *Franchisor's responsibility for the business success*, which may be reflected in the high franchisee requirements in terms of initial capital and business standards;
- *Information transparency from the franchisor's side* (incl. negative cases concerning franchise closure reasons);
- *Current franchisees' satisfaction level* (support, communications, franchisor's reaction speed etc.) Potential franchisee should talk to the current franchisees but not only to franchisor in order to find out all partnership details and peculiarities.

And finally buying a franchise is an important step that needs a lot of pre-work, so you should be very careful if the franchisor hurries you with the decision-making.

## 3. Conclusion

Franchising business model helps eliminate some business risks, on the one hand, but provides certain restrictions for entrepreneur, on the other. Its three main pillars are law, brand and relationship. Though it is a common practice in international scope, Russian franchising market is comparatively immature and was established only in 1996. It is young and lacks transparency. Nevertheless, it is growing and developing even in the crisis period. Tough economic period provides new challenges and opportunities. Taking new trends of consumer behavior into account may lead the company to success. "Problems and downtimes will happen in business. Having an established rapport with consumers can help businesses be resilient when difficulties arise” [2].

Fast-food market is comparatively less vulnerable to crisis and is unsaturated in Russia. It embraces different concepts. While traditional hamburgers and sandwiches are the market leaders new trends such as bubble tea and frozen yogurt are becoming more and more popular. The vast majority of fast-food franchise brands have more than two years of operational experience. This criteria is very important while making the business decision because it is very risky to choose brands that are too young to be well-recognized.

In conclusion, choosing a franchise is a very responsible step. Potential franchisees should take both quantitative and qualitative criteria into account. Financial parameters such as profitability and payback period are insufficient because the figures franchisor provides do not always reflect the reality. Information from current franchisees really matters as it shows franchisor’s attitude towards the partners.

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# RUSSIAN-CHINESE EFFORTS IN ESTABLISHING A MULTIPOLAR WORLD

## Abstract

*We cannot but agree with the statement that the world is in difficult political and economic conditions. Developed countries try to keep their dominant position in the world, while developing states do not want to tolerate this state of affairs. This leads to the fact that states which increasingly gain power in the international arena, actively unite in groups with common interests, views, similar economic goals. States in such unions actively coordinate positions with each other in economic, political, and cultural issues. A vivid example of such interaction represent relationships between such great powers as Russia and China. The two countries actively cooperate in many areas: trade of goods and natural resources, support each other in the framework of international organizations, the desire to strengthen their national currencies. All this is done in order to make a world order multipolar. In which all states would have equal rights and opportunity to influence the political and economic situation not only in the country but in the world.*

***Key words:*** *Russian-Chinese relations, multipolar world*
***JEL codes:*** *F01, F15, F29.*

## Introduction

Relations between Russian Federation and People's Republic of China have been developing for the last 400 years. At the present stage they are characterized by close cooperation in such spheres as different summits, trade and economic relations, cooperation in United Nations Security Council, participation in international regional organizations (SCO, BRICS). Today in the situation of unbalanced global economy countries begin to deepen and to strengthen their relations and unite their efforts in establishing a multipolar world.

## Modern picture of the world

Multipolar world is a system of international relations when there are several centers (governments or groups of governments) of political, cultural and economic influence on other countries in purposes of providing world stability and security.

Almost the entire 20$^{th}$ century world order was bipolar with the Union of Soviet Socialist Republics and the United States of America led, but with the collapse of the USSR and the end of the Cold War international system transformed in unipolarity and the US became as the only superpower. In a unipolar system the power of a state is not balanced and controlled by the other states.This inequality allows the hegemony of the international system to influence the rest of the world. In the last decades we are witnessing the lack of respect for the international community rules tainted US image as a benign superpower. However this loss of influence, together with a slow decline of the hegemon and a rise of new powers, would suggest that US unipolarity could not last forever.

Nowadays we can see that the USA actively offers to European countries to combine their power for solving global problems on the base of common interests and points of view at the present situation. The purpose of this approach is the saving of hegemony in determination of the direction of development of the main economic and political processes in the world. As an example of this situation we can remember that NATO extends increasingly.

However there are some countries that are not agree with such state of affairs. It is commonly said that the world is entering a multipolar phase in global governance with the "rise of the South" or the increasing powers of emerging economies Southeast Asia, BRICS, Islamic World, countries of the Middle East, post-Soviet space, Latin America.

## Russian-Chinese Joint Declaration on a Multipolar World

Russian-Chinese joint efforts in this field began in 1997 with the Russian-Chinese Joint Declaration on a Multipolar World and the Establishment of a New International Order. This document is based on principles of trusting partnership, strategic interaction in the twenty-first century and coinciding approaches to major international issues.

According to the declaration countries established the following provisions:

1. "In a spirit of partnership, the Parties shall strive to promote the multipolarization of the world and the establishment of a new international order.
2. The Parties are in favour of making mutual respect for sovereignty and territorial integrity, mutual non-aggression, non-interference in each other's internal affairs, equality and mutual advantage, peaceful coexistence and other universally recognized principles of international law the fundamental norm for conducting relations between States and the basis for a new international order.
3. The Parties are in favour of establishing a new and universally applicable concept of security. They believe that the cold-war mentality must be abandoned and they oppose bloc politics. Differences and disputes between countries must be settled by peaceful means, without resorting to the use or threat of force. Dialogue and consultations must be pursued with a view to promoting mutual understanding and confidence, and

peace and security must be sought through bilateral and multilateral coordination and cooperation.

4. The Parties are of the view that the role of the United Nations and the Security Council must be strengthened, and they highly appreciate United Nations efforts to maintain world peace and security. They believe that the United Nations, as the most universal and authoritative organization of sovereign States, has a place and role in the world that cannot be supplanted by any other international organization. The Parties are confident that the United Nations will play an important role in the establishment and maintenance of the new international order.
5. The Parties stress that numerous developing countries and the Movement of Non-Aligned Countries are an important force that promotes multipolarization and the establishment of a new international order. Interaction among developing countries is gaining momentum. Their role in international politics is growing, and their share in the world economy is increasing. The rise of the developing countries will provide a powerful impetus for the historical process of establishing a new international order. These countries should take their rightful place in the future new international order and participate in international affairs on an equal and non-discriminatory basis.
6. The Parties note with satisfaction that the establishment and development of a Russian-Chinese partnership based on equality and mutual trust for the purpose of strategic interaction in the twenty-first century is in keeping with the development of the international situation and international relations in the post-cold-war era, fully meets the vital interests of the peoples of the two countries and is conducive to peace and security in the Asia-Pacific region and the world as a whole.
7. Mankind is on the threshold of a new era. The peoples of all countries are faced with the increasingly urgent question of the kind of international order they will live under in the next century. The Parties call on all countries to engage in an active dialogue on the establishment of a peaceful, stable, just and rational new international order, and they are prepared to take part in a joint discussion of any constructive proposals to this end" [1].

Both Russia and China endeavor to apply these principles, based on peace cooperation and development, in dealing with political issues for the past almost 20 years thus attempting to establish the equal importance of all countries in the international arena.

## Russian-Chinese relations nowadays

At present we can see that last several years are characterized by increased interaction between Russia and China in different spheres. Especially at the last months of 2014 series of significant bilateral agreements were signed.

The most important of these documents is a gas contract which was labeled "deal of the century". It provides for the supply of more than thirty cubic meters of gas fuel annually for thirty years. For selling of gas countries will have to build required infrastructure over the next few years but in spite of it main important consequence of these documents is that Chinese People's Republic may become the largest consumer of Russian gas resources. So Russia will reduce its dependence on the European consumers and become a competitor for shale gas produced in the US.

The energy sector also provides a great opportunity for the future cooperation. For example "Rosneft has offered a 10% stake to Chinese authorities for the project of joint exploitation of Vankor oil field in Eastern Siberia, Rosneft's third-largest onshore production subsidiary"[2]. Thereby Chinese participation in Russian oil industry will expand and Moscow will offer oil for sale in Yuan.

Payments in national currency become more and more frequent practice in Russian-Chinese relations. What is more these payments are made in different spheres: from the energy sector to military and technical cooperation. Direct relations between Russian banks and Chinese financial institutions allow to minimize expenditures which are connected with exchanging of rubles and Yuan for dollars.

Many experts suppose that this step (connected with rejection of the dollar in the payments between the two countries) hurts American dollar and creates constraints for the dollar and the monetary policy of the USA. However the main role in removal of the economy from the dollar belongs to ordinary consumers and producers. American currency is still very attractive for both Russians and Chinese. Thus governments have to increase trust to ruble and Yuan for simplifying and reducing the cost of international transactions.

Except of relations connected with energy sector and currency calculations Russia and China aim for an alliance in such spheres as economics, politics and military cooperation, increase Chinese investment in the Russian economy. One of the purposes of this union is not only deepen and strengthening of relations and collaboration between countries but also the restraint of NATO near the Russian state boundary and balancing of the forces in Asia-Pacific.

## Prospects of Russian-Chinese relations

We can say with confidence that relations between two countries will only deepen and strengthening eventually. Russia and China continue to consolidate their points of view on the major events in the world, improve mechanisms of practical cooperation and of coordination of actions in the international arena.

Obviously in the coming years Russia and China will accelerate the pace of development of bilateral relations in different spheres: cultural, economic, political and cooperation and joint efforts in international relations and such summits as SCO and BRICS.

Prospects of Russian-Chinese relations are very optimistic and there are several reasons for it:

1. The absence of serious contradictions in bilateral relations. They do not strive to impose any points of view to each other and have not any territorial disputes.
2. Both Russia and China have common idea for establishing of new world order according to which developing countries will have more social, political and economic freedom. They tend to eliminate the influence of the western world and make the rule of law the basis of international relations.
3. They collaborate actively and successfully in such international organizations as BRICS and SCO.

Talking about economics we can notice that in the oil and gas sector long-term contracts were signed. So Russian natural resources will be more and more actively supplied to China. Except of this, about 50% of turnover can be transferred into rubles and Yuan. That will be achieved if countries liberalize their monetary policy.

But there is a fly in the ointment. Chinese economic recovery is very rapid. This country has made a qualitative leap in economic development in a short period of time and now its economy is developed significantly better than the Russian one. So in this conditions both Russia and China have to be very cautious in bilateral policy. For Russia it is important to save the balance in active interaction with China and adoption of assistance, however to develop independently and do not allow to its partner to subjugate Russian economy.

In this way it can be said that Russian-Chinese relations have been developing for hundreds of years and nowadays we can see probably the closest relationship between two countries. And to save it in so actively developing form states have to respect and maintain each other in difficult conditions of unbalanced global economy.

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