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Expanding FDI localization and linkages in the Russian Federation: Perspectives of firms and lessons from global experience

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Introduction

Increasing the participation of local firms in the supply chains of larger foreign and domestic investors has long been viewed as one of the primary channels for upgrading the technology, management practices, and competitiveness of the domestic private sector. While there is widespread consensus on the market failures that limit these supply chain linkages from forming – incomplete markets, coordination failures, and weaknesses in the business environment among the greatest - there is far less consistent evidence on which policies have the greatest impact on catalyzing their formation. Many of the local content requirement and import substitution policies that were common in the 80s and 90s (and persist today in many cases) have had mixed results, with reduced competition for domestic firms leading to a deterioration in competitiveness. For that reason, these policies are increasingly being replaced with more market-based approaches. These target knowledge and productivity spillovers from FDI and domestic value addition, including incentives and capacity building for firms, as well as regulatory reforms addressing market failures.

The Russian Federation has followed a similar trajectory. In the 90s and 00s, linkages required a largely local content approach; today, however, there is a transition to greater reliance on support programs to help local firms upgrade their internal capacities to work with larger investors. This is reflected in a set of ambitious national goals to be met by 2024 related, among other directions, to the development of entrepreneurialism and of small to medium-sized enterprises. The goals include specific targets to boost the cooperation between Russian SMEs and larger foreign and domestic investors. It should also be noted that many large investors in Russia implement their own supplier development programs, either built on their firm's global practices, or customized programs for their operations in Russia.

The World Bank has been an active participant in the funding, design, and implementation of linkages projects in countries around the world including the Czech Republic, Serbia, Macedonia, Mexico, Turkey, Vietnam and the Philippines. In order to support the development of linkages at the federal and regional levels in Russia, the World Bank has undertaken the following analytical study, which includes interviews with foreign companies located in Russia and focus groups with Russian SMEs, to better understand the constraints and potential for developing this cooperation. In addition, the Bank's team has analyzed international experience from several comparator countries to identify success factors in developing backward linkages that may be applicable to the Russian Federation.

Based on this global experience, the report concludes with a set of actionable recommendations that should help policy makers and private sector stakeholders take an evidence-based and strategic approach to the design and implementation of these programs.

Executive summary

The aim of this study is to propose practical measures based on Russia's existing experience and international evidence to increase linkages between foreign investors (referred to in the report as FDI and Multi-National Corporation (MNC) affiliates interchangeably) and domestic SMEs.

Chapter 1 highlights the key success factors for promoting FDI linkages and capturing spillovers from FDI based on a review of five international examples (Singapore, Malaysia, Thailand, Czech Republic and Ireland). The chapter assesses public and private sector factors, including the host country conditions to attract FDI, government objectives, and the specific policies and programs implemented.

The case studies demonstrate the importance of targeting support to local companies that are more ready to pass the supplier criteria of MNCs or to become longer-term partners of MNCs, rather than doing more generic capacity building for all firms. Successful support programs are informed by comprehensive strategies aimed at strengthening the supply capacity of local companies through market-based approaches enhancing their competitiveness and productivity. The cases from Ireland, Malaysia, and Thailand point at the need to develop technical and management skills within local companies. Countries often use incentives aimed at training & skills, R&D, high-tech and higher value-add production, and local sourcing to strengthen the technology and skills acquisition of local firms. For example, these incentives were successfully applied in Malaysia and Singapore.

The examples present different institutional set-ups of the linkages programs, but they all were aimed at a widely communicated policy goal, well-funded and coordinated by an entity covering the whole policy agenda. In addition, most policy initiatives on promoting FDI linkages apply horizontal policies such as taxation, infrastructure, red tape reduction, intellectual property protection, contract enforcement, competition policy, finance, and measures that impact the overall competitiveness of an economy.

Chapter 2 provides some context for the development of FDI linkages in Russia. Attracting FDI (and diversifying FDI outside of the energy sector) is a major priority of the Russian government, supported by a wide range of legal and regulatory reforms, investments into hard infrastructure, and the creation of various incentive programs to facilitate inward manufacturing FDI. Between 2008 and 2017, the total volume of FDI in Russia was approximately 420 bln. USD with a peak in 2013 and a significant drop from 2015. These investments were placed in 2,705 of announced FDI projects, of which 1,077 were in manufacturing.

There is limited data available on the spillovers from this FDI into the domestic private sector. Many of these projects were done under incentive regimes that included specific local content requirements and, as a result, some clusters of local supplier capacity have emerged, most notably in the auto components industry. Many other incentives have been explored to promote localization of supply.

Chapter 3 summarizes the institutional context for linkages and more broadly for SME support in the Russian Federation. The main institution responsible for the development of linkages between MNCs localized in Russia and Russian SMEs is the MSP Corporation (the "Federal Corporation on the Development of Small and Medium Entrepreneurship"). The MSP Corporation provides financial and non-financial support to foreign firms and domestic SMEs under the national project "Small and medium entrepreneurship and the support for the individual entrepreneurial initiative". Activities are aimed at increasing SMEs' share in procurement from large domestic companies with state participation as well as building linkages between SMEs and foreign investors.

In addition to the MSP Corporation's activities on linkages, regional agencies implement a wide range of services and projects more broadly aimed at increasing SME capacity. A survey of 20 of these regional agencies was conducted and found that only a half of them conduct any activities related to the facilitation of FDI linkages.

Beyond these state institutions, most bilateral and multilateral trade organizations and associations (eg the Foreign Investment Advisory Council, AMCHAM, etc) have active working groups and initiative helping foreign investors find domestic suppliers. Many MNCs also implement their own activities not only to find domestic suppliers but in some cases, to build the capacity of their core suppliers (eg Mondelez Rus, Anheuser-Busch InBev Europe and Saint-Gobain).

Chapter 4 analyzes the results of the survey of MNC Russian affiliates in the automotive, chemicals, and machinery industries. The survey included 45 companies engaged in production or assembly in the Moscow, Saint-Petersburg and Nizhny Novgorod regions. The majority of respondents plan to expand their production in Russia. These firms mostly source basic inputs and raw materials from local suppliers and, as a result, the value addition of local content is very low. MNC affiliates (with the exception of the chemicals industry) are sourcing some intermediate goods locally, but the share is low (18% in the machinery industry and 12% in automotive). Services are mostly sourced locally and include transportation, maintenance, IT, utilities, repairs & packaging, warehousing, customs brokering services, etc. However, most of the value-added engineering and R&D services are imported.

A majority of the surveyed companies would like to source more material inputs locally (90% consider it a priority) but this is hampered primarily by quality issues and by the lack of compliance certification with management and production systems.

The highest rated barriers for local sourcing included:

- A complete absence of local production for the necessary inputs;
- Inability of the Russian suppliers to meet the MNCs standards related to quality, cost and delivery;
- Difficulty in identifying and communicating with Russian suppliers;
- Low design and innovation capabilities of the Russian suppliers;
- Lack of management capabilities at the Russian companies.

Most of the respondents are familiar with the key state support measures for FDI localization such as special investment contracts. Greater awareness of support measures by MNC affiliates is correlated with a greater rate of localization.

Finally, according to the respondents, the main areas where support is needed for suppliers includes financial measures to help suppliers access better production technologies, support for certification with management and production systems, and strengthening the intermediary role of business support agencies.

Chapter 5 presents the results of focus groups of existing and potential Russian SME suppliers that were conducted in the same regions and industry groups as the FDI survey. The interviews were focused on getting supplier perspectives on cooperation with foreign investors including the opportunities, challenges, and role of the state in facilitating such linkages. 32 SMEs participated in the focus groups, of which 43% are currently supplying a foreign firm with the remainder preparing to in the future.

There were many similarities between the feedback from the suppliers and the FDI companies. Both groups have a clear intention to increase their participation in linkages and believe it is in their economic

best interest to do so. Both also cite some common constraints including a lack of specific information on supply and demand, difficulty in suppliers achieving compliance on product standards and quality systems, and the need to increase finance for investments in meeting quality requirements. Suppliers also mentioned some constraints including the low volume of order from FDI companies relative to the investment needed to meet the requirements for these orders, as well as several regulatory issues such as customs compliance and certification requirements.

Finally, Chapter 6 provides a set of recommendations to expand linkages, primarily by scaling up support for market-based programs at the regional and sector levels complementing the ongoing federal activities.

At the federal level, the legislative and institutional structure for linkages development is relatively clear with a strong lead agency in the MSP Corporation. However, given the size of the Russian Federation and the great diversity among regions in their economic structure and FDI strategies, it is recommended to complement the federal program with greater local capacity at the regional and/ or sector level to design and implement linkages initiatives. Such an approach would build on existing regional capacity to work with SMEs on related topics such as export support and productivity.

Specific recommendations include the following:

Recommendation 1: Develop strategic linkages action plans at the local and/ or sector level

- 1.1 Take stock of lessons learned and success factors in existing linkages initiatives – both public and private
- 1.2 Conduct a comprehensive regional or sectoral mapping
- 1.3 Clarify institutional roles and responsibilities
- 1.4 Articulate regional and/ or sector level linkages action plans

Recommendation 2: Implement the action plans with market-based policies and products

- 2.1 Deploy an appropriate mix of financial and non-financial products including: Supplier readiness testing, targeted supplier development programs, support for intensive technology innovation and upgrading, targeted matchmaking events and information resources, and training and methodological support for SMEs, regional governments and business development institutions
- 2.2 Implement a targeted information campaign
- 2.3 Put in place a robust M&E system to allow for impact evaluation and real time modifications to program activities

1. FDI linkages development: international experience

Key findings

- FDI can strengthen the competitiveness of domestic enterprises through involving them in MNCs' supply chains
- MNCs' willingness to create local linkages can be reinforced by the linkages programs that are aimed at widely communicated policy goals and implemented in cooperation with MNCs
- The main pillars of a typical linkage program include: (1) an enabling environment, (2) targeted FDI attraction, (3) linkage promotion services and (4) absorptive capacity
- The support and incentives should be targeted to those local companies that have the ambition and potential to become long-term partners to MNCs
- Policy initiatives on promoting FDI linkages should also apply horizontal policies that impact the overall competitiveness of an economy

1.1 The role of FDI spillovers

An important driver in upgrading both the labor force and firms to strengthen the competitiveness of domestic enterprises in Russia. International investors create demand for new products and skills, provide new know-how and guide the development of new productive capacities. A number of studies have shown that manufacturing FDI may bring stable capital inflows, job opportunities, technology transfer, and access to foreign markets, including integration into global value chains (GVCs). FDI also has positive spillover effects on local firms through increased productivity and skills formation.¹ These opportunities for MNCs to invest, create jobs, and expand are supported by a sound investment climate, which also influences the extent to which knowledge spillovers from FDI are captured and how locally connected FDI firms operate.

Supply chain linkages are an important channel through which FDI firms transfer technology, know-how and management practices. While the literature broadly distinguishes two channels of spillovers², this study focuses on vertical supply chain linkages as they hold greatest promise to raise firms' productivity and connect local firms to GVCs.³ They include 'forward linkages', when the goods and services provided by FDI firms are used as inputs in local industries, and 'backward linkages', which occur when local firms become input or service suppliers to FDI. A recent study comparing the effectiveness of both channels among high-growth firms shows that supply chain linkages are more pronounced in fostering spillovers, measured in improved productivity.⁴

The process of creating local supply chain linkages is by no means automatic. It is a function of multiple factors that can broadly be categorized as (i) the characteristics of FDI; (ii) the absorptive capacity of domestic firms; (iii) the host country's business policy and institutional environment. The scope and scale

¹ Manufacturing FDI in Sub-Saharan Africa: trends, determinants, and impact. World Bank Group, 2015 (<https://openknowledge.worldbank.org/bitstream/handle/10986/22352/Manufacturing00minants00and0impacts.pdf?sequence=1>)

² (1) Demonstration effects (firms imitate foreign technologies or managerial practices through observations or hiring workers trained by FDI companies) and (2) supply chain linkages effects (economic relationships between FDI and local firms in the host economy along or between value chains).

³ First and foremost, through creation of backward and forward linkages. Supply chains are vertical inter-sectoral linkages which can be further categorized as "downstream" (forward) or "upstream" (backward) linkages. See Havránek and Iršová (2011, 2013) and Alfaro-Urena, Manelici, Vasquez (2018, forthcoming)

⁴ Reyes in World Bank Group (2017a, Chapter 2)

of vertical linkages and technology transfers can vary significantly between countries due to a complex set of “mediating factors” at play in this process (Figure 1). These factors need to be understood to realistically assess the size of the opportunity and determine which policies to prioritize.

At first, policy-makers designing linkage programs need to understand the demand-side of the equation. The characteristics of MNCs in the host economy, investor motivations, value chain organization and global sourcing strategies all play critical roles in determining the potential for localization of production and opportunities for local entrepreneurs to become suppliers. Furthermore, the governance of the value chains in which these investors operate has a big influence on the sourcing discretion of in-country manufacturing or assembly operators. Host country characteristics such as an open investment and trade regime, learning and innovation infrastructure, the degree of market competition, adherence to intellectual property rights and contract enforcement, and the public sector’s institutional capacity not only determine an economy’s attractiveness for FDI, but can also help or hurt the formation of local linkages. On the supply-side, the width and depth of the pool of local firms available and their capacity to absorb new information, technologies and practices are key determinants that shape opportunities for local linkages.⁵

International experience proves that investing time and resources in promoting FDI linkages and upgrading local firm capacity pays off. MNCs around the globe rate the potential to link with local firms based on the capacity and skills of local suppliers as an important criterion in their location decision.⁶ Hence, a competitive domestic supplier base is a means and an end to attracting more FDI. By increasing FDI linkages with local firms, investors are more embedded in the host economy, which encourages them to apply a longer-term perspective, while strengthening in-country value addition and investment expansion.

Local sourcing may have several advantages for MNCs, if competitive suppliers are available, but imports remain important. Generally, local sourcing reduces risks and disruptions, transportation costs, lead times, and increases flexibility. Although foreign affiliates may have an interest in creating and strengthening local linkages, their willingness to do so is influenced and reinforced by government policies addressing market failures at different levels of the linkage formation process. In this regard, a multi-faceted and comprehensive approach to building and deepening linkages needs to bring together the public and private sectors in creating linkage opportunities and ensuring their effective implementation. Successful strategies tend to require a mix of policy measures improving the investment climate, targeted FDI promotion, matching services and capacity building of domestic suppliers.

Foreign investors and domestic firms often face market failures, providing a role for government. Foreign investors that provide potential for spillovers to the host country may face the following constraints as they attempt to link with domestic suppliers: (i) lack of competitive local suppliers due to incomplete markets, (ii) lack of information on domestic suppliers and their capacities, and (iii) negative externalities related to a lack of intellectual property rights (IPR) and possible poaching of productive suppliers. Likewise, domestic suppliers face a set of constraints that hinder the formation of FDI linkages. Typical market failures include incomplete capital markets (lack of access to finance), incomplete labor markets (lack of skilled workers) and information failures (missing information on buyer sourcing strategies and standards).

Coordination failures at policy or institutional level often play an important role in explaining sub-optimal localization and technology transfer outcomes. A government’s role in promoting FDI linkages is generally three-fold: an information provider, facilitator or regulator.⁷ The investment climate and, in particular, the national strategy for FDI linkages needs to be consistent with and supported by all relevant policies to attract higher FDI inflows. The specificity of each country needs to be taken into account,

⁵ Farole and Winkler (2014)

⁶ World Bank Group (2017), p. 21

⁷ Farole and Winkler (2014), p.4.

including factors such as human capital and technological capacity. This agenda thus straddles across multiple ministries and agencies as it is affected by policies focused on investment, industry and entrepreneurship, education, trade, competition, and taxation, amongst others. It is therefore not surprising that successful international case studies all rely on a strong lead institution that drives the efforts and ensures necessary government policy coordination to address the constraints identified earlier.

1.2 Findings of case studies

As part of this research, a set of five case studies were evaluated, covering Singapore, Malaysia, Thailand, Czech Republic and Ireland. These cases are presented in more detail in Annex 1. The international examples provide useful insights on the common features of successful linkages programs across varying political and economic contexts. Table 1 provides a summary of the key features of each case and some of the relevant lessons for the Russian Federation.

Table 1. Summary of case studies

Common features
<ul style="list-style-type: none"> • Linkages promotion as an integral part of an outward-oriented economic vision providing adequate policy commitment, finance, and long-standing focus; • Comprehensive linkages programs include capacity upgrading, information and matching services, the provision of an enabling investment climate as well as hard and soft support infrastructure; • Emphasis on transforming local firms through targeted interventions following MNC demand to prioritize competitiveness levels; • Tailored incentives for skills upgrading and supplier engagement; • Strong focus on building relationships and trust between public and private sectors, MNCs in particular; • Dedicated lead agency or institutional network with sufficient political clout to convene stakeholders.

Strategy	Policies and programs	Key lessons for Russia
Singapore		
<ul style="list-style-type: none"> • Focus on FDI and large international firms to foster spillovers and linkages to support SME upgrading and internationalization as part of an export-led growth vision • Careful but deliberate management of transition into higher-skilled activities and higher value-add exports based on comparative advantage assessment • Work with existing FDI and focus on expansion of tasks (e.g. HQ) accompanied by active FDI 	<p><u>Local Industry Upgrading Program (1986)</u>: forging linkages by encouraging MNCs to “adopt” SMEs in their value chains, following 3 progressive stages:</p> <ul style="list-style-type: none"> • Stage 1 - local SMEs sought to acquire the necessary skills / technology and MNCs supported by seconding an employee to the SME; • Stage 2 – transfer of new products and processes to SME; • Stage 3 - joint research and product development between SMEs and MNCs. <p><u>Partnerships for Capability Transformation (2010)</u>. Since LIUP remained short of results on joint R&D, PACT was introduced to push diversification and innovation to deepen linkages. It promotes productivity improvement of existing suppliers, encourages the localization of existing product lines through supplier upgrading, and provides incentives for new product introduction through investing in, and supporting SME innovation. MNCs</p>	<ul style="list-style-type: none"> • Involvement of MNCs in the public support activities • Incentives both to MNCs and SMEs • Coordination of policies at the national level to provide a complete set of tools and incentives for SMEs to develop their capacity as suppliers • Significant financial and consultancy support under the supplier development programs • Active matchmaking efforts

Strategy	Policies and programs	Key lessons for Russia
promotion with selected incentives regimes	<p>and large local companies are encouraged to identify and implement collaborative projects between them and local SMEs, and conduct different stages of product development together (from concept to pilot runs) supported by public cost-sharing arrangements.</p> <p><u>Proactive matchmaking support</u> that concentrates on forging technology partnerships and internationalization of SMEs and helps FDI search for and identify suitable local suppliers.</p>	
Malaysia		
<ul style="list-style-type: none"> Attraction of efficiency-seeking and exporting manufacturing FDI, in line with targeted regional development strategies From SME support with socio-economic goals achieving mixed results to linkage promotion accepting most competitive firms to respond to MNC demand; Strong partnership focus between public and private sector (domestic and international) building trust and ensuring demand-led solutions; Emphasis on providing world-class industrial eco-system, including workforce skills, quality infrastructure, firm capabilities, transport infrastructure etc. 	<p><u>Vendor Development Program (1988)</u>. The goal was to link local SMEs to foreign affiliates through joint ventures or sub-contracting.</p> <p><u>Industrial Linkage Program (1996)</u>. The goal was to build linkages between MNCs and local firms by offering tax incentives to improve SME capabilities for those suppliers producing eligible products as well as for those MNCs incurring costs by helping the supplier to upgrade.</p> <p><u>Global Supplier Program (2000)</u> emphasized the compliance with MNC criteria and training needs, and funds training and skill development for SMEs to make them more effective participants in global supply chains. MNC representatives are involved in design and content of the specific training programs and participants are selected based on MNC criteria.</p> <p><u>Tax and other incentives provided</u> to foster FDI linkages and improve suppliers' skills.</p> <p><u>Penang Skills Development Centre</u> - training and services (e.g. testing facilities) for electrical engineering, electronics and other areas, organized around the specific needs and gaps identified by foreign multinationals in the local industry.</p>	<ul style="list-style-type: none"> Use of tax incentives both for SMEs and MNCs Training of SMEs to meet the demands of MNCs Importance of involving the private sector, universities, and vocational training institutions in the development of FDI linkages

Strategy	Policies and programs	Key lessons for Russia
Thailand		
<ul style="list-style-type: none"> • Linkages as a natural extension of FDI-driven cluster and sectoral policies that establish the necessary infrastructure and eco-system for manufacturing activities • Embracing FDI (OEMs and suppliers) as a conduit for developing internationally competitive clusters and supplier base • After period of prescriptive local content requirements, it became apparent that liberalization needed to go hand-in-hand with SME development support 	<p><u>Supporting Industry Master Plan (1995)</u> - key policy for the development of Thai supporting industries in the automotive and electric and electronics sectors:</p> <ul style="list-style-type: none"> • attracting investment of foreign suppliers and promoting technical collaboration with foreign companies, • provision of information and matchmaking services was targeted, • financial support services to assist the creation of linkages, • support to upgrade technology and production methods, human resources and management skills, <p><u>FDI incentives schemes</u> to encourage foreign OEM investors to relocate together with their key suppliers to Thailand (investment benefits granted to the OEM would also be extended to the suppliers being part of one large project);</p> <p><u>Ongoing support from the Board of Investment / Ministry of Industry:</u></p> <ul style="list-style-type: none"> • tailored sourcing and matchmaking services on demand supported by access to regional supplier database; • providing technical and managerial support to firms in supporting industries in order to increase the local productive capacity <p><u>Automotive Human Resource Development Program</u> - industry-led initiative to improve the quality, cost, and delivery performance of 100% locally owned suppliers through human resource development via training of trainers.</p> <p><u>New investment policy (2015)</u> - a combination of activity-based (knowledge-intense, value-added, high technology content, etc.) and merit-based</p>	<ul style="list-style-type: none"> • Integrating SME development in the policy mix is crucial to capturing linkages dividends • Complementing FDI attraction with policies that support skills and cluster development to capture the desired spillover effects • Active promotion of supporting industries to key manufacturing sectors • Massive training of local workforce and suppliers

Strategy	Policies and programs	Key lessons for Russia
	(fostering competitiveness, decentralization, industrial development, etc.) incentive regime.	
Czech Republic		
<ul style="list-style-type: none"> Prior to EU accession, needed to increase industrial competitiveness to compete in single market Introducing demand-led approach to create awareness for needed change in competitiveness and business mindset of local firms after period of central planning Implemented a hands-on program working directly with a cohort of firms for 2 years as a signal of the opportunity to rest of the economy and to have a prove of concept for successor programs 	<p><u>National Supplier Development Program (2000-2002)</u>, implemented by CzechInvest in cooperation with the European Union and the World Bank Group. The goal was to strengthen the linkages between MNCs and Czech firms around components (semiconductors, printed circuit boards, cable harnesses), engineering supplies, and other packaging materials, automation, R&D and software. The program was based on the demands of MNCs. MNCs guided the program through participation in the High-Level Advisory Group. Access to finance and active matchmaking were offered throughout the intensive-support phase and competitive elements were integrated in the program design to ensure the most capable and committed local suppliers received most support.</p> <p>Following the success of the pilot, the program was replicated in 3 other sectors.</p>	<ul style="list-style-type: none"> Participation of MNCs in the public support activities Strong emphasis on the demands from MNCs
Ireland		
<ul style="list-style-type: none"> Adaptive linkages policy responding changes in (i) MNC needs, (ii) local firm capacity and capability, and (iii) in the structures of government agencies involved in industrial and trade promotion based on M&E Very sensitive to avoid any impression of 'compulsory' linkage-building and public influence on scope and results of programs 	<p><u>National Linkage Program (1984)</u> upgrading Irish suppliers to serve the MNC market in Ireland around 3 Cs:</p> <ul style="list-style-type: none"> Build technical competence of local firm (capabilities) Assist capable suppliers achieve scale (capacity) Build awareness of the domestic supply potential among MNCs (communication) 	<ul style="list-style-type: none"> Government efforts to grow new high technology sectors Leadership of a private sector entrepreneur in the linkages program High media attention to the supply linkages program Emphasis on the international linkages and the globalization of the local supply industry

Strategy	Policies and programs	Key lessons for Russia
<ul style="list-style-type: none"> • Invested in understanding and anticipating MNC demands and knowing local firm capabilities • Improved institutional coordination and program scope after a range of scattered activities did not deliver results expected 	<p>The fourth phase of the NLP, emphasized international linkages and the globalization of the local supply industry. The support mechanisms integrated a mix of export, outward investment, and linkage promotion.</p> <p>Global Sourcing Initiatives (2012) to build linkages between local and MNCs overseas to integrate into their global supply chains.</p>	

The cases reveal four broad pillars that a typical linkage program involves: (1) an enabling environment, (2) targeted FDI attraction, (3) linkage promotion services, and (4) local firm capacity (Figure 1). Economies that managed to link home grown companies to FDI employed a mix of interventions along these four pillars. As a result, countries increased the value added in their export sectors and often, over time, utilized such programs to upgrade and diversify their economies.

Figure 1. Strategic pillars of FDI linkages promotion (Source: World Bank Group)



The case studies reflect the broad range of experiences among host countries that have sought to increase linkages. It is commonly recognized that attracting FDI and creating an enabling policy environment are necessary but, most often, insufficient conditions for meaningful spillovers to occur in most developing countries.⁸ As countries try to upgrade the productive capabilities of SMEs and enhance the benefits from FDI, they have introduced policies and dedicated programs that foster FDI linkages. The impetus frequently started from opening up markets, which increased competition and gave space for more active FDI promotion. Although they clearly differ in approach and country-context all the examples show that a long-term view with policy commitment is required, yet flexibility to adapt to new opportunities and challenges along the way. Moreover, it is important to know what market failures apply so that subsequent measures or policies achieve the aspired impact.

The cases confirm the importance of starting with the demand-side and not to enforce linkages. This requires a thorough and realistic understanding of what MNCs need to increase their competitiveness and what requirements apply. Thus, it is advisable to integrate MNCs in the governance structure of the program or have the international private sector closely advise (e.g. Czech Republic) or even run certain linkages initiatives (e.g. Malaysia). Since trust and information gaps are often an issue, it is crucial to involve MNCs as partners in such initiatives. Countries that used legal requirements to mandate investors to use local goods or services in host country operations often undermined long-term competitiveness. These requirements tend to increase the cost or lower the quality of production. They can also deter the same investors the government is trying to convince to bring capital, technology and jobs to the host country. A recent study on the impact of local content requirements (LCRs) in the heavy vehicles sector in BRICS, shows the distortive affects and cost that LCRs have for both, consumers and producers, in Russia.⁹

Strengthening the supply capacity of local companies is, in most cases, the key challenge for developing FDI linkages. Therefore, competitiveness and productivity improvements should be at the core of the relevant support programs. Since market failures play out at the firm-level, productivity is the ultimate goal of most supplier development programs.¹⁰ This focus should not only be considered for the design

⁸ Moran (2010)

⁹ Deringer et al (2018)

¹⁰ Cusolito and Maloney (2018)

of a linkage program, but also for the selection of participating firms. In this context, it is necessary to appreciate that supplier development, in contrast to more broad-based SME development, should focus on those firms that are more ready to pass the supplier criteria of MNCs or to become longer-term partners of MNCs (e.g. for design and R&D activities). While the cases show different levels of targeting and detail in support, most cases in this chapter either started from tailored and practical support or adapted their programs to this end. In particular, the cases from Ireland, Malaysia, and Thailand confirm the need to consider the skills agenda, ranging from technical skills in production processes to management competences.

Targeted incentives for skills upgrading and supplier engagement were often applied. Tax incentives impose a significant fiscal cost on the countries granting them and thus targeted incentive schemes are more common. Moreover, evidence supporting targeted approaches over broad incentives is emerging. However, incentives focused on training & skills, R&D, high-tech and higher value-add production and local sourcing have been successfully applied in Malaysia and Singapore, to strengthen technology and skills acquisition of local firms.¹¹

All cases highlight the need for an enabling environment for FDI linkages promotion, which includes a committed and coordinated institutional landscape that puts the private sector needs first. From an institutional perspective the examples show different set-ups, but they all share a relatively well-funded mandate, based on a widely-communicated policy agenda, and high-level political buy in. While there are several institutions that have a role to play in promoting linkages, it usually always involved the national focal points for foreign investors, for domestic investors, and an entity covering the policy agenda around investment such as a Ministry of Industry, Ministry of Economy, or an industrial or investment board. This is key to be able to coordinate policies and interventions which touches upon several important thematic areas ranging from cluster policies, industrial eco-system development and quality infrastructure to access to financial services and education policies with a focus on technical and managerial skills.

Last but not least, the overall investment climate matters. The regulatory and institutional environment in which firms operate, impacts their ability to initiate productivity improvements – either through improved allocation of inputs, technology transfer and the ability to generate spillovers. Most policy initiatives in this area place their emphasis on horizontal policies such as taxation, infrastructure, red tape reduction, intellectual property protection, contract enforcement, competition policy, finance, and measures that impact the overall competitiveness of an economy.

2. Context for the attraction and localization of manufacturing FDI in Russia

Key findings

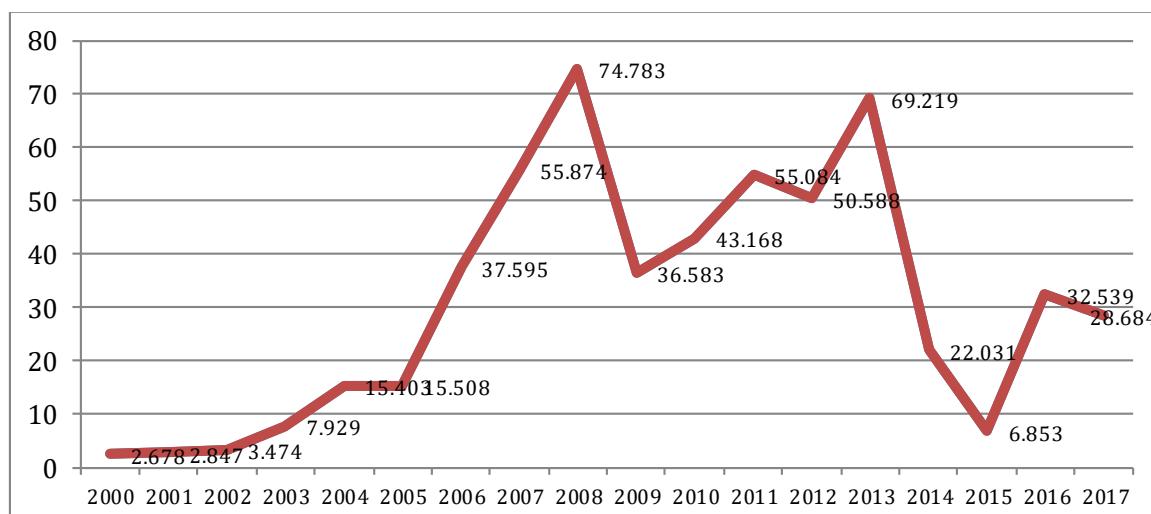
- FDI inflows in Russia from 2008-2017 were uneven with a tendency to concentrate in a limited number of leading regions and subsectors
- Manufacturing is the business area with the highest number of FDI projects
- Russia has created legislation, support measures and institutions to facilitate manufacturing FDI attraction and localization but this process is still hampered by political risks and deficiencies in the entrepreneurial and investment climate

¹¹ OECD (2018)

2.1. Inflow of manufacturing FDI in Russia

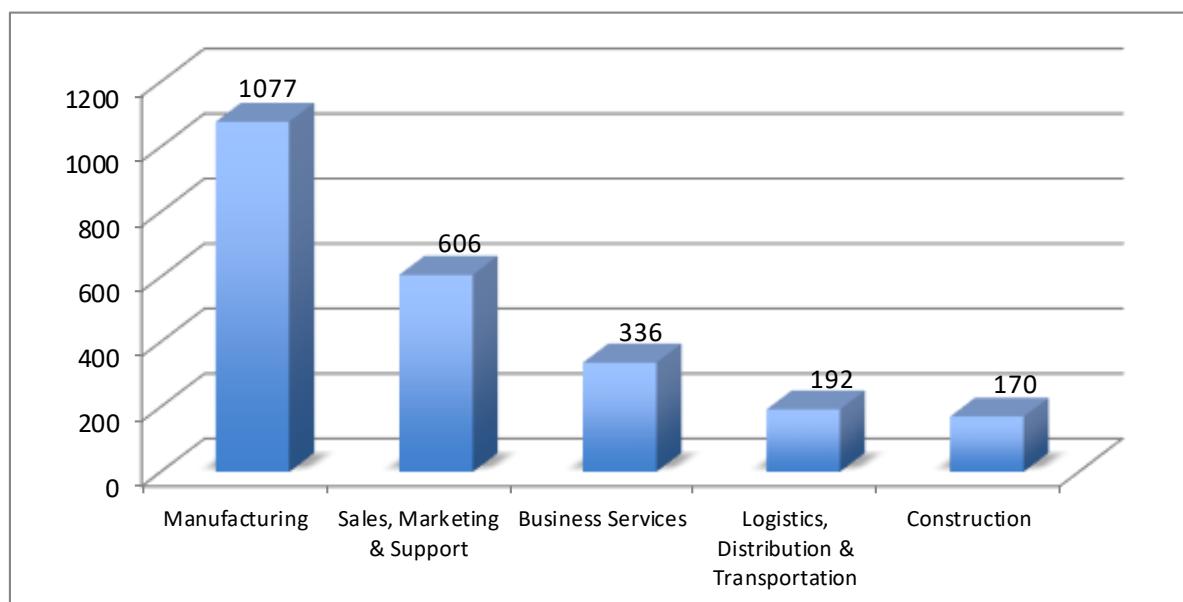
The amount of FDI in Russia was very uneven starting from the year 2000 due to macroeconomic conditions and geopolitical tensions. According to World Bank data (Figure 2), FDI grew in 2000–2008 and then dropped following the financial crisis. FDI almost reached its pre-crisis level in 2013 but dropped again, largely as a result of the political situation. The total net inflow of FDI in the period of 2008 – 2017 reached nearly 420 bln. USD.¹²

Figure 2. FDI in Russia, net inflows, Balance of payments, current USD (bln.)



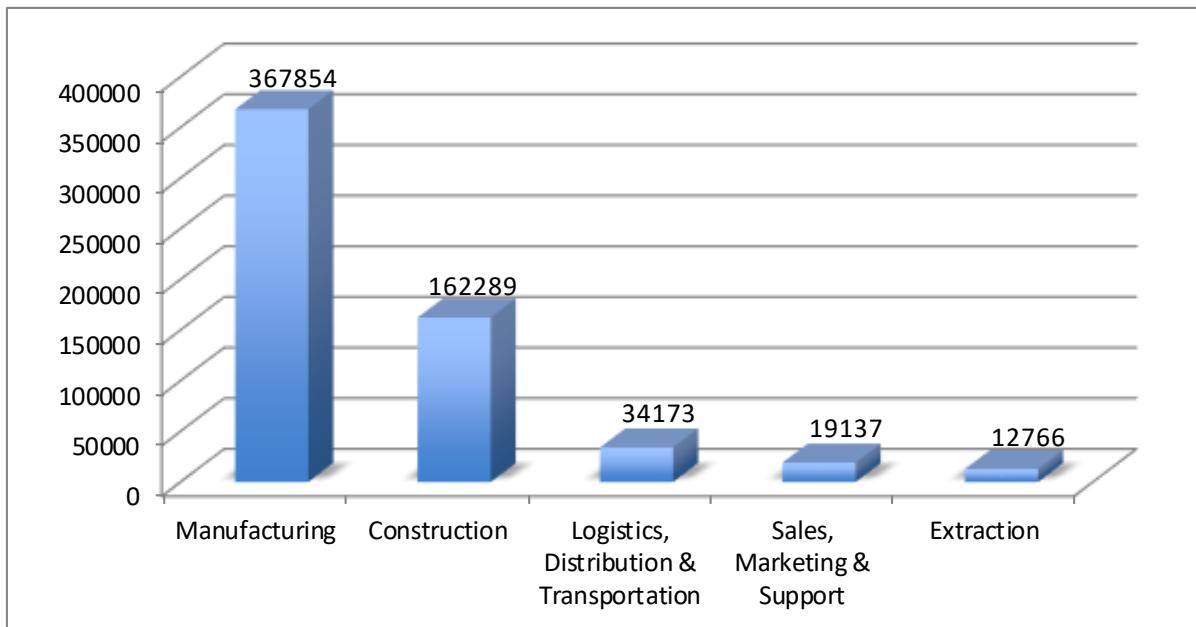
Manufacturing attracts the biggest part of FDI in Russia. According to the data on announced FDI in Russia provided by FDI Markets (Cross border Investment Monitor from the Financial Times, <https://www.fdimarkets.com>), in the period from September 2008 to September 2018 the total number of announced FDI projects in Russia was 2,705, with 625,633 jobs created. The leading business activities are shown below:

Figure 3. Leading business activities in September 2008 – September 2018 by the number of announced FDI projects



¹² <https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?locations=RU>

Figure 4. Leading business activities by the number of jobs (announced FDI)



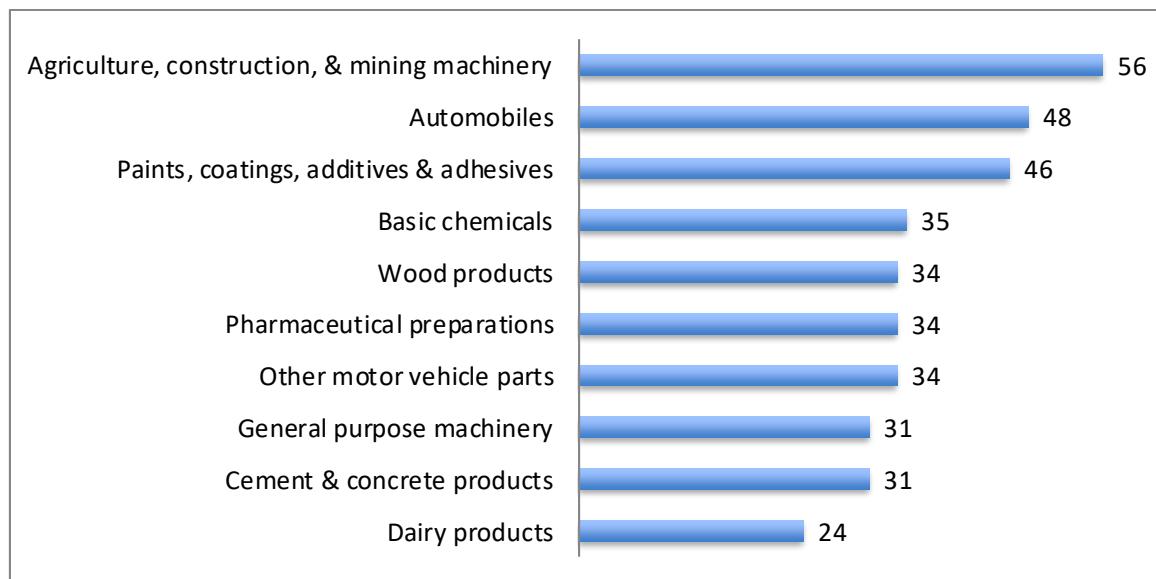
FDI is spread unevenly among the regions and sectors/subsectors. For the period of September 2008 – September 2018, the top 10 regions (Table 1) accumulated about 26% of all announced FDI (out of the total 85 regions), and the 10 leading subsectors (among the total number of 121 subsectors) attracted 22% of the announced FDI (Figure 5).¹³

Table 2. Top 10 Russian regions by the number of announced FDI projects

No	Region	Number of projects	Announced volume of FDI under the projects, mln. USD
1.	Saint-Petersburg	71	6320.48
2.	Moscow region	66	7444.58
3.	Kaluga region	62	4709.33
4.	Republic of Tatarstan	62	5760.42
5.	Nizhny Novgorod region	41	2753
6.	Leningrad region	40	2091.34
7.	Lipetsk region	39	2635.33
8.	Moscow	39	6381.87
9.	Ulyanovsk region	33	4938.74
10.	Primorsky Krai	31	4948.68

¹³ Cross border Investment Monitor from the Financial Times, <https://www.fdimarkets.com>

Figure 5. Top 10 subsectors by the number of announced FDI projects in the period of September 2008 – September 2018¹⁴



2.2. Manufacturing FDI promotion policy

Russia, like many other countries, has adopted legislative acts to facilitate manufacturing FDI attraction. The key legislative acts are:

- Federal Law № 160-FZ, “On foreign investments in the Russian Federation” dated July 9, 1999, defines the main guarantees of the rights of foreign investors on their investments and relevant revenues/profits, and the conditions of foreign investors’ activity in Russia. The Law is aimed at the attraction of foreign products and financial resources in the Russian economy, advanced equipment/technologies and managerial experience, as well as ensuring the compliance of the legal regime of foreign investments to the norms of international law and international practice of investment cooperation.
- Federal Law № 39-FZ, “On investment activity in the Russian Federation undertaken in the form of capital investment” dated February 25, 1999, defines the legal and economic basis of capital investments in Russia, including that related to such activities of foreign investors.

The Russian Government has also adopted a number of support mechanisms and created specialized institutions to facilitate the attraction and localization of new manufacturing FDI. Primary support mechanisms include:

- Special investment contracts. This is an investment agreement between the state authorities and an investor, according to which the investor shall establish, upgrade or start the manufacturing of industrial production on the territory of Russia, and the Russian Federation (or a region) shall grant the investor certain benefits according to the federal or regional legislation. Such contracts may be concluded with the participation of the Russian Federation or a region and these contracts may include specific provisions related to local content. The total number of contracts signed thus

¹⁴ Cross border Investment Monitor from the Financial Times, <https://www.fdimarkets.com>

far is 33¹⁵ (examples are Mercedes-Benz, German-Japanese concern “DMG Mori”, and Hyundai Motor Manufacturing Rus).

- Loans from the Industry Development Fund. The loans are provided for the implementation of projects aimed at the introduction of new technologies, the creation of new products, or the establishment of new production lines. The volume of the loans ranges from 5 to 750 mln. RUR, for a period of up to 7 years, with an interest rate of 1, 3, or 5%. For example, the Chinese company Haier received the Fund’s loan for the development of refrigerator production at the company’s plant in the Republic of Tatarstan.
- Industrial infrastructure. Key elements of such infrastructure are special economic zones, industrial and technology parks, territories of accelerated development, and the Skolkovo Innovation Center. At present, there are 25 SEZs, 176 industrial parks and 107 technoparks in Russia. They offer hard infrastructure for production facilities, tax and customs benefits, simplified administrative regimes, and easier access to state support measures. Many foreign companies investing in Russia, opt to locate their subsidiaries in industrial infrastructure sites. Some examples include:
 - German pharmaceutical company Merck in 2017 opened a life science laboratory in Moscow on the territory of Technopolis “Moskva”;¹⁶
 - German company WIKA, the leading global producer of measuring and metrology equipment, opened a production site together with an office and warehouse on the territory of the industrial park «Indigo» in Moscow;¹⁷
 - Schneider Electric opened a Center in Skolkovo for the development of software for systems of dispatching, control and monitoring in the power generation and in the oil/gas industry;¹⁸
 - German pharmaceutical company Bionorica CE started the construction of a new plant for the production of herbal medicines on the territory of the industrial park «Maslovsky» in Voronezh region;¹⁹
 - The company Viessmann opened its first plant in Russia in 2017 on the territory of a special economic zone “Lipetsk”.²⁰

Apart from above-mentioned support measures for FDI attraction and localization, many additional activities are conducted by various institutions at the federal and regional level with a view to facilitate the implementation of FDI-related projects and protect foreign investors’ rights in Russia. The key institutions are:

- Russian Private Equity Fund.²¹ The Fund invests in leading Russian companies in cooperation with foreign investors thus catalyzing new inward investment. The Fund has created a web

¹⁵ <http://frprf.ru/download/prezentatsiya-mekhanizma-spetsialnykh-investitsionnykh-kontraktov-po-postanovleniyu-pravitelstva-708-ot-16-07-2015.pdf>

¹⁶ <https://rg.ru/2018/05/23/lokalizaciia-proizvodstva-v-rossii-stala-trendom-dlia-nemcev.html>

¹⁷ <https://rg.ru/2018/05/23/lokalizaciia-proizvodstva-v-rossii-stala-trendom-dlia-nemcev.html>

¹⁸ <http://strategyjournal.ru/articles/lokalizatsiya-proizvodstva/>

¹⁹ <https://rg.ru/2018/05/23/lokalizaciia-proizvodstva-v-rossii-stala-trendom-dlia-nemcev.html>

²⁰ <https://rg.ru/2018/05/23/lokalizaciia-proizvodstva-v-rossii-stala-trendom-dlia-nemcev.html>

²¹ <https://rdif.ru>

portal “Invest in Russia” (<http://investinrussia.com>) with information for investors about the regions, promising sectors and public support measures.

- The Agency of Strategic Initiatives.²² The Agency facilitates the creation of favorable conditions for business, investment promotion in the Russian regions and regional investment team's capacity building. The Agency's projects are implemented under the roadmaps approved by the Government of the Russian Federation. Target indicators of the roadmaps take into account the Doing Business ranking, OECD indicators of competitive product market environment, and indicators of entrepreneurial activity and new business density. The Agency has also created a web portal with information on the regional investment opportunities and support measures for investors (<https://investinregions.ru>).
- Regional development corporations and/or investment promotion agencies. Their main functions include the presentation of regional investment potential to foreign investors, creation and maintenance of the regional investment web portals, support to foreign investors in the implementation of projects, and assistance in the improvement of investment climate at the regional level. In Russia, the National Association of Investment and Development Agencies has been established to support investment promotion, create a professional community and boost cooperation and partnerships.

More detailed descriptions of the support mechanisms and institutions are presented in Annex 1.

Box 1. Russia's import substitution policy

This policy was launched to support domestic manufacturers that aim to produce goods substituting imports, and to further stimulate foreign companies to localize the production in Russia. The policy is based on the Federal Law «On industrial policy in the Russian Federation»²³ and the Plan for assisting import substitution in the industry.²⁴ In 2014, the Government of the Russian Federation approved a state program “Development of industry and enhancement of its competitiveness”.²⁵

In 2015, the Ministry of Trade and Industry created a list of more than 800 types of products, services, and software for import substitution.²⁶ The Ministry also approved plans on import substitution in 19 sectors that include more than 2,000 projects.²⁷ The plans include target indicators to be met by 2020 – for example, it is expected to decrease the share of import in the aviation industry from 92% to 71%, in the tools and instruments industry from 88.4% to 58%, in radio electronics from 82% to 44%, and in oil and gas machinery from 60% to 43%.²⁸ The import substitution policy is also implemented by some Russian regions on the basis of the regional programs or plans.²⁹

²² <https://asi.ru/investclimate/>

²³ Dated December 31, 2014 № 488-FZ.

²⁴ Approved by the Decree of the Government of the Russian Federation dated September 30, 2014 № 1936 -r.

²⁵ Decree of the Government of the Russian Federation dated April 15, 2014 № 328.

²⁶ <http://importozamechenie.ru/rf-nuzhno-importozamestit-800-vidov-produkci-i-texnologij/>

²⁷ http://minpromtorg.gov.ru/press-centre/news/#!minpromtorg_utverdil_plany_po_importozamesheniyu_v_19_otraslyah_promyshlennosti

²⁸ <http://importozamechenie.ru/rf-nuzhno-importozamestit-800-vidov-produkci-i-texnologij/>

²⁹ http://iubpe.sfu-kras.ru/assets/content/files/1453965519_2088_2908_1_PB.pdf

One feature of the import substitution policy is the restrictions for imported products to participate in some state and municipal procurement.³⁰ A number of relevant legislative acts were adopted by the Russian Government in recent years (for example, establishing restrictions and/or conditions for the participation of imported goods in state and municipal procurement in the area of the state's defense and security, radio electronic production, machinery, etc.).

Large state corporations also contribute to the import substitution policy - these corporations prepared lists of imported equipment, tools, components and materials that should be substituted with domestic equivalents.³¹ Oil and gas companies created special divisions responsible for the work in this area and approved internal regulations and plans for the localization of the production of necessary equipment.³²

While these policies may have provided incentives for some investors to localize production, they carry a range of potential downsides, including reduced competition and higher public expenditure for procurement. Furthermore, these policies have raised concerns among WTO members as being discriminatory against imports in public procurement. And, as Russia is currently an observer to the WTO GPA, these issues will continue to be debated.

Despite these support measures, FDI attraction and localization in Russia is hampered by political risks, supplier capacity issues, and some deficiencies in the investment climate. Foreign companies implementing localization projects mention the following problems:

- lack of clear requirements on manufacturing localization in many sectors of industry;³³
- administrative barriers and cumbersome bureaucratic procedures,³⁴
- strict regulation of state procurement;³⁵
- poor coordination of regional and sectoral import substitution programs;³⁶
- possibility of different interpretations of the legislative norms;³⁷

³⁰ In order to be able to participate in state and municipal tenders, foreign investors should obtain certificates for their products that confirm their production in Russia. Industrial products are classified as produced in Russia if one of the following requirements is met:

- The production meets the criteria set in the Annex to the Decree of the Government of the Russian Federation dated July 17, 2015 № 719;
- The production meets the criteria set by the Agreement "On the rules of the identification of the goods' country of origin in the Commonwealth of Independent States" dated November 20, 2009;
- Industrial production is manufactured under a special investment contract.

³¹ <https://moneymakerfactory.ru/biznes-idei/biznes-na-zameschenii-importa/>

³² [http://minpromtorg.gov.ru/press-](http://minpromtorg.gov.ru/press-centre/news/#!minpromtorg_utverdil_plany_po_importozamesheniyu_v_19_otraslyah_promyshlennosti)

³³ [http://minpromtorg.gov.ru/press-](http://minpromtorg.gov.ru/press-centre/news/#!aleksey_besprozvannyh_prinyal_uchastie_v_kruglom_stole_tpp_po_lokalizacii_inostrannyyh_proizvodstv)

³⁴ [http://minpromtorg.gov.ru/press-](http://minpromtorg.gov.ru/press-centre/news/#!aleksey_besprozvannyh_prinyal_uchastie_v_kruglom_stole_tpp_po_lokalizacii_inostrannyyh_proizvodstv)

³⁵ <https://nangs.org/news/economics/lokalisatsiya-kak-instrument-formirovaniya-klasternoj-ekonomiki>

³⁶ [http://minpromtorg.gov.ru/press-](http://minpromtorg.gov.ru/press-centre/news/#!aleksey_besprozvannyh_prinyal_uchastie_v_kruglom_stole_tpp_po_lokalizacii_inostrannyyh_proizvodstv)

³⁷ <https://nangs.org/news/economics/lokalisatsiya-kak-instrument-formirovaniya-klasternoj-ekonomiki>

- unpredictable changes in the external environment at the global and local levels, such as new trade constraints introduced by various countries;³⁸
- the inability of Russian companies to supply some material inputs with necessary quality;³⁹
- unexpected drops of demand on the markets (for example, due to the reduction of demand for cars, a lot of projects on the production of spare parts were frozen, and some manufacturing sites were closed).⁴⁰

³⁸ <http://strategyjournal.ru/articles/lokalizatsiya-proizvodstva/>

³⁹ To solve this problem, foreign companies may invite their international suppliers to organize the production of necessary material inputs in Russia, or they will have to import them. In these cases, the development of Russian technologies and suppliers is not stimulated.

⁴⁰ <https://nangs.org/news/economics/lokalizatsiya-kak-instrument-formirovaniya-klasternoj-ekonomiki>

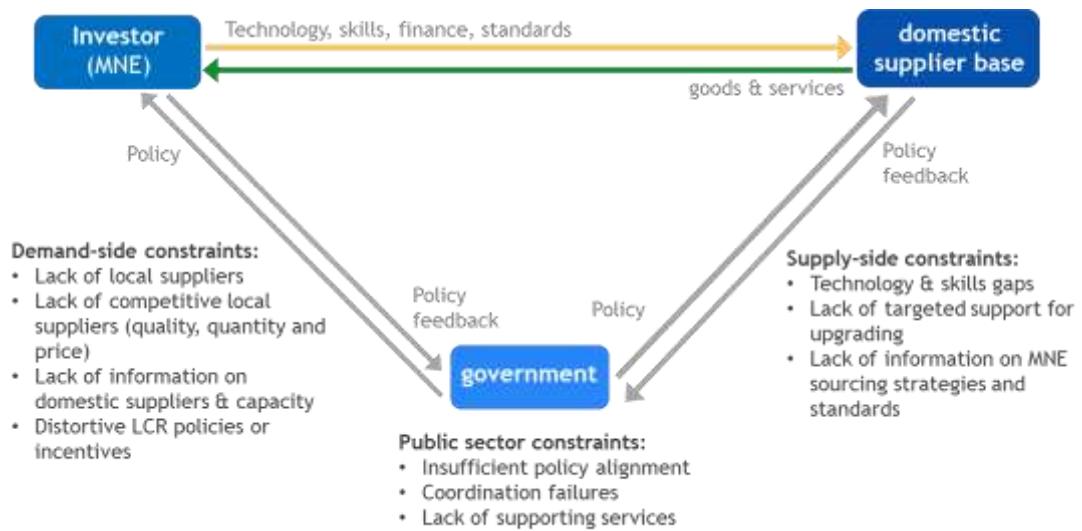
3. Development of FDI linkages with SMEs in Russia

Key findings

- The MSP Corporation is the main institution responsible for the development of linkages between MNCs and Russian SMEs
- The development of FDI linkages could be enhanced by regional business support institutions but only a half of them operate in this area. 85% of these institutions need external assistance in the collection of information about the demands of MNCs, improving the capacity of local suppliers, and matchmaking between regional and foreign companies
- Support for the development of FDI linkages is also provided by the Foreign Investment Advisory Council (FIAC), bilateral trade chambers and industrial associations
- Large MNCs usually search for Russian suppliers on their own, and many provide advisory support to their key Russian partners to upgrade their management systems and technology processes

Cooperation between foreign companies in Russia and Russian suppliers is beneficial for both sides, but is hampered by serious market failures. Foreign investors can reduce production costs, while Russian companies gain access to new technologies and can improve their production and management practices. Such cooperation, however, depends on the competitiveness of the local supplier, the motivation of investors, and the wider business environment. Presently, foreign companies localized in Russia still import a lot of materials and components which may point to weak FDI linkages.⁴¹ Russian suppliers often have problems in cooperating with MNCs due to quality issues with production, failure to certify compliance with product or management system standards, and lack of financial resources to develop the production processes to reach the level of cost, quality, and delivery required by foreign companies. These challenges are common to linkages formation around the world and global experience has shown that addressing them sustainably requires action to resolve the following market failures:

Figure 6. Typical market failures and constraints impacting FDI linkages⁴²



⁴¹ It should be noted though, that due to value chains' globalization, investors (international and domestic) across the world, especially in manufacturing sectors, import a substantial amount. Thus, limiting the base of imports may also hurt domestic firms.

⁴² In many cases, the MNC may not provide technology or skills if an MNC only needs a simple product.

While there are several initiatives to promote linkages, there are no comprehensive programs at the national or regional level in the Russian Federation addressing the above market failures. At present, the main responsible body for the development of FDI linkages in Russia is the MSP Corporation (Joint-stock company "Federal corporation on the development of small and medium entrepreneurship")⁴³. The KPIs in this area are set by the national project "Small and medium entrepreneurship and the support for the individual entrepreneurial initiative" (approved by the Presidium of the Council under the President on strategic development and national projects on December 24, 2018). This federal project includes, in addition to other support instruments, a set of measures aimed at the development of SMEs as suppliers of large companies (initially focused on companies with state participation) to facilitate the promotion of linkages. The main activities under this project include:

- Development of digital tools to facilitate the participation of SMEs in the procurement procedures of the largest buyers;
- Extending the planning horizon to three years for procurement from SMEs organized under the Federal Law dated July 18, 2011 №223-ФЗ "On the procurement of goods and services by certain types of legal entities";
- Increasing the SME share in procurement to 18% from the largest buyers to be achieved by 2020
- Ensuring the possibility of using the factoring mechanism by SME suppliers under the procurement procedures organized by at least the 100 largest buyers;
- Updating programs on the improvement of procurement activities by state monopolies and companies with state participation with the goal of targeting KPIs and relevant calculation methodologies connected with procurement from SMEs;
- Introduction of special mechanisms and the design of recommendations for the development of suppliers (SMEs) for their potential participation in the procurement of goods and services by the largest companies, including with the use of the SME support infrastructure;
- Ensuring the annual implementation of actions by at least 5 companies with foreign production localized (or planning to localize) in Russia, aimed at including Russian SMEs in their supply chains and with the goal to increase the manufacturing localization level;
- Establishment of administrative responsibility for the largest buyers for violation of the requirements set by the Decree of the Russian Government dated December 11, 2014 № 1352 «On the specifics of SMEs' participation in the procurement of goods and services by certain types of legal entities», regarding the terms of payment under contracts.

Many of the targets of the program focus on increasing the volume of state companies' and foreign investors' procurement from SMEs. The MSP Corporation observes that approximately 1500 companies with state ownership procure from SMEs, with the aim to facilitate the purchase of goods and services from SMEs and to increase the volume of high-technology products bought by large state companies from

⁴³ MSP Corporation (<https://corpmsp.ru>) is a state development institution created in 2015. The main activity of the Corporation is related to supporting SMEs and the SME development infrastructure (attraction of financial resources; information, marketing, financial and legal support for investment projects implemented by SMEs; increasing purchases of goods/services by the state enterprises from SMEs; interaction with the state and municipal bodies and other organizations with the aim of supporting SMEs; preparing proposals on the improvement of support measures and legislation related to the activity of SMEs).

SMEs.⁴⁴ As well as increasing the sales of SMEs to state enterprises, development of cooperation between foreign companies localized in Russia and their potential Russian suppliers is also an important task for the Corporation. Activities under this task are aimed at increasing the level of foreign companies' manufacturing localization, facilitating Russian companies' access to markets and enhancement of their global competitiveness.

Box 2. Cooperation of the MSP Corporation with MNCs

The Corporation implements joint activities with foreign investors to improve Russian SMEs' access to their supply chains, for example:

- In 2017, MSP Corporation signed an agreement with the Russian-German External Trade Chamber and Schaeffler Manufacturing Rus (German producer of bearings). The goal is to facilitate the promotion of Russian companies in foreign supply chains. Under the agreement it was planned to prepare a list of SMEs – potential suppliers for Schaeffler, organize an event for these companies to conduct preliminary negotiations, and, if necessary, create a working group on upgrading SMEs for compliance with the company requirements.⁴⁵
- In 2018, MSP Corporation signed an action plan with BASF and the German Eastern Business Association. According to the document, the cooperation is aimed at the search and selection of potential suppliers for BASF, organization of B2B meetings with Russian companies, and implementation of actions for the development of Russian SMEs to meet the BASF requirements. Support for the development of SMEs will be given with the use of support measures provided by MSP Corporation.⁴⁶
- MSP Corporation and the Japan External Trade Organization are creating a joint mechanism to facilitate the promotion of Russian SMEs in the supply chains of Japanese companies localized (or planning localization) in Russia. In 2017, the parties signed a roadmap for cooperative actions in this area. Under the roadmap, JETRO provides a list of promising projects for cooperation between Russian SMEs and Japanese companies interested in Russian suppliers, as well as a list of products that will be purchased under the projects. In turn, MSP Corporation organizes a search for potential Russian suppliers. The roadmap also includes a series of B2B events between Russian and Japanese companies (for example, such an event was organized at the Innovation and Industrial Exhibition in Yekaterinburg in 2017, with the participation of Isuzu Rus and Hitachi Construction Machinery Eurasia).⁴⁷

In addition to the activities of the MSP Corporation, the development of FDI linkages is indirectly supported under various SME support measures implemented at the federal and regional levels. Such measures may be aimed at improving the competitiveness of Russian SMEs, facilitating their access to finance, R&D and technology transfers. Examples of key support measures include:

⁴⁴ <https://www.youtube.com/watch?v=g4GIfK0vOLQ>

⁴⁵ <https://4science.ru/news/Korporacii-MSP-vivodit-proizvoditelei-na-germanskii-rinok>

⁴⁶ https://lenta.ru/news/2018/05/26/msp_bASF/

⁴⁷ http://osspb.ru/osnews/korporaciya_msp_i_dzhetro_podpisali_dorozhnuu_kartu_po_realizaci_izmemorandum_o_vzaimoponimaniu

- industrial, innovation and business support infrastructure (business incubators, technoparks, export support centers, engineering centers, clusters, etc.);
- tax benefits;
- grants for innovation and R&D;
- training;
- organization of exhibitions and other events;
- subsidies for the reimbursement of interest rates;
- loans from industry development funds (such as the Moscow fund for the development of industry and entrepreneurship);
- support for export development;
- investments and participation from development institutions and venture funds.

This support, although not directly aimed at improving FDI linkages, contributes to upgrading Russian companies in terms of technologies, quality of products and services, innovation and skills. This increases their chances of becoming suppliers of foreign companies in the future. The SMEs that utilize public support systems to upgrade their production processes, technologies, qualification and management systems, become better prepared to meet the requirements of foreign investors.

At the regional level, assistance to the development of FDI linkages is provided by business support infrastructure (investment promotion agencies, regional development corporations, etc.). The World Bank, jointly with the National Association of Agencies for Development and Investment, organized an online survey of 20 regional investment agencies and development corporations representing 18 regions (13 regions are among the top 20 regions in Russia by the number of FDI projects). The survey was conducted in April 2019 (detailed results of the survey are presented in Annex 3, and the questionnaire in Annex 4). 95% of the surveyed institutions provide support for foreign investors in the preparation and implementation of FDI localization projects in their regions. Most typically, the assistance takes the following forms:

- Provision of information about a region, its hard infrastructure and land plots, projects, and support measures;
- Support in the selection of investment areas in the region;
- Help in the selection of a site (land plot) for the localization of manufacturing;
- Organization of visits and meetings in the region;
- Assistance with the administrative procedures and coordination of a foreign investor's interactions with the state authorities;
- Support in the search for potential partners and buyers.

Many of the regional business support institutions work as a “one stop shop” for foreign investors to reduce barriers hampering their activities in Russia. The surveyed organizations mostly work with medium-sized enterprises (50% of the respondents) and large companies (35% of the respondents), and provide most of their services for free. These services mostly focus on information transfer and technical support.

About a half of the organizations also provide support for the preparation of investment projects, the attraction of financial resources and promotion of goods/services in the Russian market. Only 45% of the surveyed institutions provide support for domestic firms to market their products or services to foreign companies (including foreign companies localized in Russia). These results reflect the focus of most business support organizations primarily on inward investment through medium and large companies and suggest a gap in the kind of services that could catalyze the development of linkages between larger investors and domestic SMEs.

While the surveyed organizations acknowledge the constraints in the development of FDI linkages, only half of them facilitate cooperation between foreign companies and local suppliers. According to the opinions of the surveyed institutions, the most critical constraints hampering FDI linkages are:

- Lack of communication with foreign companies and a general lack of information about their demands, quality standards, etc;
- Cooperation with foreign companies requires significant investment into the modernization of production for regional enterprises;
- Regional companies do not meet the requirements of foreign companies related to the quality of products/services.

Support for FDI linkages by these regional bodies usually includes the organization of B2B matchmaking events with the participation of foreign companies and potential suppliers, promotion of regional companies at various events and through publications/catalogs, and the organization of business missions.

Activities supporting FDI linkages development in most cases are ad hoc, reflecting the low prioritization of this topic relative to other KPIs on investment attraction. There is no standard approach nor high level KPI on activities related to linkages development by regional support organizations. Each region sets its own goals and implements its own actions in this area, as there are no federal standards or regulations. Business support organizations from different regions usually do not cooperate in this area and there are few platforms or forums for regions to share experiences.

85% of respondents () need external non-financial support for the development of linkages. The greatest demand from regional business support institutions is in the following areas:

- Collection/analysis of information about the demand of foreign companies localized in Russia and their requirements around quality, management systems, etc
- The creation of a database of potential regional suppliers for foreign companies that could help match local supply capacity with the information of buyer demand and standards;
- Analysis of global markets (value chains) to identify priority segments for linkages development for companies in their region;
- Support in the organization of meetings between regional enterprises and foreign companies;
- Support in the organization of B2B events for the development of cooperation with foreign companies.

Many of the surveyed institutions also need support in developing cooperation with international organizations and, more surprisingly, with the federal authorities and development institutions as well.

This finding may indicate problems in coordination of activities between the regional and federal levels, and with international organizations such as bilateral trade chambers.

The regional business support institutions proposed a number of recommendations for the development of FDI linkages. The key recommendations are related to overcoming the information asymmetry, implementing programs on the development of competitiveness of Russian suppliers, organization of B2B events, analysis of foreign markets and demands of MNCs, design of simple and clear criteria for the localization of manufacturing FDI, and providing subsidies to regions for the creation of operational-ready standard production facilities for foreign investors and their suppliers.

In addition, industrial associations⁴⁸ serve as an important tool for improving cooperation between foreign companies and Russian SMEs. The work of such associations is usually aimed at lobbying the interests of their member companies and the industries as a whole, communication with the national and regional state bodies, development of cooperation among the companies in the industries, support for market promotion of products/services, organization of events for the exchange of information and ideas, provision of services to member companies, and publication of informational materials. For example, the National Association of Producers of Auto components (<http://rusautoconnect.com>) has created a database of companies in the automotive industry and provides support in the search for partners/suppliers and subsequent negotiations. The association also organizes meetings of purchasing departments from automotive plants and representatives of potential suppliers. In 2016, the association conducted a program for the development of suppliers. The program included quarterly meetings with the participating suppliers to give them an opportunity to present their products to the automotive plants, seminars on the aspects of operational management and existing state support measures, and consulting support by the association's experts.⁴⁹ Such initiatives at the sector level could be excellent sources of good practices that could be scaled up or replicated in other sectors or at the regional level.

The development of FDI linkages with local SMEs in Russia is actively supported by bilateral trade chambers and international structures. For example, AmCham issues an Industrial Supplier Bulletin for its members with information on potential Russian industrial suppliers. The Bulletin features local companies that offer technologies to large international players across different industries. The weekly bulletins include information on potential Russian suppliers in different technological areas, such as energy and utilities, pharma, agriculture, etc.⁵⁰ The German Chamber supports the search for suppliers for its members in the Russian market and facilitates communication between its member companies and potential suppliers. The Chamber also helps in the organization of meetings and negotiations.⁵¹ At the French Chamber, the service for the development of cooperation with suppliers is provided on demand for the members. Typically, the Chamber organizes meetings of its member companies with potential Russian suppliers. An important international body for the development of FDI linkages is FIAC. For example, in September 2017 the FIAC's Work Group on Localization in cooperation with the Russian Ministry of Economic Development conducted a seminar for Russian SMEs on the issues of integration of Russian food products' suppliers into supply chains of global producers. During the seminar, it was agreed

⁴⁸ Examples of such associations: Association of tool-making plants (<http://www.stankoinstrument.ru>); Union of producers, suppliers and consumers of aluminum (<http://www.aluminas.ru>); National Association of Exporters of Agricultural Products (<http://naesp.ru>); National United Council of Glass Industry Enterprises (<http://www.steklosouz.ru>); Association of the Russian pharmaceutical manufacturers (<http://www.arfp.ru>); Association of Enterprises of Chlorine Industry (<http://ruschlor.ru>); Russian Union of Chemists (<http://www.ruschemunion.ru>).

⁴⁹ <http://rusautoconnect.com/en/55-the-project/2512-an-international-program-of-suppliers-development-2.html>

⁵⁰ https://www.amcham.ru/eng/supplier_bulletin

⁵¹ <https://russland.ahk.de/marke/zulieferersuche/>

that the Ministry and MNCs – FIAC members – would help Russian suppliers in improving the quality of their products to the global level.⁵²

Some foreign investors that have localized in Russia also implement activities aimed at the development of cooperation with Russian suppliers. Many of the large foreign companies (such as Air Liquide, John Deere Rus, Volvo Vostok, 3M) work with suppliers directly, without external help from chambers or other structures. These companies have databases of potential suppliers, participate in the events, search for potential suppliers⁵³, and may provide capacity building support for their key domestic partners. For example, Mondelez Rus has invested heavily into building a domestic supply chain and now 100% of all sugar and flour used by the company for the production processes in Russia is sourced domestically.⁵⁴ The joint company Ford-Sollers uses an online trade platforms for finding suppliers and distributing information on their standard and requirements.⁵⁵ Anheuser-Busch InBev Europe (the largest brewery in the world) implements its own international program “Smart Barley” in Russia. The company has about 1,000 Russian suppliers, and 90% of them are SMEs. The total volume of procurement in Russia is about 1 bln. USD. The company provides training to Russian suppliers in the area of improving the quality of agricultural production, provides space photographs of agricultural lands, and organizes meetings with suppliers. Another example is the company Saint-Gobain, which helps Russian SMEs by upgrading their technological processes and involving them in the processing of the company’s industrial waste.⁵⁶

In addition, cooperation between foreign investors and local suppliers/partners has grown through the development of industrial and innovative clusters in Russia. As mentioned above, the clusters and their management companies are supported by the state with the goal of facilitating economic development in the regions on the basis of cooperation among various players (large Russian and foreign companies, SMEs, universities, research institutes, business support infrastructure, etc.). This approach of creating a group of Russian suppliers “around” a large foreign company facilitates import substitution and the development of regional industrial clusters. Examples of such conglomerates in Russia:

- The manufacturing of locomotives by Siemens is one such example which involves about 100 Russian suppliers contributing to the supply chain for the “Lastochka” high speed train. Currently, more than 60% of the value addition in the production of the train is domestic, with plans to reach 80%.⁵⁷
- The plants of Volkswagen, Peugeot & Citroën Mitsubishi, and Volvo form the core of the automotive cluster in Kaluga.⁵⁸ In the broader cluster, there are about 30 companies producing automotive components.
- In the automotive cluster of the Samara region, there are 30 projects for the localization of automotive component production for the AvtoVAZ company.

⁵² <http://economy.gov.ru/minec/about/structure/depMB/2017130904>

⁵³ Apart from own information resources, foreign companies sometimes use public or commercial databases of potential suppliers, for example: <http://rospostavshik.ru/registrar/>; <https://zakupki.mos.ru/#/>; www.metaprom.ru; <http://www.postavshiki.ru>; <http://postavki-himii.ru>.

⁵⁴ <http://economy.gov.ru/minec/about/structure/depMB/2017130904>

⁵⁵ <https://www.youtube.com/watch?v=g4GIfK0vOLQ>

⁵⁶ <https://roscongress.org/news/krupnye-rossiyskie-i-inostrannye-kompanii-vs-malyj-i-srednij-biznes-vzaimnoe-doverie-zakazchika-i-postavschika/>

⁵⁷ <https://nangs.org/news/economics/lokalizatsiya-kak-instrument-formirovaniya-klasternoj-ekonomiki>

⁵⁸ <https://nangs.org/news/economics/lokalizatsiya-kak-instrument-formirovaniya-klasternoj-ekonomiki>

- The Kaluga region pharmaceutical cluster brings together large foreign players (Astra Zeneka, Novo Nordisk, Berlin-Chemie), Russian research institutes, SMEs and other large domestic companies.⁵⁹

It should be noted that the state support at the regional level plays an important role in the development of FDI linkages. The creation of clusters and supply chains uniting MNCs and local companies in Kaluga, Samara and other regions were facilitated thanks to the efforts of the regional governments and business support infrastructure. For example, the success of Kaluga region in the FDI attraction and development of cooperation with MNCs was stipulated by the support of the Governor, the creation of hard infrastructure for investors (economic zones, industrial parks, etc.) and active work on FDI promotion.

⁵⁹ <http://www.pharmclusterkaluga.ru/>

4. Survey of FDI linkages with local suppliers in Russia

Key findings. Among FDI survey respondents:

- Most of the surveyed companies are Russian subsidiaries of large MNCs that located production in Russia to gain access to the market
- The companies mainly source raw materials and services from Russian suppliers; the share of components with higher added value is very small
- 90% of companies stated further localization is a priority for cost control and speed of input supply , but increasing local sourcing is hampered by low technological capacity of the Russian suppliers and absence or low quality of material inputs
- Decisions on the selection of Russian suppliers are usually made at the regional or global headquarters of the MNCs
- Quality management, technological level of equipment, productivity and management skills are the most important areas where Russian suppliers need improvements

4.1. Survey background

The survey was focused on foreign companies from the automotive industry, chemical industry and engineering/machinery, located in Moscow, Saint-Petersburg and the Nizhny Novgorod region. The selection was made based on an analysis of the most well-represented (in FDI) industrial sectors in Russia for the 10-year period covering September 2008 – September 2018.⁶⁰ This analysis was complemented with data on members of the most active local bilateral chambers of commerce and industrial/sectoral associations. In addition to that, research was done on recent developments in the field of FDI and localization of MNCs through communication with industrial and sectoral support organizations as well as with state and other agencies. Sectors were also evaluated based on the depth of their value chain and value addition in final products. Based on this assessment, three industrial sectors were selected for the survey: automotive component production and assembly⁶¹, chemicals⁶², and general engineering/machinery production⁶³. The survey was conducted in Moscow, Saint-Petersburg and the Nizhny Novgorod region. Selection of the regions was made based on regional quantities of FDI transactions and industrial potential in the three selected sectors, as well as based on the overall activity and development of the regional support infrastructure.

⁶⁰ Source - fdimarkets.com

⁶¹ Companies in the automotive sector manufacture either general or special purpose transportation vehicles. The manufacturing begins with the production of individual parts and materials for a car and goes all the way to the final assembly of the car. The value chain for automotive production is extended and includes multiple tiers. The sector is generally divided into production and assembly businesses. In many cases, generated products are at the same time intermediaries (inputs for further production tiers) and final products that can sell on secondary markets (spare parts).

⁶² Companies in the chemical sector are focused on the production of chemical raw materials and industrial chemistry, main organic and inorganic chemicals, paints, varnish and lacquer for construction, petrochemistry, nuclear and power industries as well as the manufacturing of fertilizers and chemical agents for biotechnologies and diagnostics, etc. The value chain for chemical production is generally of medium depth. The initial tiers of the value chain require large-scale production. In many cases, all generated products in the chain are at the same time intermediary products and final products that can be sold to the market. Initial tiers are dominating the quasi-commodity economy meanwhile further tiers of the chain are more of an “intensive” type of value-added.

⁶³ Machinery companies manufacture products for a wide variety of applications mainly, but not only, in the B2B segment. Those products are either devices/machines or their core components. The value chain for machinery production is quite extended and includes tiers of parts and components manufacturing. The main production tier includes R&D, manufacturing of parts and components, as well as assembly. Production of some specialized parts and components are outsourced. In many cases, generated products are at both intermediaries (inputs for further production tiers) and final products that can be sold on the market.

Companies with local production facilities were invited to participate in the survey. In its entirety, 31 companies participated in the survey. The FDI classification attribute was defined as: *a contribution by a foreign partner of assets in the form of monetary funds, stocks, tangible and intangible assets, etc.* Effectively the key considerations for inclusion of a company in the survey were i) existence of foreign investment in a local production business and ii) a substantial level of influence or control by a foreign partner in a corporate decision-making process. The survey was carried out in person by the project team with company management responsible for either supply policies or general management and via the subsequent filling out of the survey questionnaire. In a limited number of cases, interviews were conducted by correspondence after carefully instructing companies' representatives on the proper way of filling out the questionnaire. The questionnaire for the survey is presented in Annex 4.

4.2. FDI trends in the selected regions/sectors

The yearly dynamics of announced FDI transactions in the selected regions in the period from September 2008 to September 2018 reflects the overall pattern for the country. For the selected regions and industries, the dynamics of the announced FDI is as follows (Figure 7 and Figure 8)⁶⁴:

Figure 7. Yearly numbers of announced FDI projects in selected regions

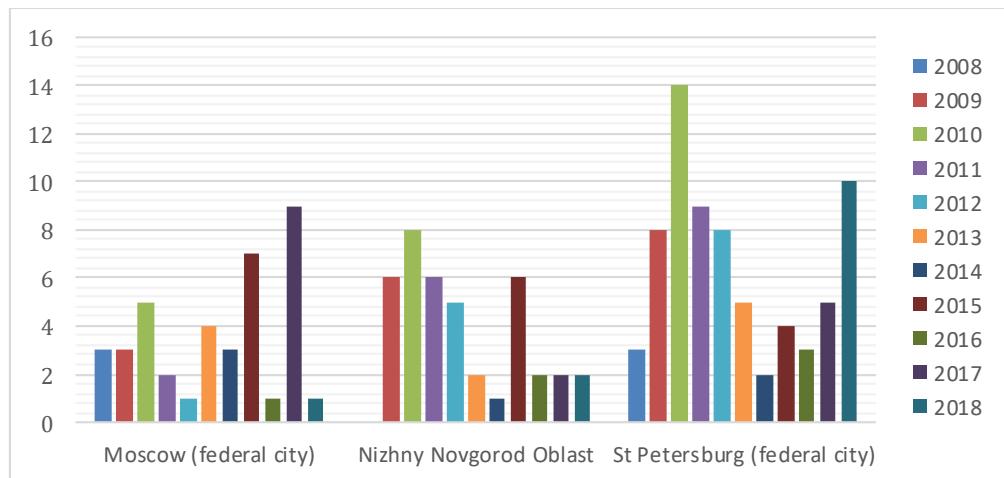
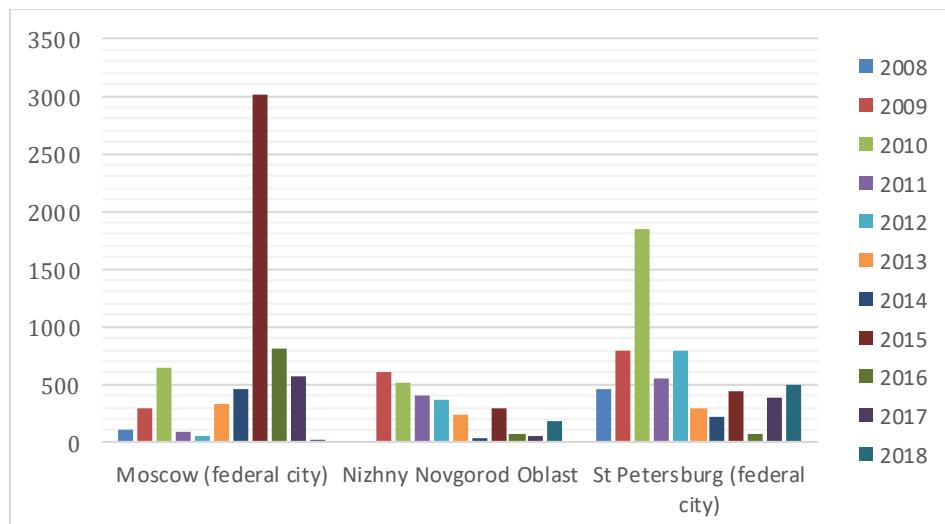


Figure 8. Invested capital in announced FDI transactions in selected regions, mln. USD



Moscow has been a leader in the monetary value of announced FDI transactions while Saint-Petersburg demonstrates a larger number of FDI transactions. Nizhny Novgorod shows a number of transactions

⁶⁴ Source of the statistic data on the announced FDI transactions - Cross border Investment Monitor from the Financial Times, <https://www.fdimarkets.com>

comparable with that of Moscow, however, the absolute monetary value is lower, which implies that smaller projects have been implemented.

Moscow has been comparably represented in all target industrial sectors. Industrial machinery and equipment are leading by the number of announced FDI projects while the automotive sector is leading with larger projects accumulating a larger amount of investments (Figure 9 and Figure 10).

Figure 9. Number of announced FDI projects in Moscow

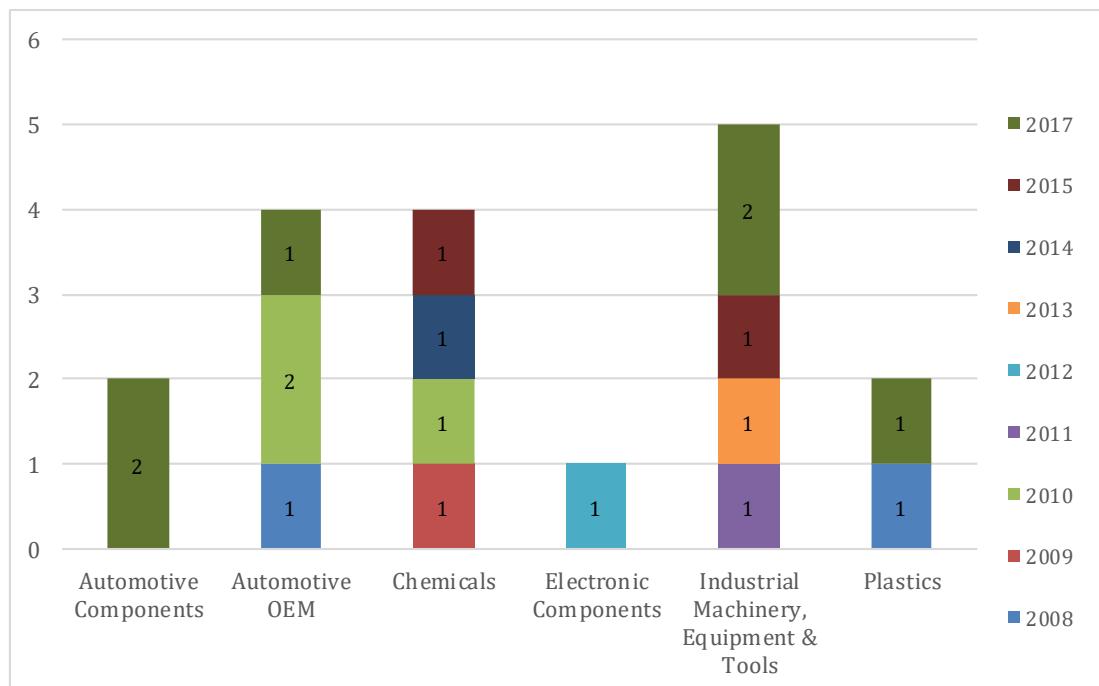
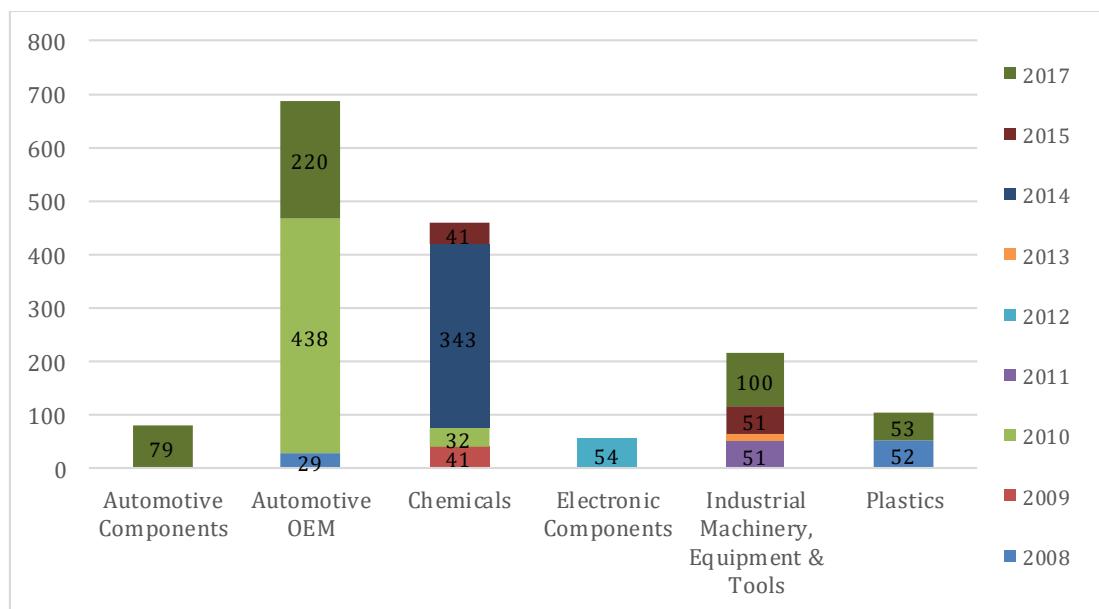


Figure 10. Invested capital in announced FDI transactions in Moscow, mln. USD



The FDI statistics in Saint-Petersburg has a clear lean towards the automotive industry with a large number of announced projects and significant amount of announced investment attributed to this one sector. The other target industrial sectors are presented with lesser amounts of announced FDI projects and even lesser average transaction sizes. Among the other sectors, the traditionally strong regional sectors of chemicals and industrial machinery are relatively better represented.

Figure 11. Number of announced FDI projects in Saint-Petersburg

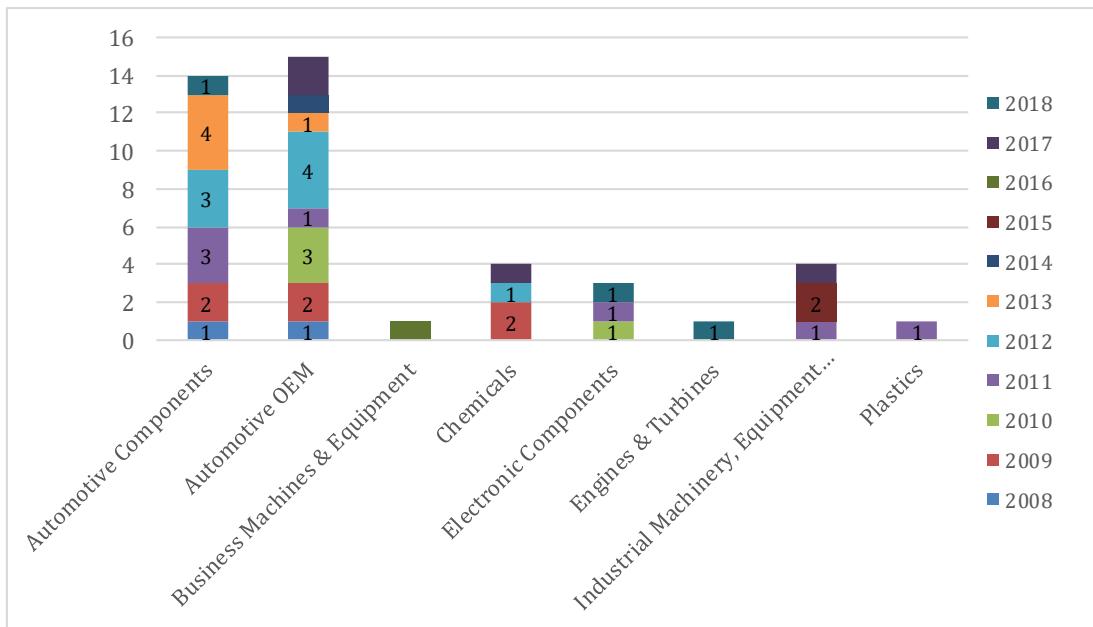
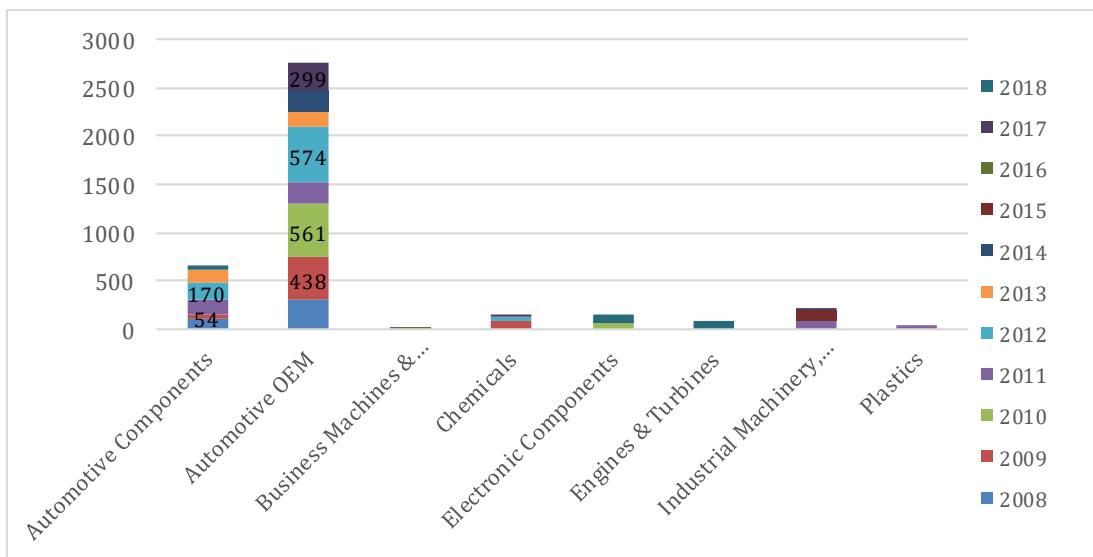


Figure 12. Invested capital in announced FDI transactions in Saint-Petersburg, mln. USD



The Nizhny Novgorod region demonstrates a more moderate number of investments, compared with the two federal cities. A larger number of announced FDI projects are concentrated in the automotive sector due to the installed industrial base of GAZ. However, a leading volume of investment is accumulated in the sector of industrial machinery and equipment with the automotive sector coming next. Another well-represented sector is chemicals due to the contribution of specialized industrial cities in the region (Dzerzhinsk, Bor).

Figure 13. Number of announced FDI projects in Nizhny Novgorod region

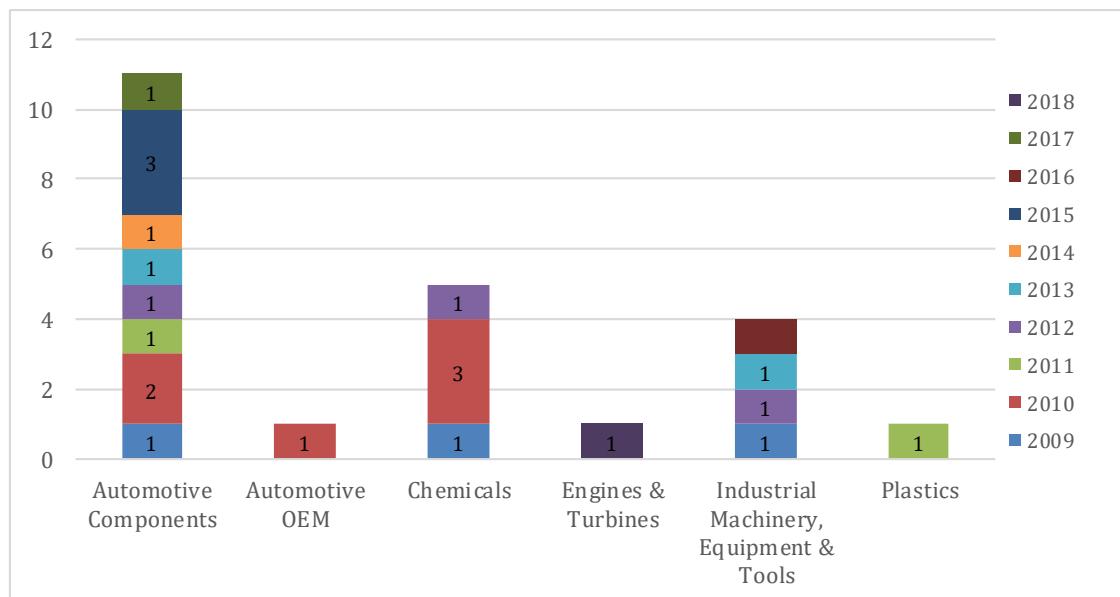
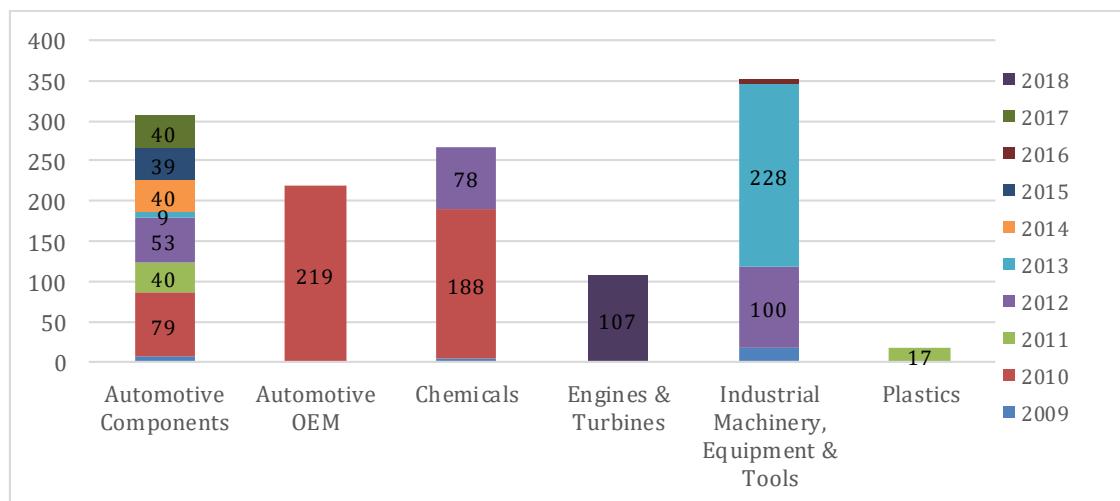


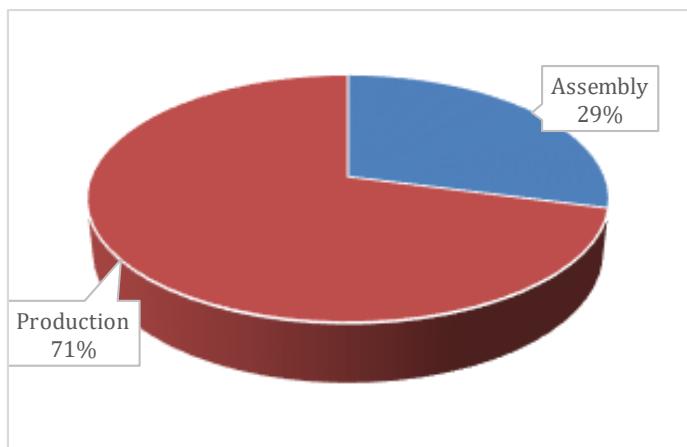
Figure 14. Invested capital in announced FDI transactions in Nizhny Novgorod, mln. USD



4.3. Profile of respondents

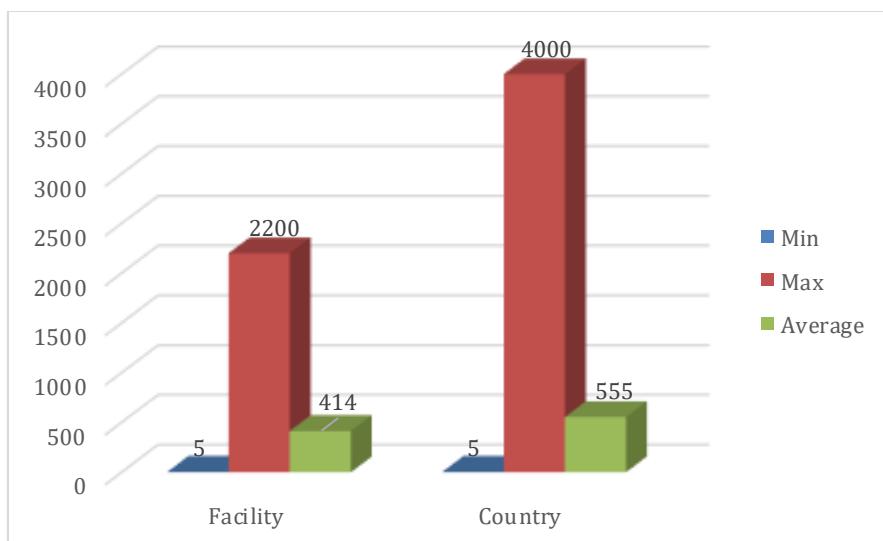
A majority of the respondent FDI companies identify themselves as production companies. A smaller share of respondents is exclusively doing assembly rather than full production. In cases where a business does both assembly and production, they were categorized based on the larger activity as a contribution to revenue. Most of the assembly companies expressed the intention to increasingly move into production, as the local supplier capacity becomes sufficient to compete with import.

Figure 15. Type of business of the respondents



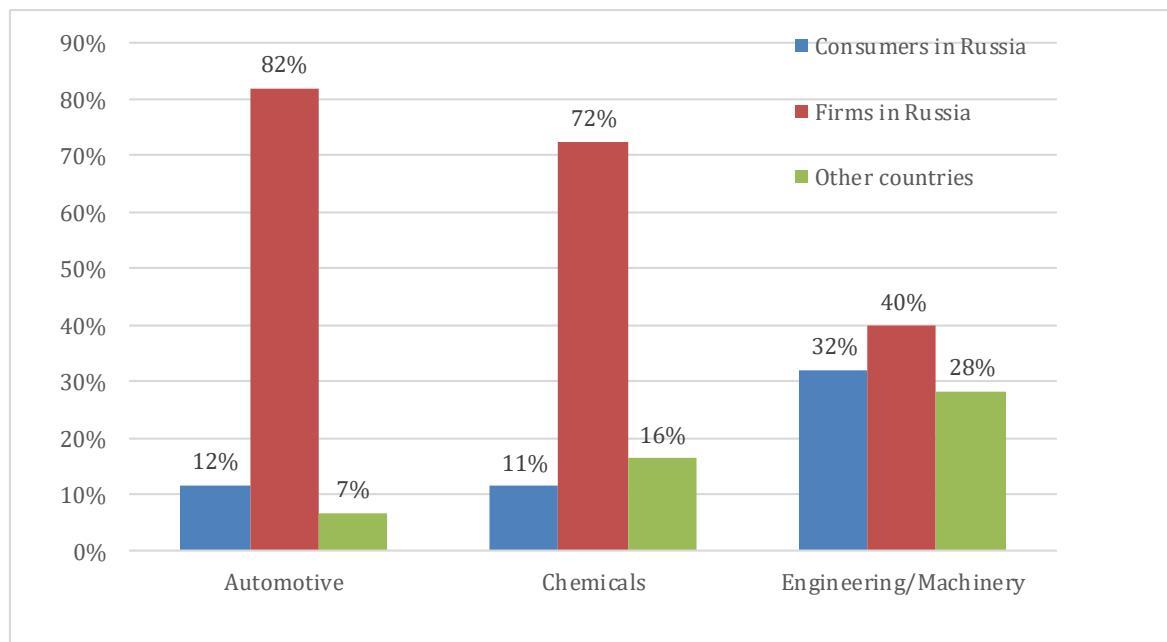
The respondents mainly represent midsized local subsidiaries of larger foreign or international companies. Larger firms are mainly working in automotive assembly or component production, while chemical and engineering businesses tend to have smaller operations. Engineering/machinery companies have the lowest average number of personnel. The chart below indicates personnel numbers reported by the respondents at separate facilities and overall in the country (in case of several local facilities in Russia).

Figure 16. Number of personnel at the surveyed companies



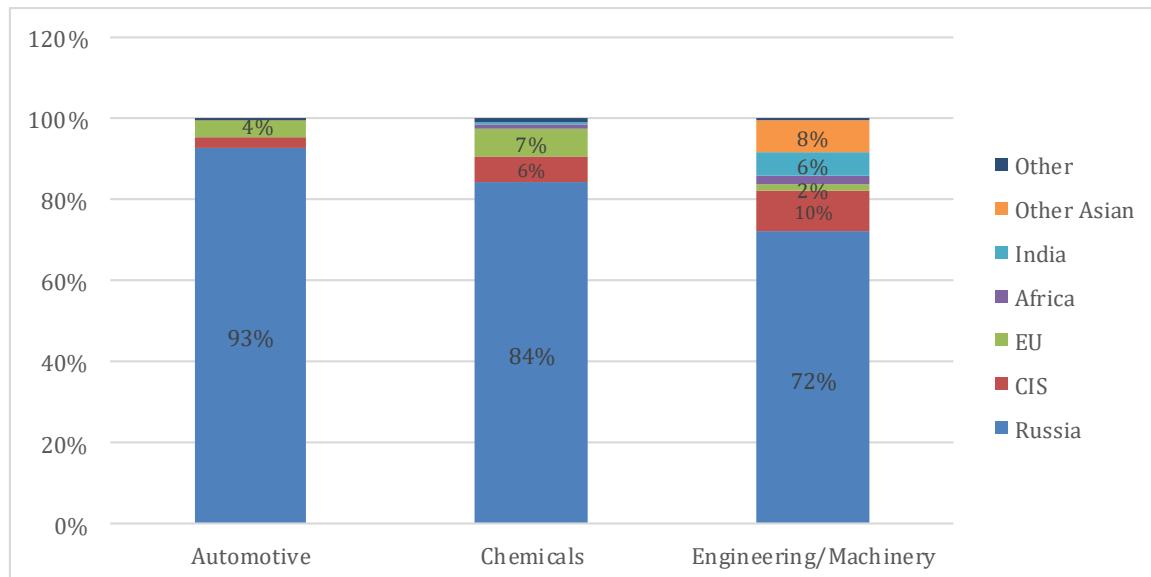
Almost all the respondents derive a clear majority of their revenues from Russia with more respondents concentrated in the B2B segment and fewer with B2C sales. The automotive sector demonstrates the highest share of local B2B sales, while the chemical and engineering/machinery respondents are more diversified with B2C revenues and exports. The B2C segment is less represented in the survey due to the selected industry sectors where B2B sales are more common.

Figure 17. Sources of revenues of the surveyed companies (% of the total revenues)



As mentioned above, for most respondents, the greatest revenue share come from Russia. The automotive sector is highly structured around supplying the Russian automotive industry, while the chemical and engineering/machinery sectors demonstrate a more diversified sales structure with greater exports. The main target export markets for Russian FDI respondents are the CIS countries and the EU. A portion of revenues does come from other regions of the world, including Asian and African countries, but its contribution to the overall picture is small. This sales pattern reflects the overall strategy of MNCs to work in Russia both to access the local market and reduce expenses for logistics as well as access neighboring markets in the CIS. Engineering/machinery FDI producers demonstrate the most versatile geography with more presence in Asian and African countries as well as in the rest of the world. In all cases, the local market provides more than 70% of revenues.

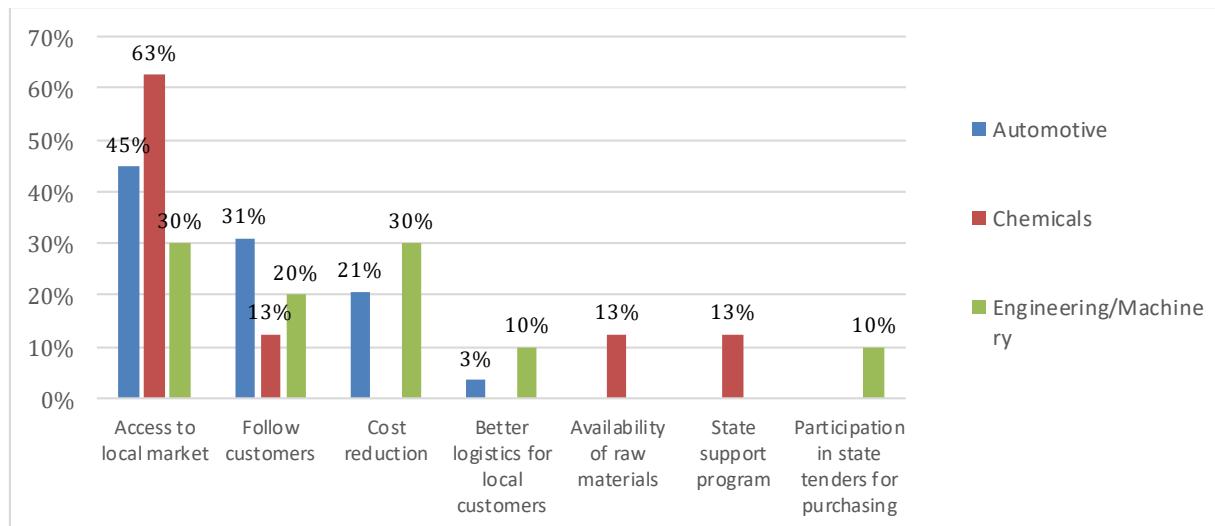
Figure 18. Primary markets of the surveyed companies (% of the total revenues)



4.4. Main survey findings

Respondents from all sectors are consistent on the main reasons why they set up businesses in Russia: access to the local market, a global strategy of following major customers that become localized in Russia and the reduction of cost for labor and infrastructure. The first two reasons may collectively be referred to as “market-seeking”. In addition to the above reasons, for some respondents, logistical considerations, aspiration to participate in state purchasing programs (which requires a “made in Russia” status), the raw material base, and intentions to obtain financial benefits from the state played a role in their decision.

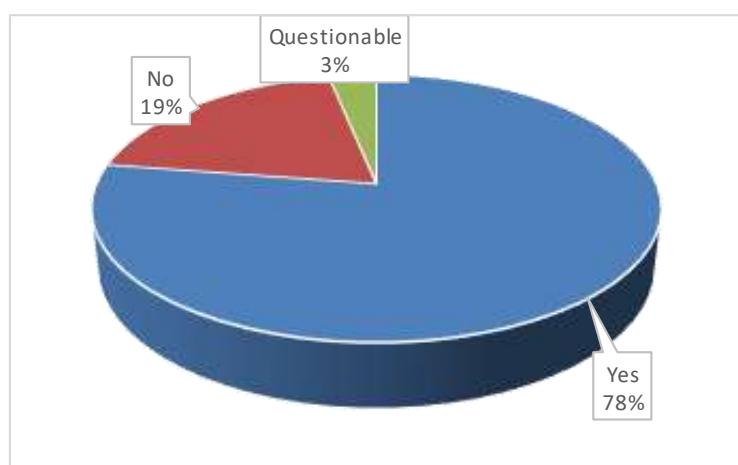
Figure 19. Reasons to set up operations in Russia (% of respondents)



Access to the local market seems less critical for engineering/machinery companies, presumably for less country sensitive output as opposed to locally marketed cars or bulky/specific chemicals. For chemical and automotive companies, the local market is a clear first priority with following customers and cost reduction issues following closely.

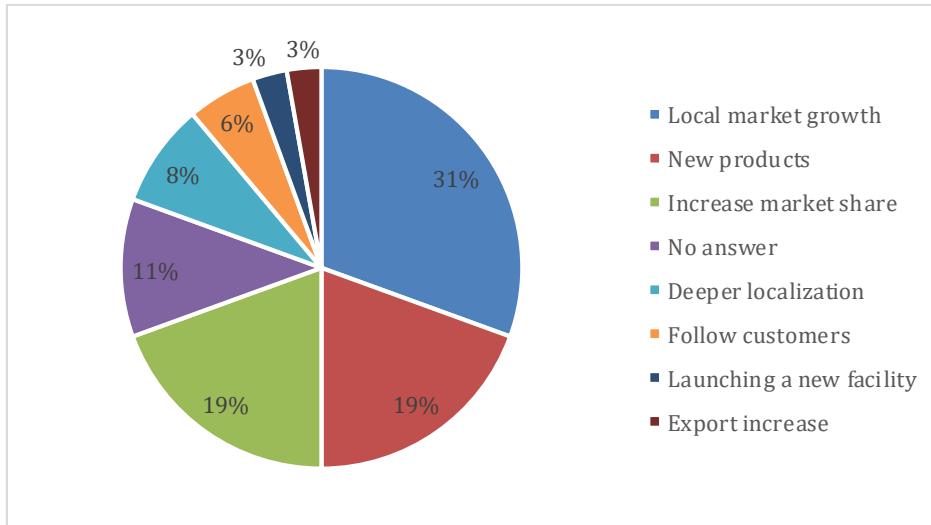
Most of the respondents have plans for further expansion in Russia. Many of them mention that their initial plans of deploying local facilities are being currently revisited, given the changes in the market landscape since 2014. Regardless, three quarters of the companies interviewed clearly expressed their intention to remain in Russia and continue the expansion of their business (Figure 20). In many cases this expansion will facilitate more linkages with local suppliers.

Figure 20. Share of the surveyed companies planning further expansion in Russia (% of quotation)



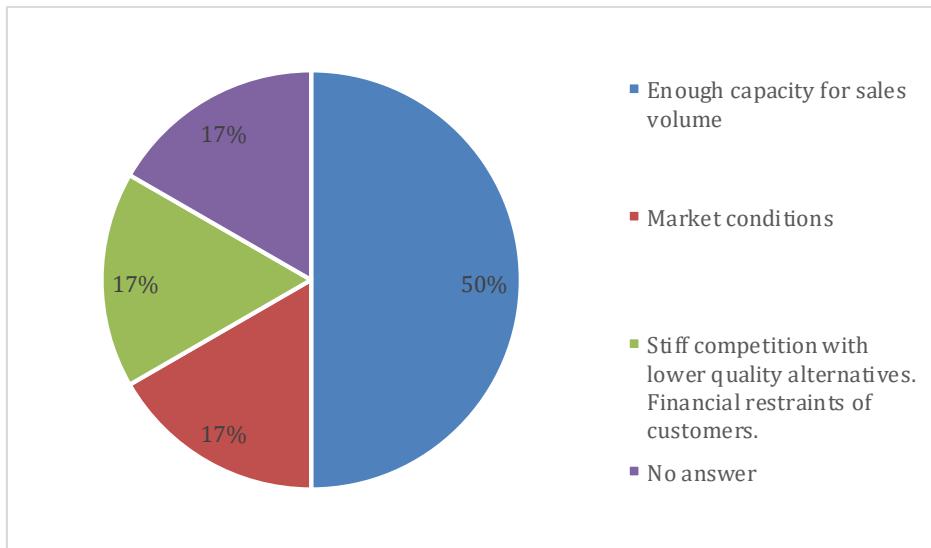
The main reasons for expansion differ from the reasons for the initial market entry. Despite adverse market conditions, the majority of respondents cited expansion plans in Russia. The reasons behind them differ from the reasons for the initial launching of local facilities (Figure 21). At the initial stages, the main drivers were access to a new market and following strategic customers. Going forward, their expansion plans are associated mainly with market growth expectations, the launching of new products and the fight for market share.

Figure 21. Reasons for further expansion



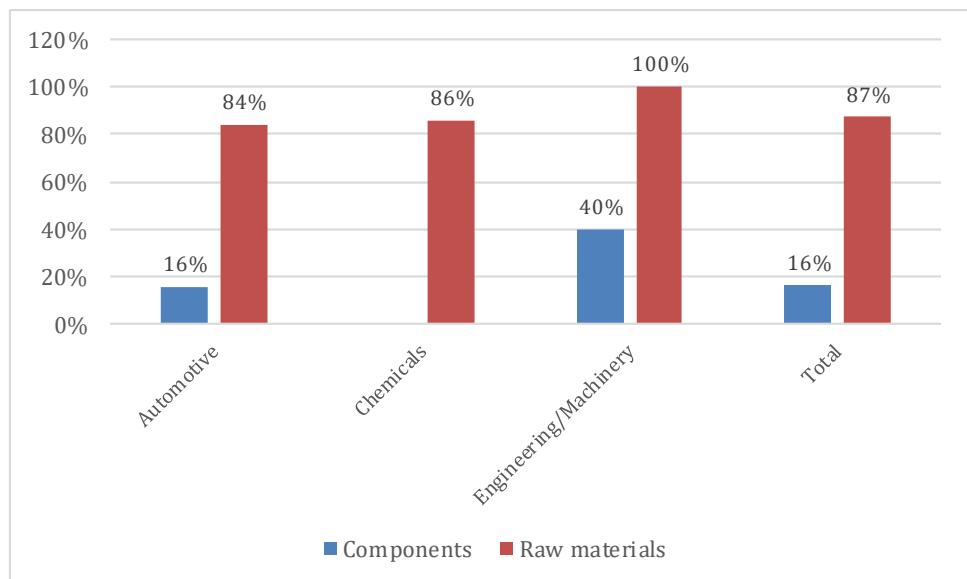
Firms not planning expansion cite market factors. These include the capacity of existing production to meet current demand as well as broader market conditions which may include both national and global economic conditions as well as increasing uncertainty resulting from trade tension and sanctions. Some companies also cited competition on prices that undermines the value-added nature of their business.

Figure 22. Reasons for not having expansion plans (% of quotation)



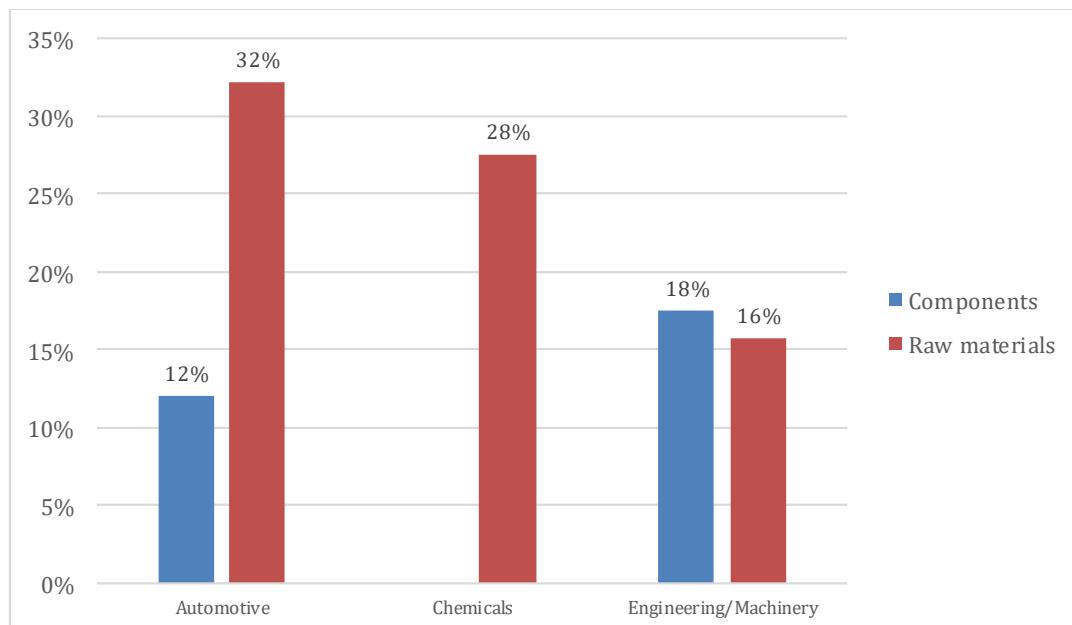
A majority of the respondents engage in local purchasing of raw materials while only a minority source more value-added components. For basic raw materials, the respondents demonstrate high rates of local purchasing (87% on average) across all sectors, while for intermediate goods or components, the rates are far lower. Companies in the chemical sector source virtually nothing beyond raw materials, but this is largely a product of the value chains for production in the sector. The engineering / machinery sector reports the highest level of component sourcing at 40%.

Figure 23. Raw material and component sourcing (by the respondents' number)⁶⁵



While a large proportion of firms source raw materials, the value of these inputs is low. Despite the fact that most of the respondents engage in local purchasing in the automotive sector, this local sourcing of raw materials amounts to only 32% of total material inputs by value. The values are even less in Chemicals and Engineering (28% and 16% respectively).

Figure 24. Average % of local supplies in total purchase of material inputs (by value)

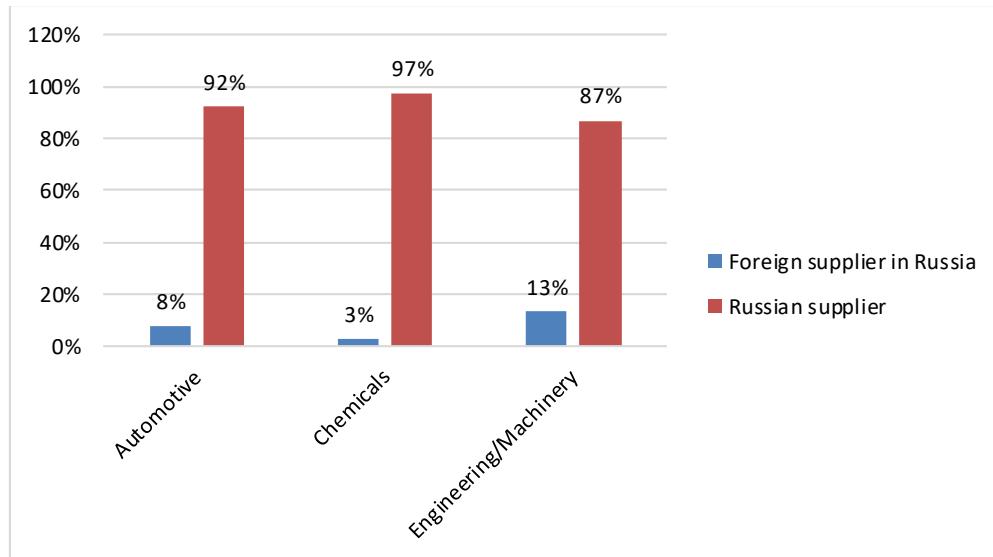


The share of locally purchased components remains at a lower level of 12% for automotive and 18% for engineering with no reported purchasing activity in the chemical sector. Figure 24 indicates the fundamental challenge for FDI linkages in Russia. Only a minor part of the lesser value-added raw materials are purchased locally and the numbers deteriorate when shifting to deeper processed materials and further when moving to components.

⁶⁵ Raw materials in this classification include generic supplies, such as packaging, etc.

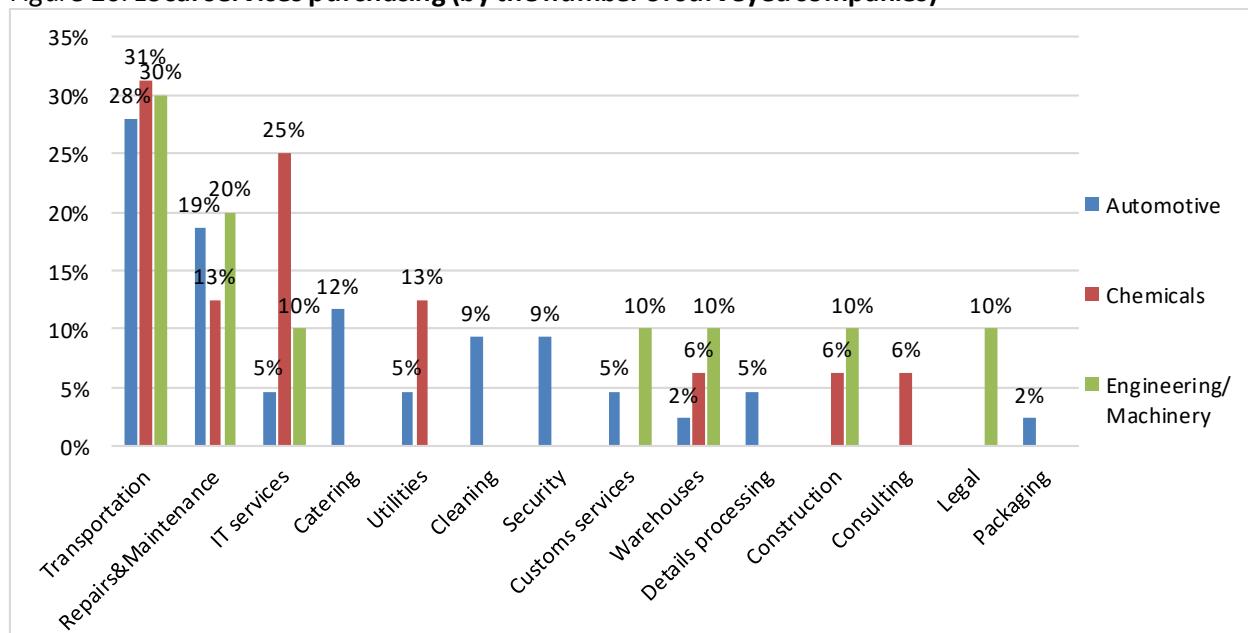
When sourcing locally, foreign investors predominantly buy from domestic firms. Only a small share (from 3% to 13%) of local inputs are purchased from foreign suppliers in Russia; the remainder are purchased from domestic firms. While many of the respondents were in favor of purchasing from local subsidiaries of foreign suppliers due to quality compliance standards, in most cases the local suppliers were unable to provide the specific inputs with the cost or volume required.

Figure 25. Type of local suppliers for the surveyed companies (% of the value of material inputs)



Most of the respondents purchase local services from contractors; the range of services is quite comprehensive. The services relate mainly to production (costs of goods sold – transportation, utilities, repairs & maintenance, processing, packaging, etc.), commercial activities (warehousing, customs, etc.) and general and administrative overheads (Figure 26). The absolute leaders are transportation, maintenance, and IT services. Chemical companies more often pay for utilities and IT services as their businesses are more resource intensive and require IT systems to control production lines. Engineering/machinery companies purchase a wider range of services related to export activities (i.e. customs services etc.), which is in line with their more versatile geography of sales. Automotive companies more frequently spend on site and personnel-related costs (transportation, catering, cleaning, security, etc.) as they are on average larger and hire more staff.

Figure 26. Local services purchasing (by the number of surveyed companies)

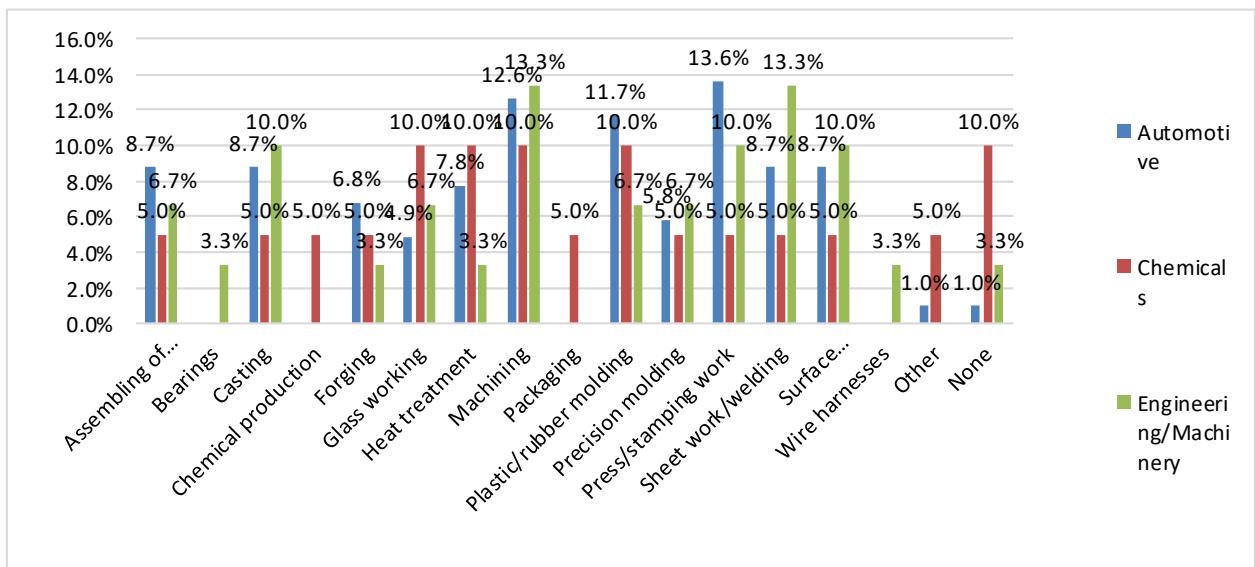


Only a small share of respondents do not intend to source more materials/ components/ services locally (9% in the automotive industry, 17% in chemicals and 8% in engineering/machinery). Others consider increasing the local sourcing as a priority, however, they view this as a long-term process, due to the need to find local suppliers compliant with their quality and management system requirements. As shown in table 3, the respondents are mainly interested in increased local sourcing of components, metals (materials and parts) and plastics (materials and parts).,

Table 3. Materials/services the surveyed companies would prefer to source locally (% of quotation)

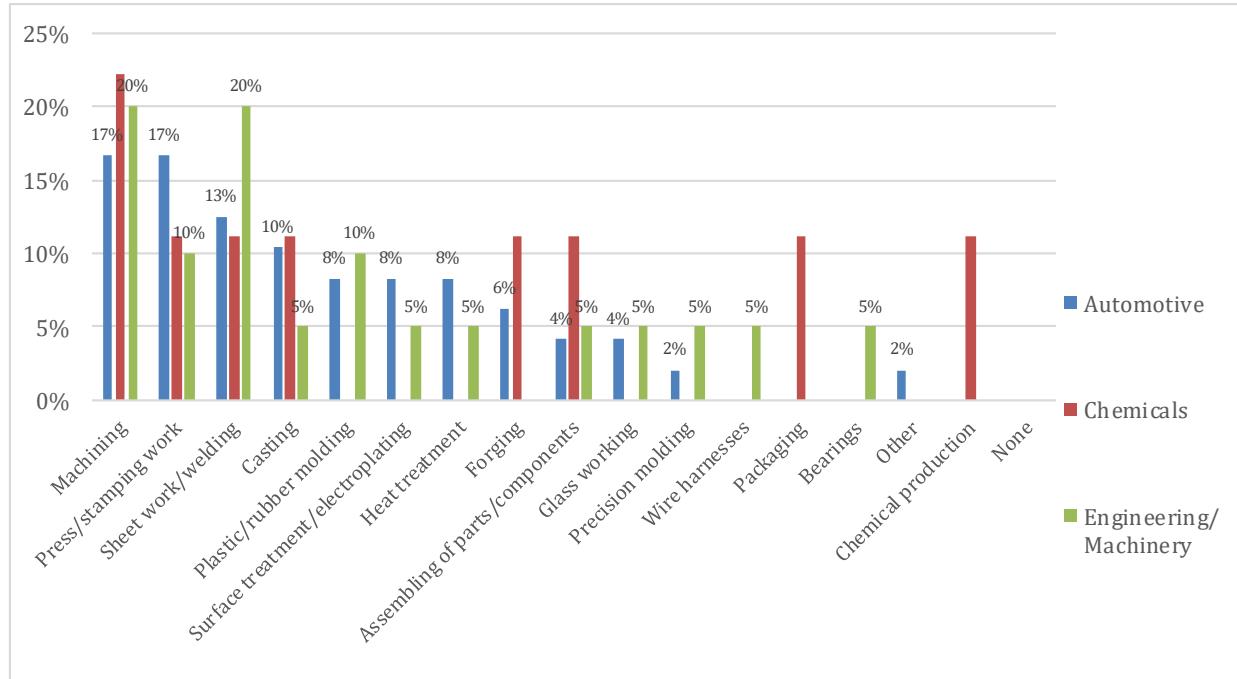
Material/service	Automotive	Chemicals	Engineering/Machinery	Total
Components	30%	25%	25%	28%
Metals, material and parts	33%	17%	25%	28%
Plastics, material & parts	14%	0%	17%	12%
None	9%	17%	8%	10%
All	0%	0%	8%	1%
Glass, material and parts	2%	0%	8%	3%
Technological processing	5%	0%	8%	4%
Resins	2%	8%	0%	3%
General supplies	2%	0%	0%	1%
Difficult to answer	0%	8%	0%	1%
Tooling	2%	0%	0%	1%
Chemicals	0%	25%	0%	4%
Total	100%	100%	100%	100%

The survey included detailed questions on specific processing methodologies and found that all are in demand. Many respondents require nearly all the indicated processing methods, reinforcing the finding that a key constraint in the development of linkages is the lack of capacity among domestic suppliers to meet the needs of large buyers. Each of the processing technologies included in the survey has unique quality requirements, technology standards, and skill requirements for the operators, all of which require a significant investment from domestic firms. **Figure 27.** Processing methods required from local suppliers



The respondents also indicated which processing methods they are currently seeking. Among them, the most popular processing types are machining, press/stamping work, sheet work/welding, casting, and molding (Figure 28).

Figure 28. Processing methods currently needed (% of quotation)



The respondents ranked the level of difficulty to find locally supplied services for a reasonable ratio of price/quality (1 means “no difficulty”, 2 – “some problem” and 3 – “severe problem”) – Table 4. Highlighted by difficulty, the most challenging types of services to locate are marked in grey.

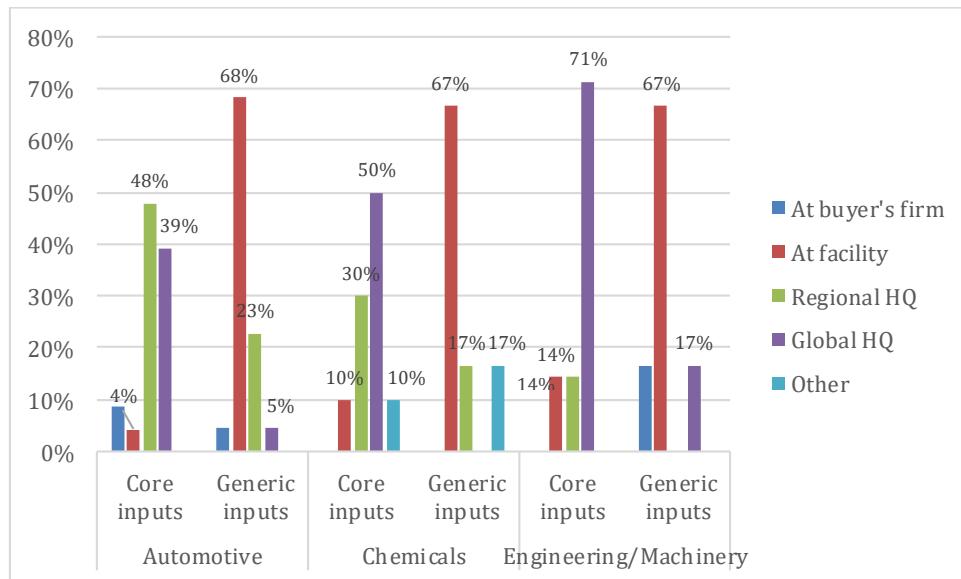
Table 4. Locally supplied services and their level of difficulty to find an acceptable price/quality ratio (from 1 to 3)

Service	Average Rating	Difficulty			Total
		Automotive	Chemicals	Engineering/ Machinery	
Other					2,5
Engineering services		2,1	2,4	1,8	2,1
Repair&Maintenance		1,9	1,6	1,4	1,7
Packaging materials		1,6	2,0	1,0	1,6
ICT services		1,5	1,3	1,8	1,5
Financial services		1,2	1,7	1,8	1,5
Warehousing&Storage		1,2	1,2	1,2	1,2
Customs brokers		1,2	1,3	1,0	1,2
Transport&Logistics		1,1	1,4	1,2	1,2
Total		1,5	1,6	1,4	1,5

In most cases, regional or global headquarters of MNCs make the selection of suppliers for core inputs (Figure 29Figure 29. Location of decision-making for the selection of suppliers (% of quotation)). This usually stems from centralized quality management and logistical systems of MNCs. This finding also

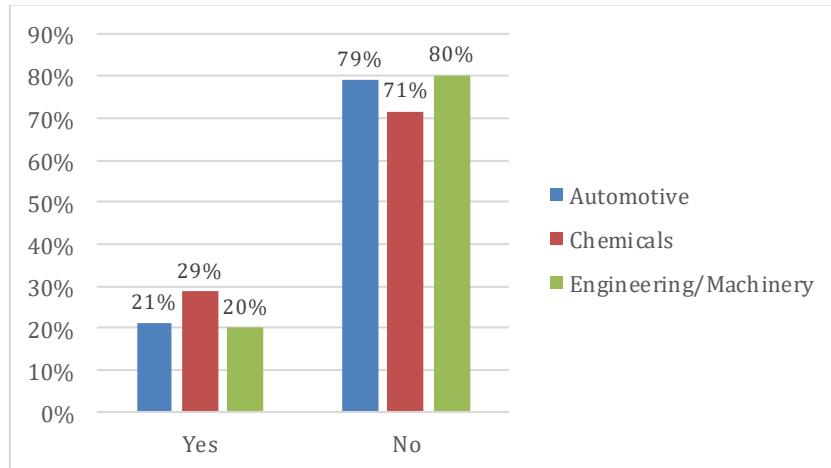
indicates a need for more comprehensive work to incorporate local suppliers into global value chains for core industries.

Figure 29. Location of decision-making for the selection of suppliers (% of quotation)



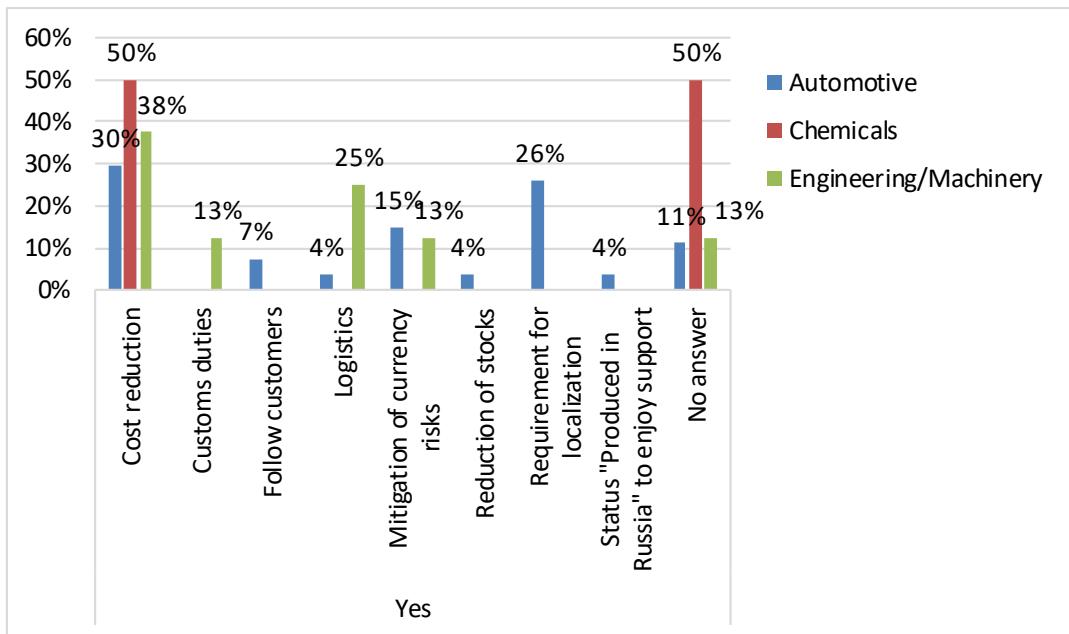
Approximately a quarter of respondents enjoy preferential terms for customs duties. These are mainly a result of industrial assembly agreements and the location of businesses in special industrial infrastructure zones.

Figure 30. Share of the surveyed companies that have exemptions from customs duties (% of quotation)



Over 90% of the respondents consider further localization as a priority. Most answers focus on cost and time effectiveness of local suppliers (Figure 31). The automotive sector often mentions pressure for localization from the state and legislation. Some MNCs also indicate other commercial motivation, such as mitigation of currency risks and inventory management.

Figure 31. Drivers for further localization



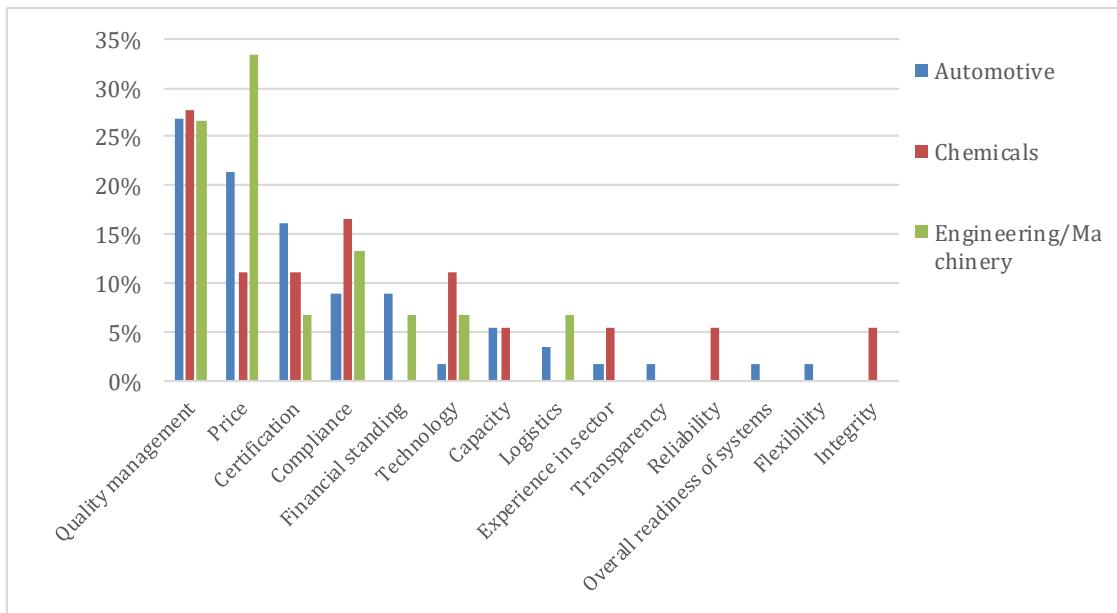
The respondents identified major barriers to local sourcing. Estimation of barriers is ranked 1-3 where 1 represents “no problem”, 2 as “cumbersome” and 3 as “severe problem”. The most problematic issues are marked in grey (Table 5).

Table 5. Barriers for local sourcing (from 1 to 3)

Issues	Average rating (1-3)
Inputs we need are just not available locally	1 2,8
Too time consuming to identify potential Russian suppliers (no local suppliers)	2 2,1
Russian suppliers lack basic certifications needed to do business with us	3 1,7
Potential Russian suppliers don't meet our Quality Cost Delivery (QCD) standards	4 2,4
Russian suppliers lack management capabilities to be long term suppliers	5 1,9
Potential Russian suppliers lack design or innovation capabilities	6 2,1
Russian suppliers lack production volumes to meet your minimum requirements	7 1,6
Fiscal incentives make importing a more competitive option than engaging with local supp	8 1,5
Dealing with Russian suppliers is cumbersome due to VAT issues	9 1,0
Other	10 2,0
Overall	
	2,0

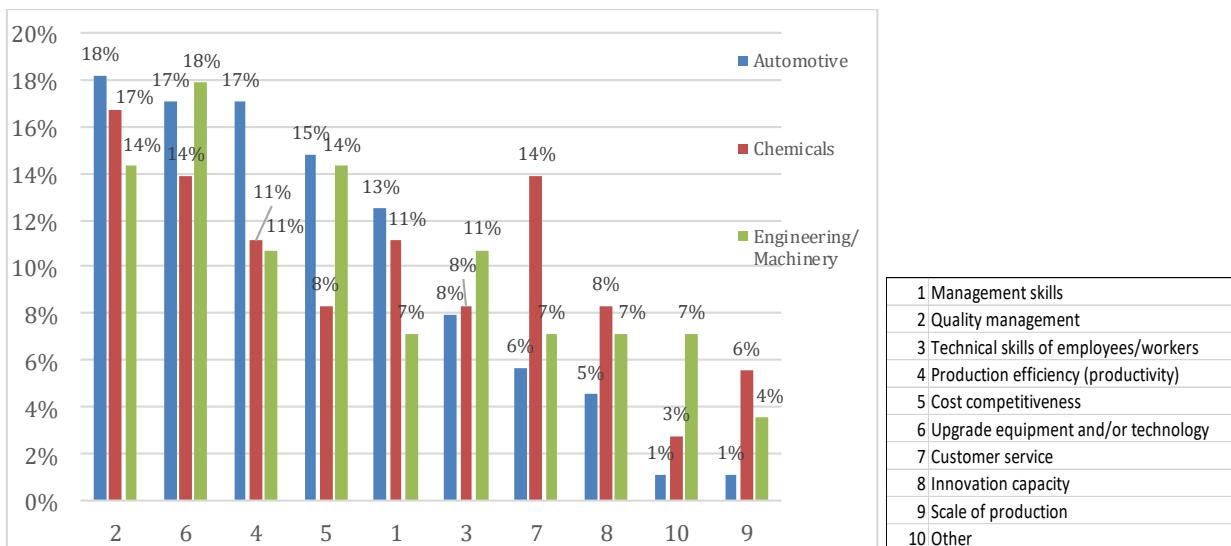
Respondents were also asked to indicate the three main criteria for working with a supplier. While price is in the second highest factor, it is important to note that the top rating is for quality management with certification and compliance ranked third and fourth respectively, suggesting buyers are not willing to sacrifice quality for the sake of price; rather the overall approach to quality including standards, compliance, and certification are together more important than price.

Figure 32. Most important factors in selecting local suppliers



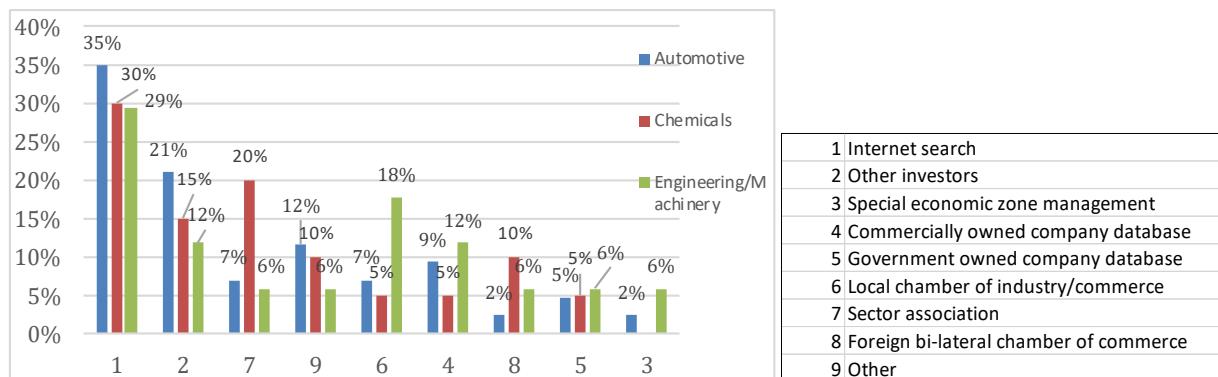
These factors mirror the priorities that buyers identified for local supplier development. The survey asked separately about the most important capabilities that local suppliers should improve to better meet the needs of FDI companies. Management and quality issues top the responses with cost competitiveness in the fifth position.

Figure 33. Critical issues for local supplier development



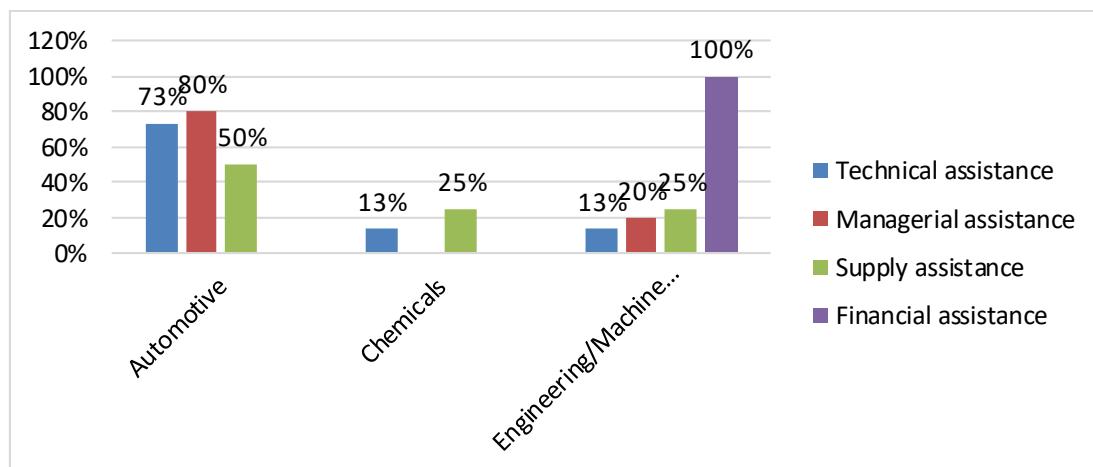
Respondents rely on traditional choices to find potential suppliers. The leading sources are internet searches, references from other investors and specialized networking organizations (Figure 34). Among other sources not explicitly mentioned in the list, respondents indicated exhibitions, information from authorities and partners, and information from the company's staff.

Figure 34. Sources of information used to search for local suppliers



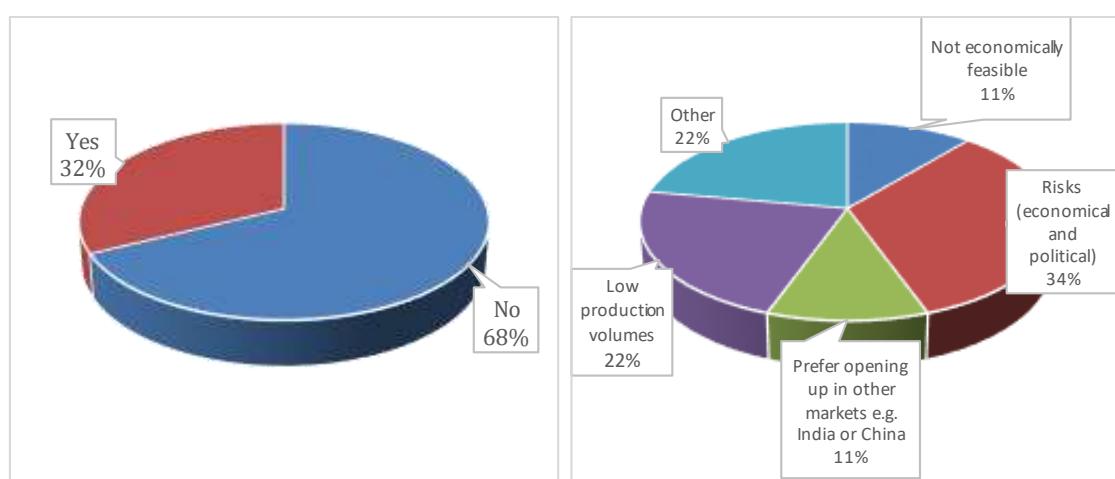
FDI companies are providing technical and managerial support to their long-term supply partners. The technical support normally includes advisory consultations with regard to technology and operation of production lines. The managerial support in many cases focuses on quality management systems. Companies are less engaged in providing assistance with supplies and even less so in providing finance.

Figure 35. Support provided by the surveyed companies to their suppliers



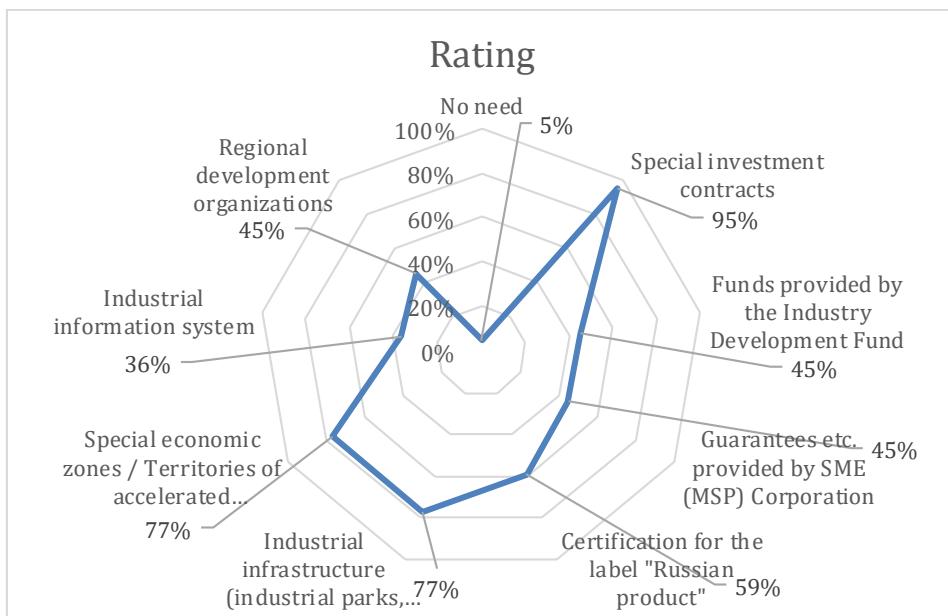
Respondents were asked if they have tried to invite their partner foreign suppliers to either relocate to or launch production in Russia. Only 1/3 of the respondents had taken such steps, and, to date none of their foreign suppliers have entered the market. Reasons given by the suppliers are indicated in Figure 36.

Figure 36. Left: Share of firms requesting foreign suppliers to establish production in Russia. Right: Feedback from suppliers on reasons not to enter the market.



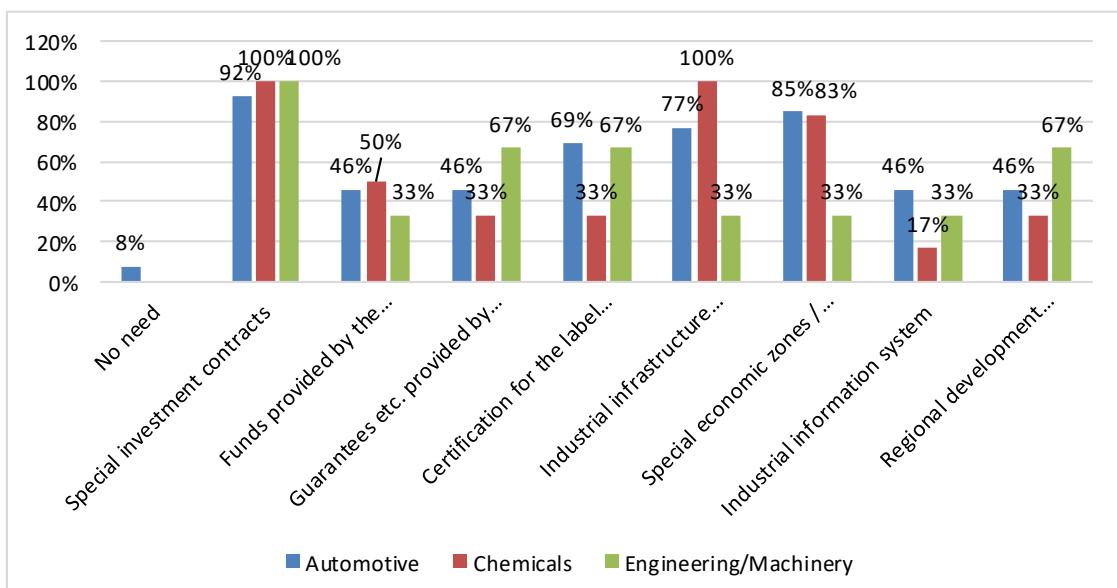
Awareness among FDI companies of state localization support measures is generally moderate. Most of the respondents are quite familiar with special investment contracts and general support infrastructure, such as special economic zones and territories of accelerated development (Figure 37). Other support measures are less known to FDI companies. While there is awareness of the activities of regional support organizations, other initiatives like the “Russian product” label are less well known. The same applies to the numerous measures of financial support. A small fraction of respondents indicated that they do not need any support (“No need” item).

Figure 37. Awareness of support measures



Surprisingly, on average, companies from different sectors demonstrate comparable levels of awareness of instruments (Figure 38). Automotive companies are historically better informed of the support infrastructure as their localization process has been a focus of companies and policymakers for more than a decade. Nevertheless, engineering/machinery and chemical sector companies report comparable levels.

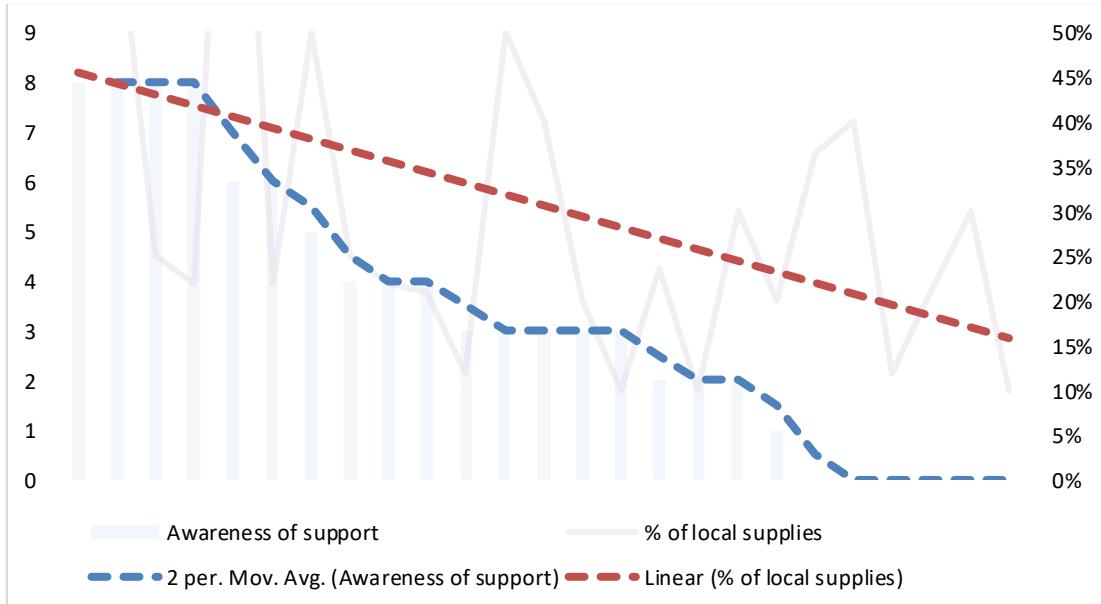
Figure 38. Awareness of support measures



A simple analysis was conducted to assess if awareness of the support systems and actual localization of supplies are correlated. First, companies were ranked in descending order of cumulative awareness of

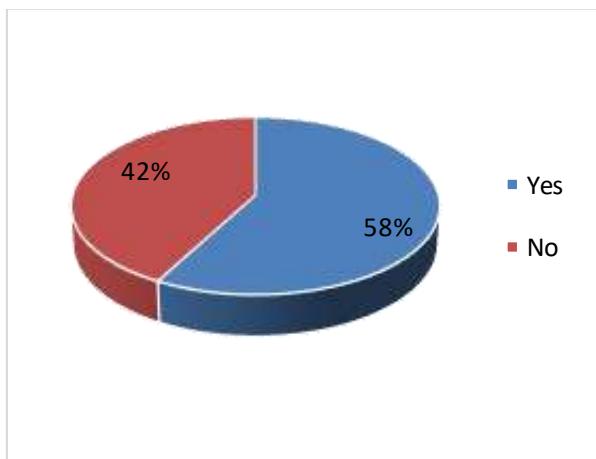
state support infrastructure. Then, to eliminate the statistical noise of deviations in individual values, a trend line for % of supplies was calculated. The result shows that awareness of support is indeed correlated with the share of localization in the supply chain. While this simple analysis is not sufficient to determine causality, the results suggest that an informational campaign to increase awareness of state support by FDI companies could be a useful means to help further the localization of supplies.

Figure 39. Correlation of support system awareness and the % of local supplies



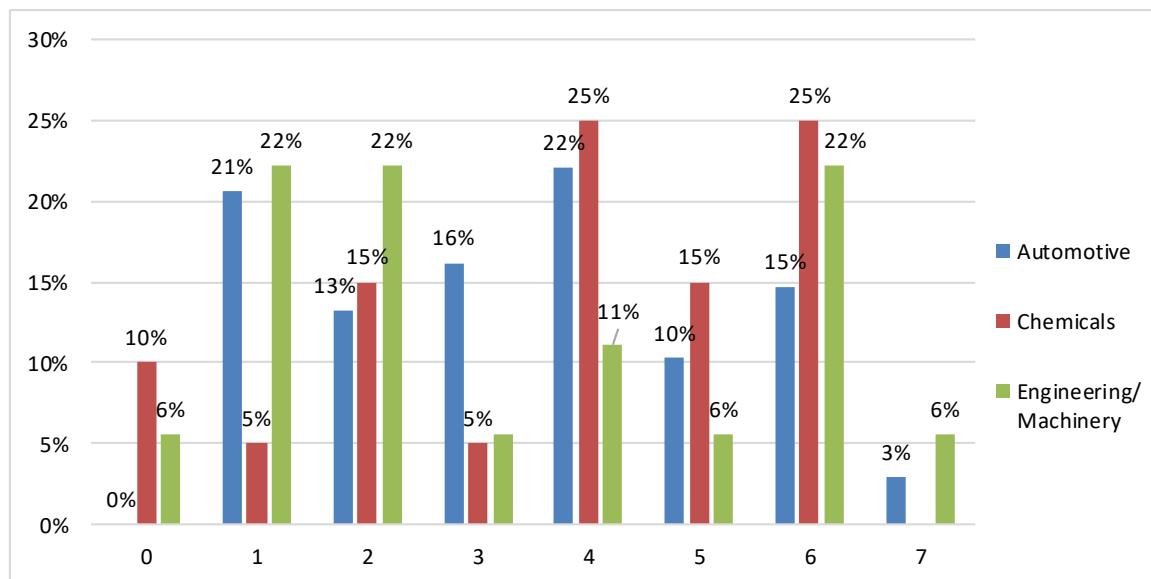
Over half of respondents expressed readiness to actively partner with state agencies on capacity upgrade initiatives. 58% of respondents are willing to participate in state programs supporting linkages (Figure 40). The 42% that would not participate stated various reasons, including negative previous experience working with state agencies, a perception of high bureaucracy and fears of corruption, and some company policies (often at the international level) limiting subsidiary participation in government support programs.

Figure 40. Readiness of companies to cooperate with state agencies on the implementation of supplier development programs



Financial incentives are in highest demand. While, on one hand, this is not surprising given the direct impact of fiscal incentives on profitability, it may also demonstrate partial unawareness by MNCs of proposed non-financial support measures and/or lack of confidence in their effectiveness.

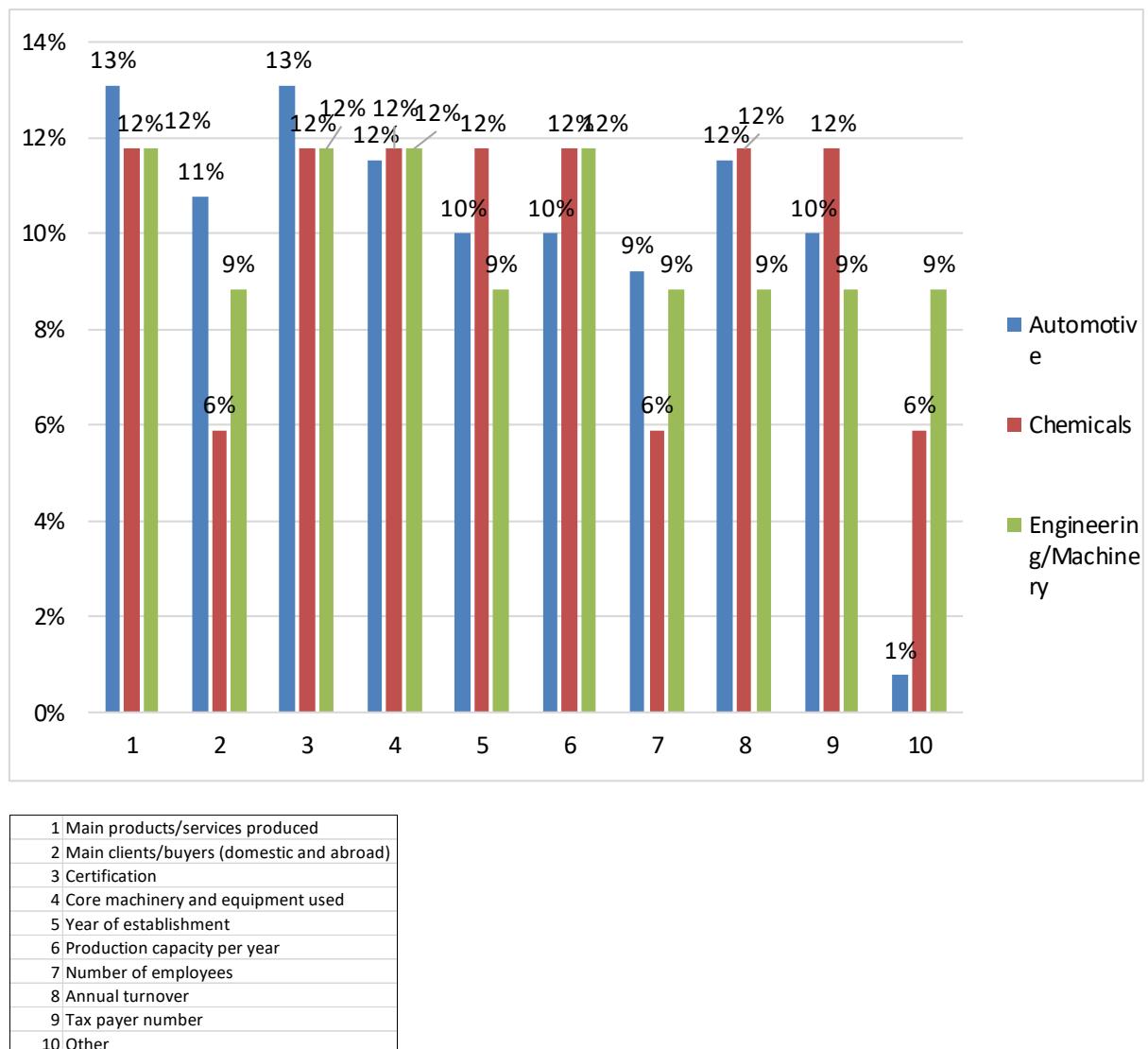
Figure 41. Estimated need for state support services/measures among the surveyed companies



0. No need
1. Availability of a high-quality supplier database
2. Organization of targeted B2B matchmaking events (meet the buyer, speed dating, etc.)
3. Introduction of supplier capacity development programs
4. Financial benefits to foreign investors to encourage local sourcing
5. Financial benefits to foreign investors for the training of local suppliers
6. Financial benefits for local suppliers to invest in upgrades
7. Other

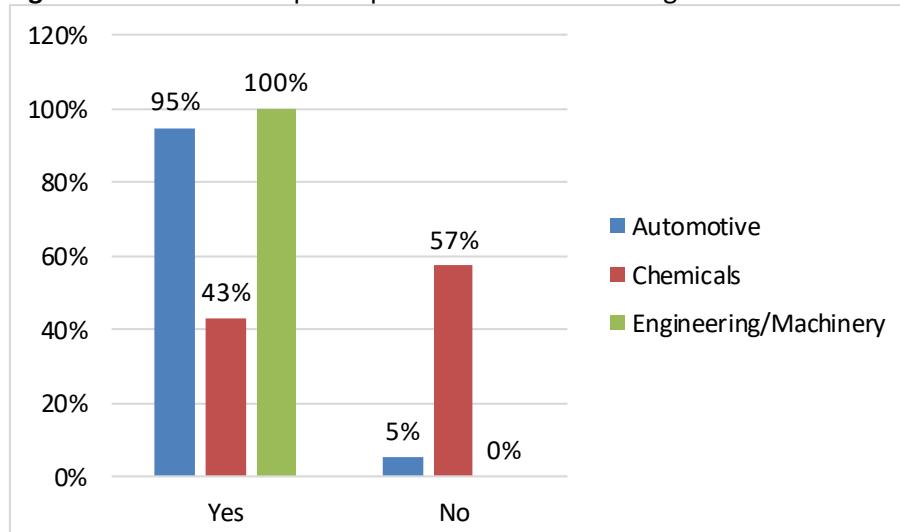
Most of the respondents (95%) believe a national database would, in principle, be of help for intensifying cooperation between FDI companies and local suppliers.

Figure 42. Desired content for a supplier database



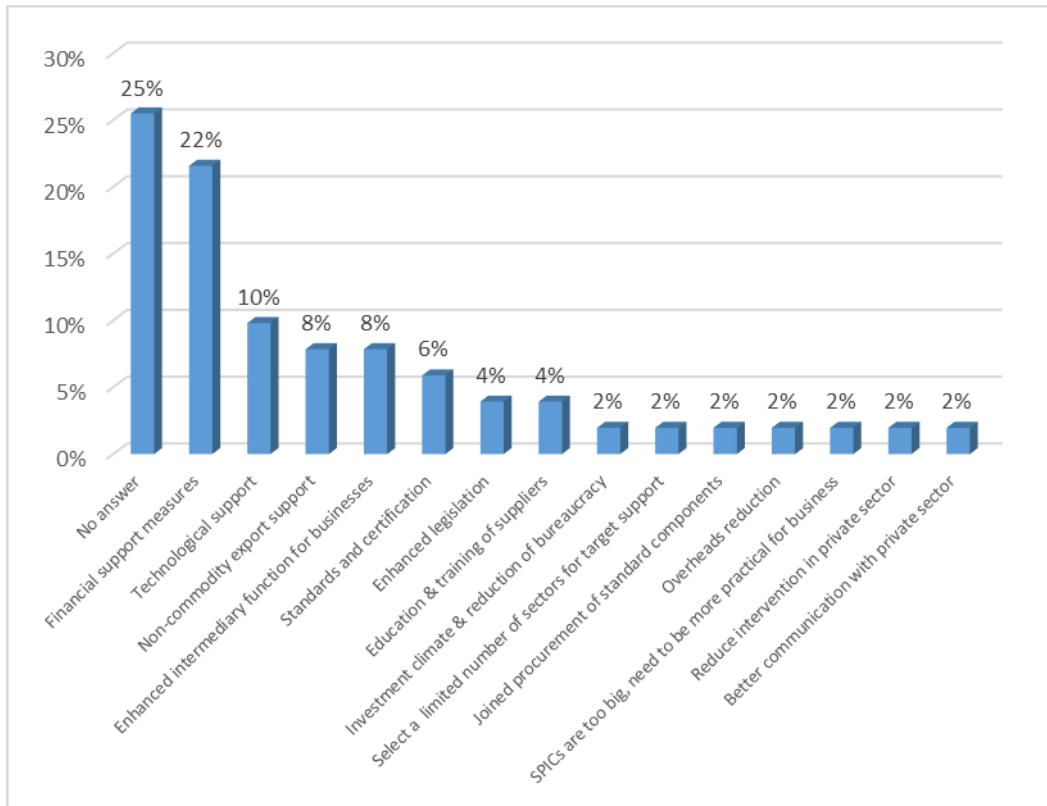
The majority of respondents would be open to B2B matchmaking events organized through state support initiatives.

Figure 43. Readiness to participate in B2B matchmaking events



Respondents shared their views on what strategic directions need to be prioritized by state support initiatives for supplier development. Responses varied (including a quarter of firms that did not answer) with financial support and technological support leading the responses.

Figure 44. Key directions for state support of suppliers



5. Results of the survey of potential Russian SME suppliers

Key findings. Among SME survey respondents:

- Most consider increasing the cooperation with MNCs as a priority
- The main obstacles for the development of such cooperation are related to communication barriers, lack of information on the demands of MNCs and their requirements to suppliers, a lack of funds for capacity upgrading, and low volumes of potential orders from MNCs
- FDI linkages development is also hampered by weak management systems and logistics, lack of skilled staff, and outdated equipment/technologies
- Most do not receive any state support in the development of FDI linkages
- Most believe that financial support, improvement of the regulatory regime (currency control, customs procedures, certification), provision of information on the demands/requirements of MNCs, and assistance in accessing decision makers at these companies are the key measures to boost FDI linkages

5.1. Background of the survey

In order to ensure consistent analysis of MNCs' procurement activities in Russia, a survey of local SMEs was conducted. The survey was organized in the same regions (Moscow, Saint-Petersburg and Nizhny Novgorod) and the same sectors (automotive component production and assembly sector, chemical sector, engineering/machinery sectors) as the survey of FDIs. The rationale for the survey on SMEs is that SMEs are major beneficiaries of state support in the development of FDI linkages, in comparison with larger corporations that have sufficient internal resources to develop their cooperation with MNCs and are less interested in such support.

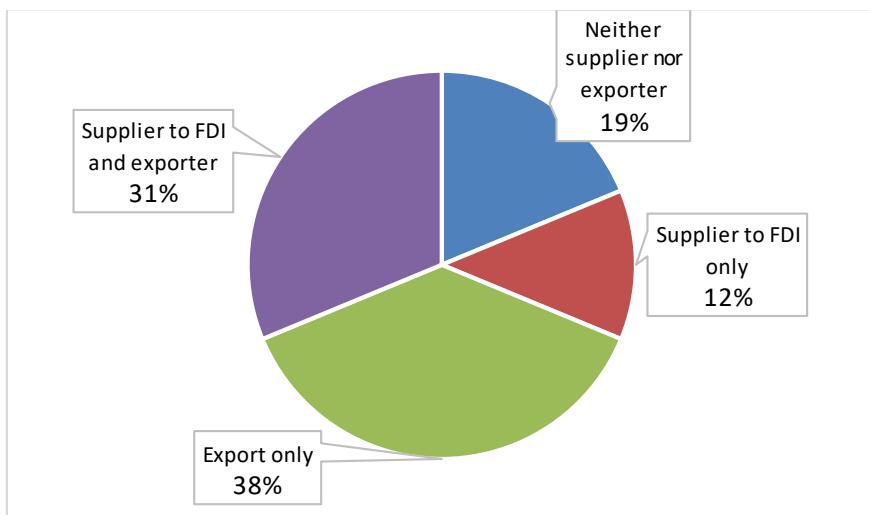
SMEs with production facilities in the above regions and sectors were invited to participate in the survey. In its entirety, the total number of those surveyed amounted to 32 industrial suppliers/potential suppliers to FDI companies with 16 producers from the chemical sector, 9 producers from the general machinery sector and 7 producers from the automotive sector. In order to select SME suppliers/potential suppliers that meet the above criteria and are interested in the survey, assistance from the regional business support agencies was sought. The SMEs invited to participate in the survey either had already cooperated with FDI companies in Russia or have the potential to cooperate in this way. As a result, 15 industrial suppliers (8 in the chemical sector, 4 in the machinery sector, and 3 in the automotive sector) were interviewed in Moscow; a focus group of 8 companies (5 in the chemical sector, 2 in the machinery sector, and 1 in the automotive sector) representing all three selected industry sectors was put together in Saint-Petersburg and three separate focus groups (3 companies in each group) for the three sectors respectively were put together in the Nizhny Novgorod region. The survey was performed via individual face-to-face interviews and in a focus group format with companies' managers responsible for either supply policies or general management and via the subsequent filling out of a respective questionnaire. Prior to the interviews, respondents were made aware of the fact that their participation in the survey and their feedback will remain individually confidential and will only be used for collective statistical processing without individual references to companies.

5.2. Survey findings⁶⁶

⁶⁶ Detailed report with the results of the interviews is presented in Annex 6 (the report was prepared by MAGRAM Market Research for the World Bank Group in 2019).

About half of the respondents (43%) have had experience working with FDI companies (Fig. 45). Respondents with this experience pointed out that cooperation with FDI companies is beneficial (in cases where these companies order large enough volumes of products) as these companies are more reliable buyers and are ready to pay adequate prices for quality products. Most of the surveyed SMEs (69%) export their products. The fact that SMEs are competitive in export markets points to their potential for working with foreign investors. It should be noted, however, that in some cases the export experience of the suppliers is confined to CIS countries. 19% of the interviewees are companies with solely domestic sales and no experience in FDI linkages; however, they possess the potential to develop accordingly. Export readiness and experience seem to correlate with an awareness of and experience in FDI linkages.

Figure 45. Activities of the surveyed companies with FDI linkages and export



Survey respondents that do not supply to FDI companies indicated that the main reasons for the limited cooperation are related to the communication barriers, information asymmetry regarding the needs and requirements MNCs have for suppliers, and a lack of funds to finance the required upgrades in the areas of technology and management.

Other key reasons for the lack of cooperation between potential suppliers and FDI clients include the following:

- A lack of understanding of FDI companies' supplier policies and ways to achieve compliance with those policies in terms of management, production, and logistics.
- Investments required to reach compliance are not economically viable due to the low volumes of orders by a single FDI client (there is limited cumulative order potential on the side of FDIs for small local markets).
- Dependence on imported raw materials and a sub-optimal scale of production undermines the price competitiveness of local suppliers.
- A lack of coordinated regional policies to guide the practical linkages between FDI companies and local suppliers.

Some SME suppliers also mentioned other problems regarding the process of supplying MNCs:

- Some experience with FDI companies that are only interested in minimal compliance with domestic localization laws and not interested in more substantive cooperation;
- A lack of qualified staff for proper interaction with FDI companies;
- Low economic incentives to work with the MNCs (some SMEs find domestic clients and state-owned companies to be easier partners to generate revenues).

The fact that nearly half of the interviewed suppliers succeeded in cooperation with FDI companies demonstrates that some of the indicated reasons for not supplying can be overcome.

The interviewees also pointed out the major deficiencies and weaknesses of their companies that hinder their cooperation with FDI clients. Key issues raised by SMEs included the following:

- Quality management systems require improvement.
- General management and administration may require improvement.
- Staff skills need to be improved.
- A suboptimal scale of production undermines price competitiveness.
- Logistics need improvement.
- The installed equipment base needs to be upgraded and some processing methods need to be upgraded/introduced.

In general, respondents are partially aware of the state support system and instruments for the development of FDI linkages and, more widely, with state industrial and export support policies. Among the most well-known/practiced instruments, there are financial support tools, support of export representation activities (exhibitions, missions, compensation of costs, etc.), and special zones/parks. Some companies reported positive experiences with state support but only in a limited sphere of cooperation with the Ministry of Industry and Trade, IDF and REC. Instruments such as services of regional centers of competence, support from FDI companies and non-financial support from state agencies are either unknown or treated with skepticism. Overall, companies do not understand the structure/requirements of the available instruments and the segregation between the federal and the regional level.

A significant portion of the surveyed companies has not obtained any support from state agencies with regard to their cooperation with FDI companies. Some SMEs reported negative experiences in communication with government structures (related to a formality and bureaucracy). Some companies mentioned that it is difficult to find information on potential foreign markets due to the lack of information provided by the state authorities and the support infrastructure, and significant delays in response to the companies' requests.

Increasing financial support and solving institutional problems (e.g. currency control, customs procedures, etc.) are the main measures that would be useful for the development of FDI linkages, according to the surveyed companies.

Among the important support instruments to improve cooperation with MNCs, the SMEs mentioned the following:

- Incentives for investments in R&D and production systems to upgrade technologies and meet the required quality standards.
- Access to finance and simplifying taxation.
- More information on FDI clients and their requirements.
- Support in accessing decision makers at FDI companies.
- Support for reducing dependence on imported materials in regional core industries.
- Simplified customs procedures and certifications.

- Simplified currency control.

At the same time, the respondents admit that more information, knowledge, and experience are required for them internally. Acknowledgment of internal challenges at the company-level may be one of the key criteria for the proper estimation of companies' readiness for a package of support measures including financial support.

6. Recommendations

At the federal level, the legislative and institutional structure for linkages development is relatively clear with a strong lead agency in the MSP Corporation. However, given the size of the Russian Federation and the great diversity among regions in their economic structure and FDI strategies, it is recommended to complement the federal program with greater local capacity at the regional and/ or sector level to design and implement linkages initiatives.

Recommendation 1: Develop strategic linkages action plans at the local and/ or sector level

- 1.5 Take stock of lessons learned and success factors in existing linkages initiatives – both public and private
- 1.6 Conduct comprehensive regional or sectoral mapping
- 1.7 Clarify institutional roles and responsibilities
- 1.8 Articulate a regional or sector level linkages action plan

Recommendation 2: Implement the action plans with market-based policies and products

- 2.4 Deploy an appropriate mix of financial and non-financial products
- 2.5 Implement a targeted information campaign
- 2.6 Put in place a robust M&E system

The analysis done for this report has shown that there is both potential to increase FDI linkages in Russia and demand from both MNCs and local enterprises. At the federal level, the legislative and institutional structure for linkages development is relatively clear with a set of KPIs outlined in a federal project, a single lead agency responsible for implementation, and a well-defined set of products, resources, and policy measures to facilitate linkages. Since 2017, the MSP Corporation has begun implementing a linkages program with large foreign investors and these efforts have already led to nearly a dozen agreements signed and several new production lines with domestic suppliers.

However, while this national level strategy is in place, its reach to smaller foreign investors is constrained. Furthermore, global experience has shown the benefit of developing actionable linkage strategies more closely aligned to the specific context of a region or sector. Indeed, it is clear from the evidence on linkages and FDI spillovers that proximity between FDI and domestic firms, or more generally, the agglomeration of economic activity within a host economy, also promotes the occurrence of productivity spillovers. When operating in the same agglomeration, it is easier for MNC affiliates and domestic firms to identify each other and explore the possibilities to create inter-firm linkages. Once such linkages are in place, buyers and suppliers will find it easier to communicate and establish the coordination that is required on input markets. Also, it is easier for the work force to develop special skills and experience that benefit firms that operate in the agglomeration, and knowledge spillovers are more likely to occur. It then makes sense that public measures aimed at supporting the development of linkages are designed and delivered as closely as possible to these agglomerations.

For these reasons, it is recommended that the national linkages focus be supplemented with specific action plans at the level of a single region or sector. Such action plans would complement the federal focus on larger investors, help identify roles and responsibilities for regional and federal institutions, add granularity and specificity to targets and activities, and help prioritize those financial and non-financial services most in demand by linkages participants. The state support could be aimed at increasing the volume of local sourcing by MNCs working in Russia and at the improvement of the sourcing structure to increase the share of high technology components and high value added services (consulting, legal, training, etc.) in the procurement of MNCs.

Recommendation #1: Develop strategic linkages action plans at the local and / or sector level, complementing the national project.

Building implementation capacity for linkage support at the regional and sector level requires a well-defined strategic vision informed by the institutional and economic context of the region or sector. The following four recommendations outline a practical approach to developing such a strategy that blends the best practices of Russian and global experience with the specificities of the local context.

1.1 Take stock of lessons learned and success factors in existing linkages initiatives – both public and private.

As described in this analysis, the Russian Federation has implemented a range of different initiatives aimed at promoting the localization of foreign investment and the deepening of spillovers between foreign investment and domestic firms. These various initiatives cumulatively represent decades of practical experience across varying geographic and sector contexts in the Russian Federation making them an invaluable source of lessons learned and best practice. Some examples that may be of particular interest include the development of the auto components clusters in Saint-Petersburg and Leningrad region, the Republic of Tatarstan, Nizhny Novgorod region, Kaluga region, Samara region and Moscow region; various local supplier development programs implemented at the private initiative of foreign investors, such as Anheuser-Busch InBev Europe's "Smart Barley" program; initiatives of bilateral and multilateral trade promotion organizations, many of which include specific initiatives to boost localization; and the more recent experience of the national program aimed at increasing SOE and MNC procurement from SMEs implemented by the MSP Corporation.

While there are many examples of federal and regional stakeholders sharing experiences with these initiatives on both an ad-hoc and structured basis, a lot of benefit could be gained by conducting a systemic evaluation to draw out the key success factors, lessons learned, and best practices in implementation arrangements. This exercise could be structured as a series of case studies or an impact evaluation, depending on the availability of data, and would not only benefit the design and implementation of linkages initiatives in the Russian Federation, but would also be relevant to many other countries working on similar programs.

1.2 Conduct comprehensive mapping at the local level of existing or previous linkages experiences, current sourcing patterns of large investors, existing support programs aimed at SMEs, etc.

One of the current challenges in FDI linkages support initiatives at the local level is the scattered combination of programs and instruments that are dissipated over a range of support organizations, encompassing not only linkages support but also wider support for SME development and investment attraction. These instruments have the potential to be highly complementary but are rarely harmonized. More importantly, they do not always constitute a unified system that is clearly understood by both support organizations themselves and recipients/ potential recipients of support. This lack of clarity reduces the motivation for potential clients to access existing support programs. The situation is similar for sector-based promotion initiatives which are operated by a wide range of federal and regional agencies.

As a precondition to introducing regional or sector actions plans, it is recommended to conduct an in-depth review of existing support programs. Such a detailed study would consider the policy and institutional environment as well as the delivery of support tools for linkages and would identify gaps, overlaps, and opportunities to strengthen the delivery of such programs.

1.3 Establish a ‘lead agency’ role to coordinate linkages at the regional level and draft institutional guidelines including KPIs and coordination functions for the agencies playing this role

The national legislative environment in Russia is largely sufficient in terms of FDI linkages support. In addition, there are several organizations and agencies at different levels involved in the support process for FDI linkages, most significantly represented by the MSP Corporation at the federal level. However, those agencies appear to operate with little formal coordination and in each case, FDI linkages is just one of many support functions being offered. As a result, the combination of organizations involved in linkages support at the regional level is rather arbitrary; their functionality is fragmented with gaps and overlaps; the overall structure of FDI linkages support is complex and, more importantly, can be unclear for MNC affiliates and local suppliers.

Global experience has demonstrated that the most successful linkage development programs are organized around a dedicated implementation agency with a mandate to coordinate with other agencies to deliver linkages support. Given the already complicated institutional environment supporting SMEs, a general recommendation is to clarify and optimize the structure of existing agencies and give a strong mandate to a lead agency at the local level for the delivery of linkages services. While a single agency would be in the lead on linkages support implementation at the local level, the delivery of support services would be shared with a broader range of organizations. For instance, financial support tools could be delivered through existing entities working on SME finance, while advocacy services could be delivered by existing associations.

This single lead agency may differ among regions based on their existing institutional environment and private sector support functions. However, regardless of the agency that performs this role, they should utilize a common stock of products and services along with a standard M&E framework, communications strategy, etc. There is also a need for a basic training program that could help build the capacity of regional officials to implement linkages initiatives or even to better cooperate with the MCP Corporation. This could be as simple as a two-day training session for one or two staff from the regional institutions that would support linkages development.

1.4 Based on these inputs, develop the regional and/ or sector action plans for the linkages program. These regional and sector action plans would help align high level regional development plans with the federal project targets and any ongoing linkages initiatives from public or private stakeholders. The action plans should include specific targets as well as the roles and responsibilities for the various institutions involved in linkages support. Global experience has shown the importance of involving the private sector closely in the development of such action plans, and this should include not only MNC affiliates and suppliers, but also any active trade organizations and business associations.

Recommendation #2: Implement the action plans with market-based policies and products

Once the action plans have been completed, they should be implemented with a mix of financial and non-financial products and supported by outreach and M&E tools. Most of the specific financial and non-financial products that are successful globally are already in use in the Russian Federation. The focus on implementation, therefore, should be less on the design of new products, but rather on ensuring that buyers and suppliers are aware of, and can easily make use of, existing products and that they are effectively and efficiently administered.

2.1 Deploy an appropriate mix of financial and non-financial products

Supplier readiness testing and monitoring system

The analysis for this report found that domestic SMEs with potential to supply MNC affiliates have substantially varying profiles in terms of size, existing experience supplying domestic and foreign markets,

corporate structure, technological readiness, and other parameters. It therefore makes it impossible to assume that all suppliers would be suitable clients for all financial or non-financial support products. In addition, many SMEs are uncertain of their readiness to supply foreign firms. This creates suboptimal outcomes in ‘potentially ready’ firms not choosing to engage with support services and ‘far from ready’ firms electing to participate in support services. A structured approach to evaluating supplier readiness through a simple tool, which could be delivered online or in person, would help triage potential suppliers and improve the overall efficiency of support programs by ensuring that their resources are directed toward those firms that are most ready to benefit. Similar tools are already in use in the area of export readiness and could be easily adapted to linkages programs.

The readiness assessment may also have the benefit of targeting either generic or specific support to potential suppliers. SMEs that do not meet a certain ‘readiness threshold’ could be referred to other, more generic, state support programs aimed broadly at building SME capacity, while those SMEs more ready could become clients for targeted linkages support initiatives.

Targeted supplier development programs

The analysis found several persistent gaps between the needs of MNC affiliate buyers and domestic suppliers:

- Most of the FDI respondents to the survey indicated a systemic weakness in local supplier capacity in several basic processing methods and technologies and, in more advanced processes, required higher value-added components. At the same time, domestic suppliers reported a lack of clear information on which technologies or processes are most in demand by large buyers, a lack of access to finance to procure the necessary technology, and reservations about the profitability of such investment given the small size of potential sales relative to the capital expenditure needed.
- Most of the FDI respondents highlighted a gap in local supplier compliance with international product and management system standards. Many suppliers are increasingly investing in certification of their production and management (in many cases as a prerequisite to accessing export markets) but there remains an informational gap for firms that are either not aware of these requirements and/or not able to meet them.

A targeted approach to supplier development, modelled on existing experience, would help address these gaps. The supplier development programs (SDPs) may be implemented in partnership with MNCs in relevant sectors (including SDPs aimed at the potential local suppliers of high value-added services), to ensure that the programs correspond to their requirements and to the modern technology level.

Support for intensive technology innovation and upgrading.

Standalone SDPs can help raise knowledge and capacity of domestic suppliers in manufacturing and service sectors, but in most cases, these suppliers will also need to make investments into upgrading their technology and production systems. This is particularly true in Russia where the installed capital base is ageing rapidly in some manufacturing sectors (average reported depreciation in 2018 is approximately 50%⁶⁷). Respondents to the survey of the Russian SMEs collectively indicated the following issues:

- Access to finance. Most domestic suppliers face constraints in financing technology upgrades as the investment needs are usually beyond their internal resources and they report difficulties in receiving bank finance. It should be noted that there are many initiatives underway in Russia to broadly improve SME access to finance and additional specific measures such as subsidized lines of credit available for linkages investment. The constraints reported by SMEs may reflect a lack of awareness of these programs or the lag between the roll out of these initiatives and their impact on specific SMEs.

⁶⁷ http://www.gks.ru/wps/wcm/connect/rosstat_main/rosstat/ru/statistics/enterprise/fund/#

- Mid-term economic justification. In many cases, the new technologies required by foreign buyers are not required by the potential supplier's existing domestic buyers. Furthermore, in many cases, a potential contract with an MNC affiliate will not represent the majority of a supplier's sales. While SMEs do understand that technology upgrades can open new markets beyond single linkage contracts including exports and new domestic sales, they are reluctant to finance large purchases without better evidence on the return on the investment.

There are several financial and non-financial products that could help resolve this constraint. Non-financial services may include financial literacy support for SMEs, assistance in drafting business plans and loan application documentation, help with technology sourcing, and matchmaking.

It is no surprise that financial products are in high demand by potential suppliers. SMEs report many constraints in access to commercial capital. Traditional lending carries high rates of interest (as compared with average EBIT percentages) and strict terms (such as full tangible collateral, strong covenants, etc.). Equity investments are limited, particularly for smaller businesses, and generally come with low entry valuations due to a high-risk profile of projects. Finally, there is limited (but expanding) access to alternative forms of finance such as leasing, factoring, and seller finance. Under the federal project on SME development, a range of financial products have been developed to address some of these constraints. These include subsidized lines of credit and guarantees in addition to the expansion of leasing and technical assistance for some SMEs to make an initial public offering.

Targeted matchmaking events and information resources, including a nation-wide supplier database, and a database of the demands of MNC affiliates.

One of the points of the survey, where respondents nearly unanimously expressed interest, is matchmaking initiatives. As one of matchmaking instruments with good international record of accomplishment, a nation-wide supplier database was widely supported. In addition, most of the respondents among SMEs mentioned the lack of information on the demands of MNCs in locally produced material inputs. Various databases have been set up in Russia, including a large database with more than 6,000 SMEs operated by the MCP Corporation, but this experience has shown that the majority of suppliers are relatively inactive on the database while potential buyers may be reluctant to provide many details on their specific needs as this is often commercially sensitive information. Nonetheless, given the strong interest in this product from potential buyers and sellers, more experimentation should be done to find a way to share this information and to make existing databases a more valuable tool to participants.

In terms of matchmaking events, respondents highlighted the need for strong targeting of such events to avoid a mismatch in participants.

Training and methodological support for SMEs, regional governments and business development institutions

The surveys done for this analysis have shown that SMEs, as well as the regional business support institutions, lack knowledge and experience in the area of FDI linkages. Specialized knowledge exists at the federal level, particularly within the MCP Corporation, but there is no dedicated training program to help build the capacity of regional officials to support linkages initiatives. In addition to training for regional officials, many countries have adopted guides and training materials aimed at SMEs to help raise their understanding and capacity to supply MNC affiliates.

2.2 Implement targeted information campaigns to raise awareness of MNCs and local suppliers of the contents and benefits of FDI linkages support programs.

The survey has shown that the level of awareness of private businesses of the state support system for FDI linkages varies from middle to low depending on instruments / programs. While many SMEs or FDI

companies that have previous experience participating in state programs are generally aware of linkages support, this excludes a high number of potential firms on both the supply and demand side. It is therefore recommended to analyze more precisely the reasons for the mismatch between existing outreach and informational activities and the actual awareness of these programs and then to design targeted approaches to fill the gaps in awareness. These approaches may involve forming expanded partnerships with business or sectoral associations, experimenting with new dissemination channels and formats, and greater targeting in informational activities.

2.3 Ensure a robust M&E system is put in place to allow for impact evaluation and real time adjustment to linkages programs.

A proper M&E system is critical to the ability of policymakers to evaluate the efficiency and impact of public spending programs as well as to enable continuous learning in implementing agencies and the revision of programs in real time based on this learning. There is a wealth of international experience in KPIs and broader M&E indicators specific to FDI localization programs that could complement Russia's existing KPIs which are largely output and outcome oriented. It may also be possible to consider impact evaluation work as part of the M&E plan for linkages initiatives. Such evaluations could be used to determine how engaging in linkages impacts the supplier firm's operations through metrics such as profitability and productivity.

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Annex 1. International experience in designing FDI linkage programs – selected cases

Singapore – from trading post to global innovation center

The economic progress of Singapore has been heavily driven by FDI inflows, enabling the country to evolve into a regional headquarter hub for MNCs today. FDI, coupled with investments through government-linked corporations (GLCs), underpin Singapore's open, heavily trade-dependent economy facilitated by strong government commitment to maintaining a free market and active management of Singapore's economic development.⁶⁸ The Singapore government has actively encouraged FDI inflows and facilitated the attraction of export-oriented FDI in strategic industries, supported by the Economic Development Board (EDB) - the country's chief investment promotion and economic planning agency. Although manufacturing remains a key industry for Singapore, accounting for 20-25 percent of GDP, policies focused on a twin-approach to develop a world-class manufacturing and services industry. In addition to its industry clusters, Singapore has advanced to the lead aviation hub in Asia-Pacific and due to its strategic location established a global logistics hub in recent years.

Singapore is a case of highly successful industrial development and economic transformation. It was the first among the Southeast Asian countries to promote export-led growth but – faced with rising competition from other exporters with lower wage rates - decided to transition from exports dependent on cheap labor into a knowledge economy based on skilled labor and higher value-added exports already by the late 1980s. Over the last three decades, Singapore continuously upgraded its industrial structure and achieved high-income status.⁶⁹ Given the small geographic size and population, the government actively encouraged local and multinational companies to upgrade their Singapore-based operation to higher-end activities (configuration and design activities) that make use of its specific set of competencies, including regional headquarter functions, while creating economic space beyond Singapore by taking resource-intensive operations to countries in the region (China, India, Indonesia, Philippines, Vietnam). The rapid transformation demanded increasingly higher-level human resources and entrepreneurs which was a key factor to absorb new technologies. This was in line with development strategies' focus on "learning to learn" which is critical in an era of fast-changing technologies in which specific knowledge learned at one moment risks being outdated and obsolete in the next.⁷⁰

Singapore's economic structure has significantly diversified over the years. Targeted investment promotion was an important driver. Focused on efficiency-seeking FDI, i.e. the type of investment that leverages the host country's competitive factors to enable the investment to export elsewhere, it carefully selected MNCs to fit the target sectors and value chains. Singapore's key competitive factors today include an efficient and skilled labor force, access to international markets due to its favorable location, connectivity and domestic infrastructure, preferential trade agreements, and the country's sound and open investment climate. Not least due to the lack of land and limited manpower, Singapore's focus quickly shifted from labor-intensive manufacturing to higher value-added areas and skills-intensive activities. International businesses are also encouraged to establish R&D facilities in the country, and to use it as a location for international or regional headquarters.⁷¹ About half of the 7,000 MNCs based in Singapore now have regional operations that they manage out of Singapore.

⁶⁸ Menon, Ravi (2015), "An Economic History of Singapore: 1965-2065", a keynote address at the Singapore Economic Review Conference, 25 August 2015.

⁶⁹ Stiglitz and Norman (2015)

⁷⁰ Hosono in Stiglitz and Norman (2015)

⁷¹ UNCTAD (2011)

While Singapore had traditionally relied on MNCs and GLCs⁷² as drivers for growth, the large presence of FDI also generated strong demand for competitive local partners. Upgrading the capabilities of the domestic supply-side has thus gained increasing importance. Following the sharp downturn in the global electronics industry and sluggish regional and global growth, the economy experienced an acute economic downturn in 2001. The vulnerability to external shocks was a wake-up call to proactively foster diversification and to ensure that local SMEs had the necessary absorptive capacity to create and benefit from supplier linkages with MNCs. Key government committees started to identify SMEs role in driving productivity growth.⁷³

Supplier linkages initiatives are managed collaboratively by three key public agencies all reporting to the same ministry. The delivery model of Singapore's supplier development strategy is heavily centralized within its economic agencies under the Ministry of Trade and Industry, namely the Economic Development Board (EDB) - as the national agency to lead Singapore's industrialization including the FDI policy agenda, SPRING - the SME development agency, and International Enterprise Singapore (IE Singapore) - the export promotion agency. This in turn facilitated a strategy of coordinated policy measure and a concentration of administrative responsibilities and resources.

Singapore's supplier development focus has been an integral part of economic diversification strategies. It reflects the government's recognition of the role of FDI linkages in fostering overall economic competitiveness through productivity growth and the internationalization of Singapore companies. Since the domestic market is small, the presence of internationally successful businesses which have sophisticated demand and serve the global market out of Singapore has been a key foundation. By linking to these foreign affiliates and GLCs, SMEs built export capabilities and established a track record for their international competitiveness. Thus, promoting FDI linkages not only facilitated attracting and embedding FDI, but also served the government's long-term vision of developing globally competitive local companies and taking them abroad.

The Local Industry Upgrading Program (LIUP) was the first linkages program. Introduced by the EDB in 1986, it targeted the transfer of technology, marketing and business process know-how from MNCs to Singaporean firms, with a view for them to become subcontractors and suppliers to foreign MNCs operating in Singapore. Local firms were also encouraged to follow their buyers to other affiliate locations, thereby establishing an international footprint. Around 70 per cent of partnerships forged were concentrated in the electronics industry, which had been prioritized by the government. These early interventions ensured that local SMEs had the necessary absorptive capacity to create and benefit from supplier linkages with MNCs.⁷⁴

LIUP's main approach was to encourage MNCs to "adopt" SMEs in their value chains, encouraged through government support to both parties. Although LIUP evolved through several changes in emphasis, its core strategy remained. The relationship between MNCs and SMEs was envisaged to gradually upgrade with public support being available for three progressive stages. At first stage, local SMEs with the capacity and willingness to take up contracting opportunities identified by EDB are assisted to acquire the necessary skills and technology. At the same time, MNCs were encouraged to support the scheme by seconding an employee to the SME to act as a LIUP manager who was responsible for assisting SMEs to meet the performance and delivery requirements of the MNC. The secondee's salary was paid by EDB, which covered either a full-or part time appointment for one or two years. In the second stage, new products and processes were to be transferred to the SME. The third stage envisioned joint research and product development with MNC partners. This three-stage support ensures that the program is flexible enough to meet the specific needs of the MNC and their suppliers, while evolving in ambition.⁷⁵

⁷² Government-linked companies

⁷³ Summarized from reports by the Economic Review Committee (ERC) 2002, and the Economic Strategy Committee (ESC), 2010.

⁷⁴ EDB (1994)

⁷⁵ WBG interview with representative of EDB's Supplier Development team (August 2017)

The LIUP succeeded in increasing the productivity of SMEs and in facilitating the development of new relations but underperformed in transferring new capabilities to SMEs. By the mid-1990s, evaluation of the LIUP found that suppliers in the early years of partnerships with large firms improved productivity by 17 per cent on average, while value added per worker rose by 14 per cent. By 1999, the LIUP included 670 local SMEs as well as 30 MNCs and 11 large local organizations (mainly government-owned or government-linked companies) on the buyer side.⁷⁶ Besides establishing new supplier relations and improving efficiency of the production SMEs were already undertaking, LIUP's contribution to the upgrading of SME's technical capabilities remained below expectations. In practice, MNCs' assistance rarely exceeded learning facilitation, exposing selected suppliers to their quality management and production practices and sometimes offering training and management support but did not entail a real transfer of expertise as originally envisaged. Thus, the ultimate target to facilitate joint R&D was not met.⁷⁷ Furthermore, local firms raised concerns over the sustainability of the relationships established since the localization of inputs was less of a priority in an increasingly costly and resource-constraint economy.

Consequently, a new initiative, the Partnerships for Capability Transformation (PACT), was introduced in 2010 to support SMEs throughout their life-cycle. This was in line with intensifying pressure to diversify the economy and to compete on quality and innovation. PACT therefore promotes targeted productivity improvement of existing suppliers in the short term, encourages the localization of existing product lines through supplier upgrading in the medium term, and provides incentives for new product introduction in the long term through investing in, and supporting SMEs' innovation. Participating SMEs go through different stages of product development from the ideation stage to pilot runs with the support of the MNC. Implemented jointly by SPRING and EDB as focal points for both parties, PACT works with large organizations (MNCs and large local companies) to identify and implement collaborative projects between them and local SMEs in areas of knowledge transfer, capability upgrading, and the development and test-bedding of innovative solutions. Just like the LIUP, PACT operates on a cost sharing basis. SMEs whose projects are approved are eligible for up to 70 per cent funding support for qualifying development costs.

As such, PACT is regarded as an effective tool to deepen FDI linkages in Singapore. Between 2013 and 2016, 1 024 SMEs were reported to be involved in 147 PACT projects. It represents a significant evolution from the LIUP approach. While the LIUP focused on enhancing efficiency and reliability in products and processes that SMEs were already doing, PACT's overarching aim is to improve productivity, quality, and range of products and services delivered by SMEs. Hence, PACT is moving towards greater support for Singapore's SMEs in a more diverse range of sectors, including medical technologies, aerospace engineering, oil and gas, e-commerce and complex equipment, while LIUP predominantly benefitted manufacturing companies. As part of an ecosystem of new policies and incentives established to promote SME innovation, PACT is complemented by Singapore's science and technology agencies that provide support to SMEs through the Research, Innovation and Enterprise (RIE) masterplan. The RIE allows private companies to work with public research institutions to create new products and services, improve processes, facilitate partnerships with lead enterprises to co-develop innovative technologies, and provide a platform for Singapore-based companies to testbed and commercialize their innovations overseas through the Overseas Living Labs (OLLs).⁷⁸

⁷⁶ Perry (2012)

⁷⁷ Perry (1998)

⁷⁸ Information provided by EDB in presentation delivered at the Investment Policy Forum in Singapore in May 2017

Table 6. Overview of Singapore' grant program for FDI linkages (authors, adapted Enterprise Singapore, UNCTAD 2011)

	Objective	Key aspects	Incentives
Local Industry Upgrading Program (LIUP)	<ul style="list-style-type: none"> To upgrade, strengthen and expand the pool of local suppliers to foreign affiliates, by enhancing their efficiency, reliability, and international competitiveness Supports local suppliers to upgrade through collaborations with MNCs and to expand their activities abroad 	<p>Implemented in 3 phases:</p> <ul style="list-style-type: none"> <i>Phase 1:</i> improvement of overall operational efficiency, such as production planning and inventory control, plant lay out, financial and management control techniques <i>Phase 2:</i> introduction and transfer of new products or processes to local enterprises <i>Phase 3:</i> joint product, process research and development with foreign affiliates' partners 	<ul style="list-style-type: none"> Variety of organizational and financial support measure for upgrading vendor relationships (e.g. contribution to salary of foreign affiliate representatives seconded to local suppliers)
Partnerships for Capability transformation (PACT)⁷⁹	<ul style="list-style-type: none"> Encourages collaborations between a lead enterprise and other firm(s) based in Singapore to drive projects beyond regular commercial activities (e.g. selling products to partner firm) Lead enterprise must be registered in Singapore and can be a MNC or Singapore company though the majority of project partners shall be Singapore firms Lead enterprise needs to have clear capabilities above those of other partners in the project and takes responsibility for implementation and successful delivery of the project 	<p>Projects may relate to</p> <ul style="list-style-type: none"> <i>capability development:</i> lead enterprise (i) helps existing or new suppliers upgrade their technology to improve quality of supply chain, (ii) helps to co-develop and test-bed an innovative product from its supplier, (iii) develops a coaching program to improve cashflow management skills <i>business development:</i> lead enterprise (i) forms alliance with smaller firms to jointly pursue new international projects, (ii) pools common resources with smaller firms to achieve economies of scale 	<ul style="list-style-type: none"> SMEs supported with up to 70% of qualifying costs non-SMEs supported up to 50% of qualifying cost

⁷⁹ Enterprise Singapore (<https://www.enterprisesg.gov.sg/financial-assistance/grants/for-partners/pact-programme/overview>), accessed June 2019

Matchmaking efforts concentrate on forging technology partnerships and internationalization of SMEs. Singapore, mostly through EDB and IE, helps FDI search for and identify suitable local suppliers. For instance, local precision engineering companies are listed in supplier directories that are provided to foreign companies in the machinery, aerospace, oil & gas and medical technology sectors. These directories enable the foreign-owned firms to easily identify local suppliers should they wish to source locally. Focusing on international expansion, IE Singapore as part of its export promotion mandate, links local companies with trade specialists based in the export market to provide market intelligence and identify potential agents, distributors and customers of their products or services. In addition, Singapore SMEs looking for overseas business contacts can access a global database of 64 million verified contacts from 7 million organizations across 145 countries through a proprietary platform (“Leadbook”). It aids in lead generation by finding potential customers by profiling the global audience with meta-tags and attributes like geography, designation, industry, size, job titles and contact email addresses.⁸⁰

The focus on technology upgrading is maintained for matchmaking initiatives. Besides the available grants and program in this space, such as the Technology Adoption Program (TAP), there are also dedicated platforms and organizations created to facilitate and encourage SMEs to pursue technology innovation and upgrading. The Intellectual Property Intermediary (IPI), for example, under the Ministry of Trade and Industry, focuses on industry needs. It translates industry's innovation objectives into specific technology requirements and helps SMEs navigate the complex R&D landscape. Through IPI, SMEs are matched with the right technology partner and enabled to develop new processes, products and services. IPI further supports other government agencies like SPRING or International Enterprise Singapore in establishing innovation clusters for new technologies such as robotics and advanced analytics. In addition, it enhances its online virtual marketplace, making it easier for local enterprises and SMEs to access IPI's technologies and innovations.⁸¹

Investment incentives played a key role in shaping the pace and direction of industrial development. Financial and tax incentives were used both for the promotion of new investments in industries and services, for encouraging existing companies to upgrade through mechanization and automation, and through the introduction of new products and services. Under the Pioneer Certificate Incentive and Development and Expansion Incentive, Singapore encourages foreign MNCs to set up local upstream and downstream activities that are more typically conducted at companies' headquarters. The incentive provided is a corporate tax exemption or a reduced concessionary tax rate on eligible income. Companies that apply for this incentive must commit to upgrading their employment and business investments. The program intends to foster technology transfers and the scaling-up of the local economy.

Since the supplier development programs were introduced, Singapore has grown an extensive network of competitive SME suppliers. Its effective supplier development strategy is underpinned by significant financial and consultancy support and facilitated by strong institutional coordination. PACT, for example, was allocated around SGD 300 million with another SGD 80 million added to enhance the program.⁸² According to a 2012 report by the Ministry of Trade and Industry, FDI in Singapore's manufacturing sector has led to productivity improvements in locally-owned manufacturing firms, especially in those clusters that have stronger vertical linkages with foreign-owned firms. It concludes that such productivity gains from backward integration are not surprising, as foreign-owned firms that set up local supplier networks would be more willing to share technological and organizational improvements with their local suppliers. Productivity improvements through linkages were positive and significant in all clusters, except for chemicals where the majority of upstream FDI firms purchase their intermediate inputs from crude oil abroad. The extent of backward linkages with local firms thus tends to be weaker in chemicals than is the case for all other clusters.⁸³

⁸⁰ WBG interview with EDB and IE in 2017.

⁸¹ IPI website (www.ipi-singapore.org), accessed June 2019

⁸² OECD-UNIDO (2019)

⁸³ Ministry of Trade and Industry (2012), Feature article on “Productivity Spillovers to Local Manufacturing Firms from FDI”

Malaysia – developing a cutting-edge electronics cluster

FDI has always played a central role in the development path of Malaysia – even though its specific development model changed over time. In pursuit of an export-oriented development model, the attraction of efficiency-seeking and export-manufacturing FDI, supported by targeted regional strategies, was promoted. Institutionally, the establishment of the Malaysian Industrial Development Authority (MIDA⁸⁴) in 1967, mandated to encourage industrial investment, in part by providing incentives and infrastructure to attract FDI, was a significant event. Reporting to the Ministry of International Trade and Industry (MITI), MIDA has functioned since then as a comprehensive and autonomous investment promotion agency. Regional governments were also active in FDI promotion through the provision of subsidized land, water, electricity and other physical and institutional infrastructure.

The promotion of FDI linkages has been an early policy goal. Ever before general SME development was prioritized in late 1990s, the government had some experience with policy measures to link foreign affiliates with local suppliers. Early initiatives such as the Vendor Development Program (VDP) introduced in 1988 had limited success, primarily due to the limited capacity of the selected local SMEs to meet the needs of MNCs. In its early version, only supplier owned by Bumiputera, the native ethnicity in Malaysia, were eligible to join. While a fair goal, it led to competitiveness criteria being pushed to second rank which had proven problematic when the supplied inputs revealed quality and pricing problems. As the program developed and ventured from automotive into the electronics sector, the eligibility criteria became less restrictive, underscoring the need to select companies with the capacity to produce high-quality products at a reasonable cost.⁸⁵

Learning from the origins of the VDP, subsequent linkage programs have yielded better results, as they incorporated a more demand-driven design and more support for supplier capacity-building linked to a merit-based selection. The Industrial Linkage Program (ILP) and the Global Supplier Program (GSP) both sought to give MNCs more of a role in supplier selection and have provided complementary support for SMEs to access finance, build their capabilities, and expand to new markets. Introduced in 1996, the ILP seeks to build linkages between MNCs and local firms by offering tax incentives to improve SME capabilities for those suppliers producing eligible products as well as for those MNCs incurring costs by helping the supplier to upgrade. As of 2007, 906 SMEs were registered under the ILP, of which 128 were linked to TNCs and other large companies. The GSP, created in 2000, funds training and skill development for SMEs to make them more effective participants in global supply chains. Subsidies are provided to SMEs for training programs offered by a variety of regional centers and institutes, such as the Penang Skills Development Centre (PSDC) described in more detail below. The key element for linkages promotion is that MNC representatives design the content of the specific training programs and participants are selected based on MNC criteria. Within its first year, the GSP had already trained 813 employees from 225 SMEs, with the involvement of 23 MNCs or large domestic companies. Intel, for instance, has made significant use of the PSDC and the GSP.⁸⁶

The effective use of tax and other incentives to foster FDI linkages and improve suppliers' skills has also proven effective in Malaysia. Under the ILP, for example, investors can claim tax deductions for costs involved in providing support to local suppliers, including training, product development and testing, and factory auditing to ensure local supplier quality. The GSP offer financial and organizational support to MNCs, if specialists from their foreign affiliate are seconded to local firm (for up to 2 years) for the purpose of local upgrading. These targeted tax incentive programs reduce the perceived risk for foreign investors when engaging in capacity building of local suppliers. Studies have shown that these programs have been effective in establishing linkages and boosting productivity in the SME sector. The programs in Malaysia have influenced Intel in its decision to develop local SMEs as suppliers. Intel is reported to have developed

⁸⁴ Since 2012, MIDA stands for “Malaysian Investment Development Authority”

⁸⁵ UNCTAD (2011), “Best Practices in Investment for Development: How to create and benefit from FDI-SME Linkages, Lessons from Malaysia and Singapore”, Geneva.

⁸⁶ Ibid.

a model for supporting supplier development and upgrading: potential suppliers are selected based on the quality of their management; human resources; technical, materials and process capabilities; and cost competitiveness. They are then provided with training and opportunities to supply the affiliate and, ultimately, the global Intel network. Intel estimates benefits amounting to USD 50 million per year from participating in these programs.⁸⁷

Table 7. Overview of specific policies and programs for FDI linkages (adapted from SME Information and Advisory Centre, UNCTAD 2011, OECD 2018)

	Objective	Key aspects	Incentives
Vendor Development Program (VDP)	<ul style="list-style-type: none"> Provide opportunities for SMEs to participate in subcontracting arrangements and other joint-venture related activities Develop and strengthen SME performance as manufacturers and suppliers of components, input materials, machinery, parts and supporting services to large corporations and MNCs 	<ul style="list-style-type: none"> Vendors supply components and spare parts to the anchor companies operating in Malaysia In return, the anchor companies are directly involved in the development of the SME, particularly through technology transfer and by providing a stable market Such long-term contracts should enable the vendors to grow into large corporations and penetrate the international market 	<p>Incentives for SMEs:</p> <ul style="list-style-type: none"> The anchor company provides a market for the SME's products and technical facilities and support in the area of training and quality improvement The government provides soft loans and other types of financial support
Industrial Linkage Program (ILP)	Develop domestic SMEs into competitive manufacturers and suppliers of parts and components and related services to MNCs and large companies	<p>Matching services supported and enhanced by SMIDEC's existing financial schemes and developmental programs</p>	<p>Incentives for SMEs:</p> <ul style="list-style-type: none"> Pioneer Status with tax exemption of 100% on statutory income for 5 years and Investment Tax Allowance of 60% on qualifying capital expenditure incurred within a period of 5 years provided to eligible SMEs To qualify, SMEs must manufacture products or undertake activities in the List of Promoted Activities and Products in the ILP. They should also be supplying to MNCs or large companies

⁸⁷ Christiansen and Thomsen (2005), "Encouraging linkages between small and medium-sized companies and multinational enterprises", Background paper by the OECD Secretariat in OECD (2018), "OECD Investment Policy Reviews: Southeast Asia 2018", Paris.

Global Supplier Program (GSP)	<p>Develop SMEs into competitive suppliers of parts and components, not only to MNCs in Malaysia, but also their worldwide operations through the mentoring activities and the linkage initiative of the GSP</p> <ul style="list-style-type: none"> • Involves training in critical skills where MNC provide inputs to curriculum and SME selection criteria • The training initiative is implemented in collaboration with local Skills Development Centers (e.g. Penang Skills Development Centre) 	<p>Incentives for MNCs: Expenses incurred in developing SMEs such as training, product development and testing, factory auditing and technical assistance to ensure the quality of vendors' products will be allowed as deduction in the computation of income tax</p> <p>Incentives for SMEs: SMEs that send their employees for courses at any of the training providers will be eligible for 80% training grant from SMIDEC. Remaining costs may be claimed through the Human Resource Development Fund</p> <p>Incentives for MNCs: Financial and organizational support to MNCs for seconding specialists to local firms for upgrading purposes</p>
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The case of the electronic and electrical sector development in the State of Penang is a case in point. The Penang Development Corporation (PDC), created in 1969, was effective at creating infrastructure and incentives tailored to particular MNCs. The State also acquired a strong reputation among investors for efficient institutions and effective government leadership. Penang today houses the offshore operations of MNCs such as Intel, Dell, Motorola, Sony, Agilent Technologies, Seagate, Jabil, Canon, Philips and NEC. The PDC and other regional development corporations, such as Selangor State Investment Centre (SSIC), continue to offer a variety of promotional services and incentives related to infrastructure, skills development and research and development (R&D).

The Penang Skills Development Centre (PSDC) is frequently referenced and studied⁸⁸ as a successful model for skills upgrading. Established in 1989, it was the first tripartite, industry-led skills training and education center in Malaysia. The PSDC initially concentrated on vocational training in electrical engineering and electronics, as part of the country's strategy to advance into the production of standardized components. Subsequently, it ventured into higher value-added products and components (semiconductor, IT, audio visual, digital camera sectors) and from 2000 onwards continued its upgrading path, adding life sciences, biotechnology, pharmaceuticals and medical devices to its focus activities. Since its inception, the PSDC has grown phenomenally to become the premier vocational learning institution in the country, dedicated to meet the immediate human resource needs of the business community in Penang and to support and strengthen the local skills base. Its management board continues to be staffed by MNC representatives to induce the demand-led focus into the training curricular. Over a period of 29 years, the Centre has trained over 200,000 participants through more than 10,000 courses, pioneered local industry development initiatives, assisted in the input and formulation of national policies pertaining

⁸⁸ E.g. UNCTAD 2011, OECD 2013, OECD-UNIDO 2019

to human capital development and thus contributed directly to the Malaysian workforce transformation initiatives.

At the same time Penang – and Malaysia overall – have produced one of the world's more successful records in generating backward linkages and supply chains within the host economy, from complex packaging to a broad array of contract engineering services. Hence, the PSDC has attained both national and international recognition as a truly successful example of shared learning and a model institution for human resource development to be emulated within and beyond Malaysia.⁸⁹

The virtuous cycle that the Penang success story created for Malaysia illustrates the importance of involving the private sector, university, and vocational training in carrying out an effective FDI linkages program. The PSDC organizes its curriculum around the specific needs and gaps identified by foreign multinationals in the booming regional electronics complex. To ensure that its vocational training programs stayed abreast with the FDI promotion efforts and disruptive industry trends on the one hand and to facilitate spillovers to the academic sector on the other hand, the PSDC created several partnerships with renowned universities in Malaysia, Australia, Germany and the UK.⁹⁰ The Micro-Electronics Centre of Excellence at Universiti Sains Malaysia, for example, is such a partnership which relies on support from international corporations for specialization in mechanical engineering (e.g. robotics, micro- and nano-assembly), chemical engineering (e.g. gasses and chemical delivery techniques), materials sciences (e.g. packing R&D), and supply chain management. More recently, Universiti Sains Malaysia has begun to cultivate similar government-industry-academic partnerships in the pharmaceutical and nutraceutical sectors.⁹¹ In line with its commitment to facilitate industry growth and development, the PSDC executed its Industry 4.0 initiative in 2016, a strategy that supports the new phase of industrial revolution in Malaysia. Moving forward, the PSDC will expand its role and gear towards becoming the Centre of Excellence for Industry 4.0 in Malaysia by providing leadership, the right platform for learning of best practices, as well as talent development support through its high-end shared services facilities (such as state-of-the-art testing facilities) to meet the current needs and demands of the industry.⁹²

Thailand - rise towards Southeast Asia's automotive hub

A long-standing policy focus on FDI attraction and linkages has enabled Thailand to become Southeast Asia's largest car manufacturer. From the 1960s onwards, the government facilitated the formation of industrial clusters by establishing the necessary infrastructure for manufacturing activities, especially automatable assembly and parts production. Car manufacturers enhanced their competitiveness when they were agglomerated as a cluster with articulated value chains.⁹³ The Thai automotive industry experienced different phases of development, from the introduction of the localization policy (1971-1977), strengthening of localization capacity (1978-1990), to liberalization (1991-1999).⁹⁴ By initially focusing on component manufacturing rather than the 'national car' project approach (as neighboring Malaysia), Thailand was able to attract increasing amounts of foreign investment in the automotive sector based on offering supplier network capability, infrastructure, and investment incentive measures.

With WTO accession in 1995 and the subsequent phase-out of local content requirements, Thailand promoted FDI linkages to embed its firms in the supply chains of foreign affiliates. Compared to other ASEAN members, the Thai approach realized that integrating SME development in the policy mix is crucial to capturing linkages dividends. Effectiveness of these programs further required a strong political and financial commitment that has not been observed in many ASEAN countries so far. Thailand, similar to Malaysia, has succeeded in complementing FDI attraction with policies that support skills and cluster

⁸⁹ OECD-UNIDO 2019

⁹⁰ <http://www.psdc.org.my> (accessed 8 June 2019)

⁹¹ OECD 2013

⁹² <http://www.psdc.org.my> (accessed 8 June 2019)

⁹³ Stiglitz and Norman (2015)

⁹⁴ Natsuda and Thoburn (2013)

development in order to capture the desired spillover effects on Thai SMEs. Today, both countries show high levels of domestic sourcing reflecting advanced local supplier capacities. In key sectors such as automotive, machinery and equipment, and electronics, foreign lead firms that established a few decades ago were followed by foreign multinational suppliers to also produce in Malaysia and Thailand. As the industries grew, local producers developed.⁹⁵

These developments gave rise to the New Automobile Investment Policy in 2002. It aimed to develop Thailand into a regional center of the automotive industry in Southeast Asia, the '*Detroit of Asia*'. proclaiming pick-up trucks and related component manufacture as its first 'product champion'. In 2007, Thailand introduced the 'Eco-car' program as the second product champion element, supported mainly by tax incentives, which attracted a number of hybrid and electric vehicle production investment from Japanese firms as well as Volkswagen and Tata Motors.⁹⁶.

In pursuit of this vision, the FDI incentives schemes was adapted to encourage foreign OEM investors to relocate together with their key suppliers to Thailand. When an automotive OEM applied for a new auto-assembly project together with accompanying suppliers, the investment benefits granted to the OEM would also be extended to the supplying companies being part of one large project. Previously, suppliers had been unable to realize benefits such as import duty and corporate tax exemptions since the investment threshold was too high for auto component producers at lower supply tiers which require relatively smaller investments (as it used to focus on OEMs). This change in policy has resulted in a high number of Japanese entrants at tier 2- and tier 3-level which further broadened the base of the automotive industry in Thailand and increased its competitiveness.⁹⁷

Simultaneously, measures to upgrade the local supply capacity were introduced. The government issued the Supporting Industry Master Plan in 1995 and, at the same time of the new investment policy, programs to strengthen domestic SMEs⁹⁸ and workforce. It realized that with the abolishment of local content enforcement, the active promotion of supporting industries to key manufacturing sectors was an important source of industrial competitiveness. Supporting industries – a term often used in the Asian context - are commonly understood as a group of industries to supply manufactured inputs, mostly intermediate goods. In the supply chain, they usually concern tier-2 and -3 segments covering a broad range of product groups (plastics, metal, rubber, parts), steps in the production process (pressing, casting, forging, molding, machining, plating) and include production services such as logistics, storing, distribution and insurance. Together they form an important industrial foundation and can supply several sectors relevant for Thailand (e.g. automotive, electric and electronic equipment sectors).⁹⁹

The Supporting Industry Master Plan was the first comprehensive policy that addressed the promotion of FDI linkages. It provided key policy guidance for the development of Thai supporting industries in the automotive and electric and electronics sectors focusing on measures that can be broadly grouped along the four strategic pillars outlined in the introduction (see figure 46):

- 1) *Attract* - To close the gap between buyers and suppliers, this intervention focused on attracting investment of foreign suppliers and on promoting technical collaboration with foreign companies.
- 2) *Connect* – To establish the link between suppliers and buyers, the provision of information and matchmaking services was targeted. Furthermore, the government mediated financial support services to assist the creation of linkages.
- 3) *Upgrade* – To overcome the skills and technology gap impeding linkages, this intervention provided support to upgrade technology and production methods, human resources and management skills.

⁹⁵ OECD-UNIDO (2019)

⁹⁶ Natsuda and Thoburn (2013)

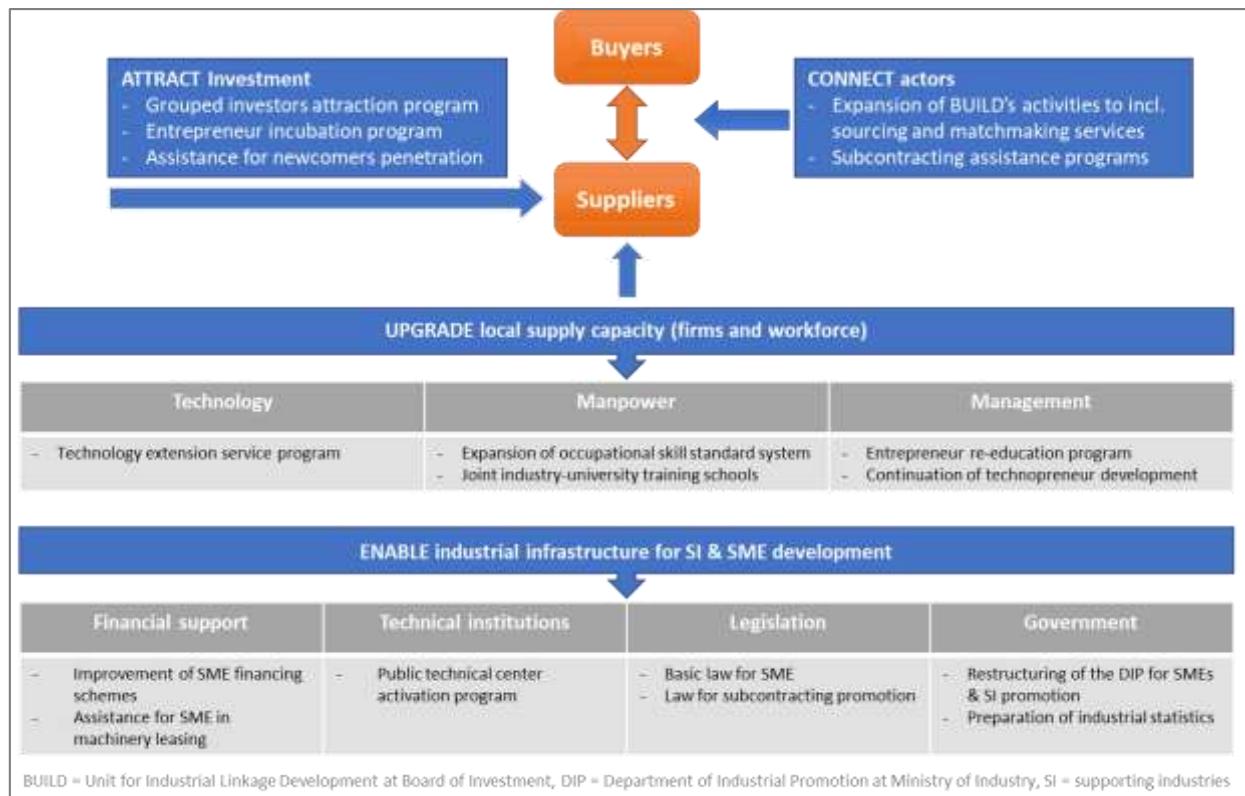
⁹⁷ Japan Ministry of Economy, Trade and Industry (2016), p. 43

⁹⁸ In particular, the SME Promotion Act 2000 and the first SME Master Plan 2003.

⁹⁹ Mori (2006)

- 4) *Enable* – To provide an enabling business infrastructure, the government updated policies and legislation, established financial support schemes and public technical institutions to foster industrial testing and R&D.

Figure 46: Thai Master Plan for the Development of Supporting Industry (Source: authors, adapted from Ohno 2016)



In Thailand, linkages promotion was coordinated through a network of strategic stakeholders. The Board of Investment (BOI) and the Ministry of Industry (MOI) are the key official actors responsible for linkages promotion. They share the space with private sector associations, such as the Alliance of Supporting Industries Association (ASIA), and other academic institutions and non-profit organizations to maintain the direct dialogue with business and include those organizations providing technical support and business consulting. The BOI and MOI coordinate initiatives in a flexible and rather informal manner. Together with the external stakeholders, this approach results in a network that is neither dominated by a single organization nor governed by explicit rules. While every network member performs its functions separately, they refer customers to each other and share program implementation in areas where other members are better equipped to fulfill required functions.¹⁰⁰

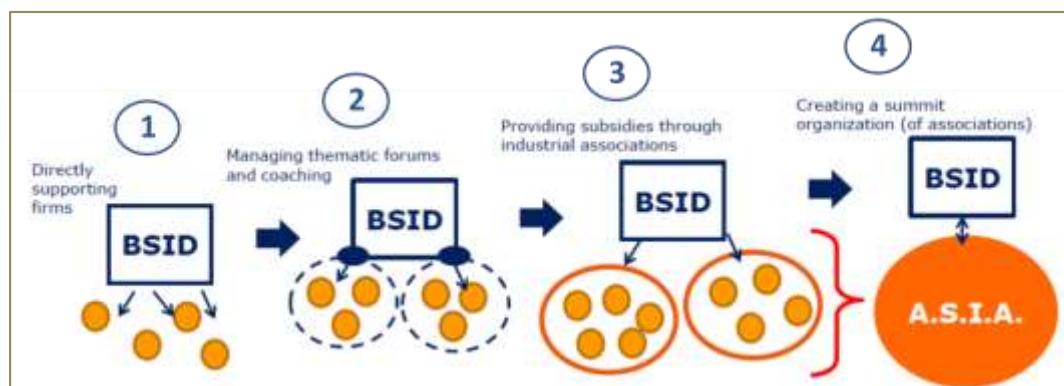
The BOI, the national investment promotion agency, is the first contact point for foreign investors and mandated to attract and link FDI strategically. It is thus well placed to follow up on investors' inquiries to identify suitable suppliers and houses the Unit for Industrial Linkages Development (BUILD) for this purpose. BUILD offers the following services: (i) tailored sourcing and matchmaking services on demand, received through various channels such as national one-stop-shop or BOI's overseas offices, (ii) organizing subcontracting exhibitions and industry fairs, (iii) hosting and managing the ASEAN Supporting Industry Database to enhance sourcing from beyond Thailand, and (iv) providing various business linkages support services to connect the supply chains of part and component manufacturers (incl. plant visits, firm participation in overseas trade shows, industrial exhibition space, seminars).¹⁰¹

¹⁰⁰ Punyasavatsut (2008)

¹⁰¹ GRIPS Development Forum (2015) and BOI website (www.boi.go.th)

The Department of Industrial Promotion (DIP) at MOI was responsible for developing the local capacity required for FDI linkages promotion. In charge of industrial policy design, implementation and monitoring, it coordinates capacity building and upgrading initiatives directly and indirectly through various bodies, including sector-specific institutions, industry associations, industrial real estate and infrastructure entities. The most prominent, the Bureau of Supporting Industries Development (BSID), was originally tasked to increase the local productive capacity by providing technical and managerial support to firms in supporting industries. Over time it was assisted by the Bureau of Service Provider Development (BSPD) which in turn was responsible for developing management and technical consultants to provide the necessary services and training for establishing a competitive industrial eco-system in Thailand. Figure 2 shows the significant evolution of BSID's service delivery and structure due to increased capacity and size of the business support ecosystem in Thailand.

Figure 47: BSID's gradual approach to SI development (Source: Ohno 2016)



BSID evolved from direct firm support to an umbrella for business associations. At the beginning with a small number of SI firms, BSID provided direct technical and managerial support to individual companies. With support from foreign donors, it further trained a cohort of private consultants to help deliver this support to Thai firms (Phase 1). As the number of SI firms grew, BSID set up and coordinated thematic forums that were structured around specific activities or materials (e.g. design, machinery, foundry, metal, etc.) and acted as a secretariat and coach to these forums (Phase 2). As the forums gradually gained experience and the number of private consultants able to advise SI grew, they detached from BSID and transformed into privately-run industrial associations. BSID then shifted its role from direct support to providing subsidies to associations (Phase 3). Lastly, the Alliance of Supporting Industry Associations (ASIA) was created as an umbrella organization which consists of 12 privately-run industrial associations. BSID now concentrates on policy-making, project-piloting and anticipated needs of emerging industries (Phase 4).¹⁰²

Implemented by four lead FDI firms, the Automotive Human Resource Development Program (AHRDP) was a successful example of an industry-led initiative to upgrade the industrial workforce. Realizing that Thailand had not enough adequately skilled people to cover the needs of the fast-growing automotive sector, Honda, Denso, Nissan, and Toyota, together with support from Japan, joined forces with the Thai government. They established AHRDP to improve the quality, cost, and delivery performance of 100% locally owned suppliers through human resource development via training of trainers. Each of the OEMs designed and delivered specific modules based on their core expertise and needs, while Japan (JETRO, JICA) provided company experts and equipment and the Thai government covered all other running costs. The AHRDP was managed by a Steering Committee and Coordinator Group which provided a useful platform for parties directly involved as well as external stakeholders. After its first two 2-year-cycles, the program delivered 132 examiners, 318 trainers, as well as 7,151 trained staff and developed 233 SMEs per Toyota's production system.¹⁰³

¹⁰² Techakanont (2011)

¹⁰³ Thai Automotive Institute (2013)

As the recent revision of its incentive regime shows Thailand maintains focus on FDI linkages today.. Against the backdrop of decreasing investment inflows compared to neighboring and peer countries and needs to upgrade its position in GVCs, the government revised its investment strategy in 2015. To better align FDI and national policy goals, it refocused its FDI promotion efforts away from lower-end manufacturing activities towards targeting higher value-added segments of international production networks. The new strategy constituted a major shift in Thai investment policy as it moved from a system of location-based incentives, which granted different amounts of incentives depending on economic zones, to a combination of activity-based (knowledge-intense, value-added, high technology content, etc.) and merit-based (fostering competitiveness, decentralization, industrial development, etc.) incentive regime. The new plan promotes investments enhancing national competitiveness through R&D, innovation, and value creation as well as environment-friendly activities and includes the promotion of SME linkages and skills.¹⁰⁴

Czech Republic – an upgrading journey to compete in the European market

The Czech Republic had been one of the most successful locations in attracting FDI after the fall of communism in the 1990s. Its skilled labor, stable business and political environment, strategic location in Central Europe and attractive investment incentives had resulted in substantial amounts of FDI. However, relatively few benefits of this FDI were felt in the local economy. MNCs drew little of their inputs from Czech suppliers and local content figures stagnated at very low levels, even in sectors where the Czech Republic had relatively strong skills and traditions, such as automotive and electronics. An effective mechanism was required to widen FDI benefits to the local economy. There was a need to strengthen local suppliers' capacities so that they would have the capacity to cope with EU single market forces in the near future and succeed in becoming internationally competitive following enterprises' isolation from world markets and comparative advantages under central planning.

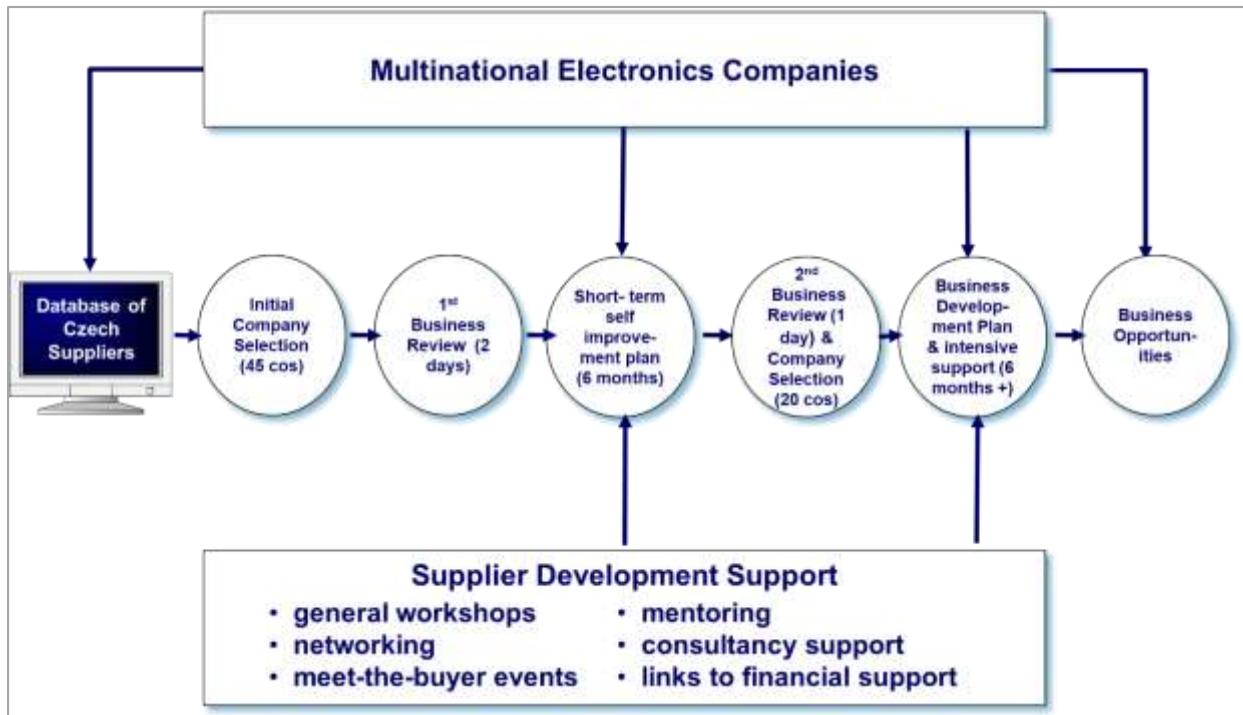
In response to this challenge, the Czech government took a more proactive approach and piloted a National Supplier Development Program in 2000-2002. In cooperation with the European Union and the World Bank Group, a backward linkage promotion program was designed for the Czech electronics sector, the fastest growing sector at the time. It focused on strengthening the linkages between MNCs and Czech firms around components (semiconductors, printed circuit boards, cable harnesses), engineering supplies, and other packaging materials, automation, R&D and software. CzechInvest, the national investment promotion agency under the Ministry of Industry and Trade, implemented the supplier development program (SDP).

Starting from the demand of MNCs, improving the competitiveness of Czech SMEs to meet this demand was at the core of the program. The pilot adopted a phased approach over two years. The key objectives of the SDP were two-fold: (i) Czech suppliers to obtain more business from MNCs, increasing both volume and value-added ; (ii) develop a local world class supplier base which would help retain existing inward investors and attract new ones. Collecting the supply needs of MNCs showed that Czech suppliers had to enhance their competitiveness, developing new skills and changing their way of conducting business to meet the MNC requirements. Thus, the program was working directly with suppliers to realize these enhancements. A secondary objective was to train a group of staff at CzechInvest so they had the knowledge and ability to run and expand the program beyond 2002. This was important to ensure sustainability get the right capacity ready to keep on improving Czech suppliers beyond the initial EU-funded program. Therefore, two external consultants were seconded to work full-time alongside CzechInvest's team. To ensure focus on demand , MNCs have been involved from the beginning of the program.¹⁰⁵

¹⁰⁴ World Bank Group (2016)

¹⁰⁵ Martin (2014)

Figure 48: Key steps in the Czech SDP Delivery Model (Source: WBG, 2008)



MNCs guided the program through participation in the High-Level Advisory Group. This Group oversaw the overall strategy and focus of the program and brought together representatives of government, general managers of MNCs, presidents of business associations and managers from CzechInvest. To establish the necessary clout, only decision-makers with seniority were invited to the group which met twice a year. The meetings served as a discussion forum, ensuring the highest possible political support for the project and mutual understanding of the performance gaps suppliers needed to tackle. 18 major MNCs in electronics, including automotive electronics, were invited to take part in the program, which required them to share their local sourcing needs as well as the minimum requirements suppliers had to meet to become 'qualified suppliers' for the MNC's supply chains. Moreover, MNCs were asked to identify priority areas for improvement of Czech suppliers, nominate suppliers to the program, and participate in the seminars provided to suppliers. The elementary requirements demanded by MNCs were the following: quality certification, competitive price, reliability of deliveries, technical capacity, flexibility and innovative capacity. Despite this, the most important improvement areas identified by MNCs were rather related to soft-skills, i.e. strategic business focus, presentation skills, and customer service.¹⁰⁶

Only those Czech companies with the highest potential to become long-term suppliers were selected. Out of the 200 applications, 45 suppliers were invited to participate in the pilot. The intention from the outset was to select companies with the greatest potential to meet MNC requirements, not on those that had the biggest need. Particular weight was therefore assigned to nominations sought from MNCs, but attention was also given to ensuring the sector and size balance of those selected and to including promising companies unknown to MNCs. The suppliers were selected based on a pre-defined set of criteria, including: (a) relevance of the industrial sector and needs of the multi-national; (b) registration in the Czech Republic; (c) financial stability and performance; (d) demonstrated commitment of company management; and (e) demonstrated quality, including ISO certification.¹⁰⁷

A rigorous process to select suppliers to participate in the program served a dual benefit. Ensuring a transparent selection process, avoided accusations of bias, and facilitated the selection of viable enterprises with potential for growth and strong interest and commitment to the program. The final

¹⁰⁶ WBG (2004)

¹⁰⁷ WBG (2017b)

sample included mainly dynamically growing companies, which had already been cooperating to varying degrees with multinational clients. However, as the competition continued to increase in the Czech market due to entry of foreign suppliers, they encountered problems in getting new orders for more sophisticated parts and components. Czech companies also struggled to diversify their portfolios of clients and reduce their dependency on a single large customer.¹⁰⁸

The initial two-day business review focused on drawing up a self-improvement plan to implement over 6 months. The European Foundation for Quality Management (EFQM) was applied as the quality management tool providing a framework for a whole-of-business assessment with which a MNC checklist was developed that focused in more detail on the key issues of importance to MNCs. It was thus not a simple audit in terms of a standard external analysis of a company, like a MNC would undertake in assessing a potential supplier, but a review of all aspects of the business in which external assessors acted as facilitators to help the company management review the way forward for their business. Besides identifying and prioritizing performance gaps, the first business reviews also aimed at securing the buy-in from company management and convincing them of the value of the process despite the significant commitment of management time. Management carried out a parallel self-assessment using a simplified version of the EFQM. The two assessments were brought together in an interactive workshop resulting in an agreed short-term action plan. The modalities of support for the implementation of the action plans included a series of workshops focusing on selected topics covering strategy and change management as well as operational efficiency.

To ensure the companies with the most potential to succeed where selected for the resource-intensive individual support, a competitive element was built in. At the end of the six months, a second round of business reviews was conducted. Based on its results, 20 firms were selected for the final stage which encompassed one-on-one business consulting, tailored to each company and delivered by a mentoring team pairing an EU expert and a Czech consultant, ensuring knowledge transfer and local expertise were matched. Mentors helped companies with the implementation of the business plans, identified areas for external consulting support and acted as contacts with banks of MNCs. Besides assessing the initial improvements realized, the key intention behind the second business reviews was to test the commitment and capability to make the necessary changes (as a proxy absorptive capacity) to succeed in becoming a long-term MNC supplier.¹⁰⁹

Access to finance and active matchmaking were added features throughout the intensive-support phase. The role of the mentors was established to also act as a contact between the Czech companies and other parties as necessary, including financial institutions. However, they mainly provided the crucial link with MNCs participating in the SDP, helping communication, and establishing working relationships so that ultimately, new supply chain linkages were formed.

An evaluation undertaken 18 months after the end of the pilot, confirmed the significant impact on participants' bottom line. A survey of all 45 companies participating in the pilot (with 42 responding) showed that 15 companies had gained new business which they attributed to the program. These contracts were worth \$46 million for the period 2000-3. Four companies had also found new customers abroad, and 3 companies had obtained contracts with a higher value-added content. The share of components sourced from Czech companies by the MNCs participating in the program correspondingly increased from a rate of 0-5% at the start, to 2.5-30% by 2004.

Following the success of the pilot, the government decided to replicate the program in 3 other sectors. It led to increased focus on local benefits of FDI in national policy making and CzechInvest played a key policy advocacy role. The supplier department team of CzechInvest had been very closely integrated with the pilot project and facilitated aftercare departments with the identification of suppliers for greenfield or expansion investors. Many of the activities conducted under the SDP continue to this day, such as

¹⁰⁸ WBG (2004)

¹⁰⁹ Martin (2014)

sector-level supplier databases, matching services, market screens, Supplier Days connecting businesses, etc. The program also informed the development of the follow on Czech national cluster policy at the time.

The program's strong emphasis on understanding and following MNC demand in promoting supplier linkages was critical for its success. One of the most significant reasons for why linkages between MNCs and SMEs were not manifesting to the expected degree was the lack of knowledge about potential demand or supply, and lack of trust between MNCs and Czech suppliers. MNCs' memberships in the High-Level Advisory Group and input in selecting potential suppliers helped to identify suppliers' skills gaps while at the same time ensuring MNCs that the program also bears their competitiveness in mind. It thus increased trust in working with each other and increased information. On the flip side, the prospect of MNC contracts, was a key motivating force for Czech SMEs to continue with the program. While many SMEs had good technological skills, the program helped them build their capabilities to be suppliers by upgrading their communication and management skills, such as business planning, which were lagging after years of working in a planned economy.¹¹⁰

An independent study confirmed long-term positive results. As part of the Enterprise Survey, a study was undertaken in 2014 which found multiple benefits accruing to suppliers of MNCs, reaching far beyond any direct support received from the MNC. It found that MNC suppliers (i) enjoyed a faster growth rate in sales, value added and employment, (ii) were more productive, (iii) noted a reputational effect of becoming a MNC supplier which made it easier to supply affiliates in other countries, as well as to enter the value chain of other MNCs, and (iii) improved creditworthiness of SMEs. In line with the SDP's goal to move suppliers up the value-added curve, almost half of the suppliers in the sample reported "that over time they increased the complexity and/or value added of the products they supply to MNCs operating in the country", and an even stronger effect of 60% was found among firms who supply MNCs operating domestically and MNCs located abroad. Controlling for specific inputs used, the value added of MNC suppliers was on average double that of a comparator non-supplier group. Lastly, it highlighted the strong market linkages aspect as a critical success factor for the SDP program.¹¹¹

Ireland – gradual economic transformation through FDI

Given the importance of MNCs for the Irish economy, their degree of integration into the local economy has always been a policy focus. Promoting forward and, particularly, strong backward linkages through customer and supplier relationships with local Irish companies has been regarded vital to determining MNCs long-term commitment to Ireland and the extent to which they contribute to the overall development of the manufacturing sector. As will be shown, Irish linkage policies have developed significantly in response to three factors: (i) the changing needs of MNCs (especially associated with increased globalization and technology advancements), (ii) the changing capacity and capability of local firms, and (iii) the change in the structures of government agencies involved in industrial and trade promotion.

Ireland attracted sizeable amounts of FDI after it adopted an outward-oriented strategy to spur growth and jobs. This change in policy included the use of fiscal and financial supports to incentivize export-oriented FDI to set up in Ireland. However, local sourcing was limited and consisted mostly of basic inputs with low added-value. Local suppliers could not meet the quantity and quality requirements of foreign investors, not least due to dis-economies of scale within a small local market and also because of weak technological capabilities. Moreover, the purchasing managers of MNCs were unwilling to risk buying from domestic firms with no record of producing and selling high-quality products. In order to increase domestic procurement, the government made several attempts to encourage stronger backward linkages, including the creation of a database to match FDI firms' purchase requirements with potential

¹¹⁰ World Bank Group (2017b)

¹¹¹ Smarzynska and Spatareanu (2014)

domestic suppliers in the electronics industry and the establishment of a liaison service to help foreign affiliates identify potential suppliers. However, these initiatives remained largely weak and uncoordinated and thus did not yield expected results as they failed to bridge the technical, managerial, and cultural gaps between FDI and Irish suppliers.¹¹²

The Industrial Development Authority (IDA) established to promote and support industrial development in Ireland, plays a key role for FDI linkages until today. Its goal was to transform the economy – away from traditional manufacturing where Ireland was no longer competitive to more modern and high-tech production. Financially well-equipped and with political clout, IDA was able to force through proposals for modernization and targeted the emerging software development, customer support and data-related services sectors which became major new sources of jobs. While Ireland had no tradition in these high-tech sectors, there was growing belief that, with its good educational base, it could succeed in becoming a competitive production base for MNCs in Europe. In anticipation of a gap in likely demand for electronics engineers and the number available in Ireland in the 1980s, it instituted a number of one-year conversion courses to furnish science graduates with the necessary qualifications. The rapid response by the educational authorities became a selling point for IDA to target prospective foreign investors.¹¹³ Till date, Ireland is Europe's lead location for software and shared services.

The National Linkage Program (NLP) was Ireland's first program of this kind. Launched in 1984, it aimed at upgrading Irish suppliers to serve the MNC market in Ireland and to tackle three key problems: (i) to build the technical competence of local companies (capability-building), (ii) to assist capable suppliers to achieve scale (capacity-building), and (iii) to build awareness of the potential domestic supply potential among MNCs (communications-building).¹¹⁴ Due to the firm-level approach adopted by IDA in the previous years, the agency had a considerable knowledge of MNC needs and the capability of Irish firms. What's more, it also had established relations with both parties which made its new role in promoting linkages a natural evolution of its previous function.¹¹⁵ The NLP support covered 5 elements¹¹⁶:

- *Market research:* to identify linkage opportunities between MNCs and domestic firms;
- *Matchmaking:* to work closely with individual suppliers and buyers to remove all obstacles and reach a subcontracting arrangement;
- *Monitoring and trouble-shooting:* to monitor the progress of on-going local subcontracting, and, with the consent of the firms involved, act as a trouble shooter when problems occur;
- *Business and organization development:* to provide advice and consultation services to help SMEs build their management, production, accounting, quality control and human resource systems, understand MNCs' ways of conducting business, and develop business strategy and plans;
- *Broker for state assistance programs:* to help local firms access state assistance programs to enhance their technical, financial and managerial capabilities;

Participation in the NLP was entirely voluntary – with no element of compulsion to localize. To increase the NLP's credibility, it was taken outside the existing public industrial development agency structure and headed by a private sector entrepreneur who possessed market credibility. The rest of the staff was seconded from IDA. Since the reputational risk of one failed linkage which would cause damage to the MNC was high and could have undermined the FDI-driven development policy of the country, a lot of efforts were made to underscore the voluntary and market-based nature of the program. A related issue was the inevitable selectivity in choosing Irish companies admitted to the program. To minimize concerns and complaints, a database on sub-supply opportunities was established which was open to all companies to register and thus reduced the impression of selectivity.¹¹⁷

¹¹² Battat et al. (1996)

¹¹³ Ruane (2001)

¹¹⁴ Crowley (1996)

¹¹⁵ Ruane (2001)

¹¹⁶ Battat et al. (1996)

¹¹⁷ Ruane (2001)

The NLP enjoyed high media attention, which created high expectations. During the first phase of the NLP, including 50 local firms, targets were to increase local sourcing share in the sector by 1% each year and to have 66% of participating firms succeed in linking to MNCs. These results were not met, and the NLP entered its second phase. It established new and more realistic targets, with a success rate of about 50% of companies, and placed stronger emphasis on building capabilities, especially technical competence, within the local firms. Matching support continued but assumed a relatively minor role.

The third NLP widened its sectoral focus and programmatic scope. IDA established a Linkages Division with a dedicated team focusing on electronics and one covering all other sectors given that support mechanisms needed to be increasingly tailored to sector requirements. These teams focused on increasing horizontal and vertical cooperation by being actively engaged in matchmaking (communications-building) and started to tackle the scale issue (capacity-building) while focusing also on more specialized skills development (capability-building). Compared to previous phases, this was the most inclusive linkages policy, where enterprise development support was integrated in a comprehensive sectoral framework.¹¹⁸

From an institutional perspective, the Irish example raises interesting considerations. While the NLP was established as a stand-alone entity at the beginning, to provide more credibility to the program and repel any concerns of public influence in the focus of the program, its consolidation within IDA during the third phase of NLP reflected both acceptance and maturity. It coincided though with the establishment of two separate agencies to promote and support industrial development, IDA Ireland to handle MNCs, and Enterprise Ireland (EI) the point of contact for Irish companies. Since the main effort to make linkages happen was regarded to be with local firms, EI was given responsibility of the linkage program. The need and terms of cooperation on this agenda had been agreed. EI's additional resources which allowed more direct agency involvement, including even taking equity in local firms, accelerated the performance improvements of Irish firms, especially in electronics, in the 1990s.

With increasing globalization, the goalpost for local linkages had changed. By the end of the century, the electronics sector was among the most globalized industries in the world. While Irish suppliers now had the capacity to supply MNCs hosted in Ireland, they were not yet competitive to become global suppliers to the industry. This led policymakers to realize that the whole industrial potential is under threat if Ireland continued to focus on local linkages only. Thus, the fourth phase of the NLP, emphasized international linkages and the globalization of the local supply industry. This change was facilitated by the merger of the national export promotion entity with EI. The support mechanisms offered integrated a mix of export, outward investment, and linkage promotion, including (i) assisting local firms finding global partners to help them meet scale targets, (ii) finding international owners for local firms that did no longer succeed so that local plants could continue to operate, (iii) assisting local firms in finding international markets for their outputs, often following on the parents of international affiliates who source locally, (iv) assisting local firms in finding/building cheaper sub-supply sources in lower-cost locations, and (v) assisting local firms in drawing on sub-supplier outputs produced in Ireland and/or other European low-cost production bases.¹¹⁹

The NLP is considered an unequivocal success in Ireland. Between 1985 to 1992, MNCs operating in Ireland doubled their local purchases of raw materials and increased services sourcing by 50%. The local content in the electronics sectors rose from 9-19% and, on average, suppliers saw their sales increase by 83%, productivity by 36%, and employment by 33%. Several also became successful international subcontractors.¹²⁰

¹¹⁸ Crowley (1996)

¹¹⁹ Ruane (2001)

¹²⁰ Battat et al. (1996)

Ireland continues to operate linkage programs, keeping the focus on developing global suppliers. The Global Sourcing Initiatives was introduced by EI in 2012. The increased complexity of managing global supply chains requires strong risk management capabilities, identification and management of hidden costs arising from distance to market and volatility, and strategic partnership management. Likewise, supply chain management and flexible business models are increasingly relevant to Irish firms as they internationalize through acquisition and/or outward direct investment (OFDI).¹²¹

¹²¹ Forfas, Manufacturing 2020

Annex 2. Support measures and institutions in the area of FDI attraction and localization

Special investment contracts

Special investment contract (SPIC) is a new instrument of the state industrial policy aimed at the stimulation of FDI into industrial production in the territory of Russia. The definition and key peculiarities of SPICs are provided in article 16 of the Federal Law "On industrial policy in the Russian Federation" dated December 31, 2014 № 488-FZ.

A special investment contract is an investment agreement between the Russian Federation (or a region) and the investor. Under the contract and within its duration, the investor shall establish, upgrade or start the manufacturing of industrial production on the territory of Russia, and the Russian Federation (or a region) shall grant the investor certain benefits according to the federal or regional legislation.

SPICs may be concluded with the participation of the Russian Federation (federal SPICs) as well as with the participation of the regions (regional SPICs). Rules and conditions for the preparation and signing of federal SPICs are defined in the Regulations of the Government of the Russian Federation dated July 16, 2015 № 708 "On special investment contracts for individual sectors of industry". The procedures for the preparation and signing of regional SPICs are defined by the regional legislative acts.¹²²

Main forms of support for investors under the contracts at the federal or regional level (all the benefits provided to investors should be based on existing legislation):¹²³

- Guarantee of non-increase of the total tax burden;
- Tax benefits (land tax, property tax, profit tax);
- Obtaining the status "Made in Russia";
- Access to state procurement;
- Sectoral subsidies;
- Creation of infrastructure objects by the regions;
- Special conditions for renting land plots.

Until now, 33 of such contracts have been signed.¹²⁴ For example, Mercedes-Benz signed such a contract in 2017 for the creation of automobile production in the Moscow region. The contract was signed with the Ministry of Trade and Industry and the government of the Moscow region.¹²⁵ The company is responsible for the localization of production, development of technologies and the creation of a new plant. In return, Mercedes-Benz receives tax benefits, simplification of administrative procedures and the status "Made in Russia" which gives them an opportunity to participate in state procurement.¹²⁶ Another example is a contract signed by the German-Japanese concern DMG Mori. According to the contract, the company will create the production of modern lathe and milling machines in the Ulyanovsk region.¹²⁷

¹²² <http://minpromtorg.gov.ru/activities/vgpp/vgpp2/>

¹²³ <http://frprf.ru/gospodderzhka/o-spetsialnykh-investitsionnykh-kontraktakh-dlya-otdelnykh-otrasley-promyshlennosti/>

¹²⁴ <http://frprf.ru/download/prezentatsiya-mekhanizma-spetsialnykh-investitsionnykh-kontraktov-po-postanovleniyu-pravitelstva-708-ot-16-07-2015.pdf>

¹²⁵ <https://auto.rambler.ru/news/36160236-avtomobili-mercedes-nachnut-sobirat-v-rossii-s-2019-goda/>

¹²⁶ <http://strategyjournal.ru/articles/lokalizatsiya-proizvodstva/>

¹²⁷ <http://strategyjournal.ru/articles/lokalizatsiya-proizvodstva/>

Another interesting example is Hyundai Motor Manufacturing Rus which signed a contract related to the creation of an R&D center at the production of auto-components with the status “Made in Russia”. The project also is aimed at modernizing main assets for the production of the models Hyundai Solaris, Hyundai Creta and Kia Rio.¹²⁸

Certification for the “Russian product” label

This support measure is connected with a recent policy of the Russian Federation to establish restrictions with regard to certain types of foreign products for participation in state procurement. As a result, certain types of goods produced in Russia (or “Made in Russia”) enjoy an advantage over goods imported from foreign countries in state procurement. The status of a local producer could be demanded in certain cases of participation in state procurement and is usually not necessary when it comes to selling goods on the private market. However, taking into account that state procurement is a huge part of the Russian economy, foreign producers often decide to develop local production in order to participate in state procurement. The “Russian product” certificate enables a foreign investor to participate in state procurement as well as in the procurement of state-owned companies in those cases where Russian-made products are privileged.

To use the benefits of the «Russian product» status, it should be confirmed that the goods produced by a localized foreign company are really produced in Russia. For state procurement purposes, industrial products are classified as produced in Russia if one of the following requirements is met:¹²⁹

- The production meets the criteria set in the Annex to the Decree of the Government of the Russian Federation dated July 17, 2015 № 719;
- The production meets the criteria set by the Agreement “On the rules of the identification of the goods’ country of origin in the Commonwealth of Independent States” dated November 20, 2009;
- Industrial production is manufactured under a special investment contract.

The main legislative act defining the procedure for obtaining the “Russian product” label is put out by the Regulations of the Government of the Russian Federation dated July 17, 2015 № 719 “On the confirmation of manufacturing of industrial production on the territory of the Russian Federation”. According to the Regulations, the main criteria for the confirmation are:

- The special investment contract signed by the investor with the Russian Federation, a region of the Russian Federation and or municipality;
- Act of expertise conducted by the Chamber of Commerce and Industry of the Russian Federation on the compliance of manufactured industrial production to the requirements specified in the Annex to the Regulations;
- Certificate of origin of the product, according to the country of origin (in case the manufactured product is not mentioned in the Annex to the Regulations).

The detailed procedure of confirmation is defined by the Order of the Ministry of Industry and Trade of the Russian Federation dated November 12, 2015 № 3568.

The issue in this area is that many foreign companies with production facilities in Russia are unable to receive a “Russian product” certificate for their products, especially if they only have assembly facilities.

¹²⁸ http://frprf.ru/proekty-i-zayavki/proekty/?region=&branck=&type_support=2063

¹²⁹ http://www.amchamrussia.ru/presentations/20170124_CUS_Goltsblat.pdf

An assembly plant in Russia is not sufficient to receive a “Russian product” certificate. Moreover, requirements on local content and technology transfer must be met. At the same time, the requirements specified in the legislation cannot usually be met within the established timeframes. Therefore, investors need a grace period. At present, this grace period can only be achieved with a special investment contract. Thus, a special investment contract empowers the investor to start production and to receive immediately a “Russian product” certificate for the first three years, even if the manufactured products do not meet the localization requirements. After the grace period, the required degree of localization must be achieved.

Support for new investment projects

The support in the form of subsidies is provided to enterprises for the reimbursement of a portion of expenses in regards to paying interest rates on the loans received in 2014-2019 and/or payments of coupon income on bonds issued in 2017-2019 for the implementation of investment projects in priority areas of the civilian industry.¹³⁰ The support measure is based on the Decree of the Government of the Russian Federation dated January 3, 2014 № 3. The subsidies are provided in the case where a project is included in the list of investment projects in priority areas of the civilian industry. The volume of supported projects should be between 0.15 and 7.5 bln. RUR (up to 10 bln. RUR for projects implemented under the special investment contracts). The loan should not exceed 80% of the total cost of the project.

Loans from the Industry Development Fund¹³¹

The Fund was established in 2014 to facilitate the modernization of the Russian economy, the creation of new production plants and import substitution. The Fund provides loans for the implementation of projects aimed at the introduction of new technologies, the creation of new products or the establishment of new production. The volume of the loans may be from 5 to 750 mln. RUR, for the period of up to 7 years, with an interest rate of 1, 3 or 5%.

Program supporting investment projects implemented in the territory of the Russian Federation on the basis of project financing

The program was approved by the Decree of the Russian Government dated October 11, 2014 № 1044. The program's goal is to create a mechanism for support for investment projects that will facilitate the increase of the volume of credits provided to Russian enterprises with beneficial conditions. The loans/credits may be provided by the Russian crediting organizations or international financial organizations selected for the participation in the program, or by Vnesheconombank. The selection of projects for the participation in the program and provision of state guarantees are made by the special interdepartmental commission under the Ministry of Economic Development.

Support for R&D

The R&D support is provided in the form of subsidies, on the basis of the Decree of the Government of the Russian Federation dated December 30, 2013 № 1312. Subsidies are provided to organizations selected at a special competition for the compensation of a portion of expenses for R&D under the implementation of complex investment projects in priority areas of the civilian industry. Decisions on the provision of subsidies are taken by a special commission established by the Ministry of Trade and Industry.

¹³⁰ <http://frprf.ru/gospodderzhka/subsidirovanie-protsentnoy-stavki-na-realizatsiyu-novykh-investitsionnykh-proektov/>

¹³¹ <http://frprf.ru/zaymy/proekty-razvitiya/>

The total volume of a project should be in the range of 100 mln. rubles – 2 bln. rubles, and the volume of credit financing should not be more than 80% of the total project cost.

Export support measures

A set of measures that indirectly stimulate foreign companies to locate their production in Russia is related to export support. Most of the measures in this area are implemented by the Russian Export Center. This kind of support helps subsidiaries of the foreign companies located in Russia to export their products, thus improving the economics of their localization projects. For example, one of the measures is a subsidy for compensation of a portion of expenses (from 20 to 80%) for delivering products to export markets (based on the Decree of the Russian Government dated April 26, 2017 № 496).¹³² In 2018, this subsidy was used by “Volvo Vostok” to export truck cabins from the company plant in Kaluga to the Volvo plant in Germany.

Sectoral measures

The Russian Government also implements specific localization support measures in various sectors. For example, in agriculture, the demand for new agriculture machines and equipment produced under the import substitution projects is supported by the compensation of discounts for domestic technics and beneficial leasing.¹³³ Agricultural production is stimulated under a number of programs, including subsidies for the reimbursement of interest rate payments.¹³⁴ In the automotive industry, the incentives for localization were established by the Decree of the Government of the Russian Federation dated March 29, 2005 № 166.¹³⁵ This Decree provides significant customs benefits for automotive producers in return for the obligations to achieve certain localization levels. The benefits may be provided if a company signs a special agreement on industrial assembly (the rules on signing such agreements were established by the Order of the Ministry of Economic Development and Trade, Ministry of Industry and Energy, and the Ministry of Finance dated April 15, 2005 № 73/81/58H). However, the agreements' term ends in 2018-2019, and further support will be regulated under the special investment contracts. Localization of auto producers in Russia was also stimulated by other state programs, including beneficial loans for the purchase of cars assembled in Russia and the “trade-in” program (support for changing an old car for a new one).¹³⁶ Another area of support for the auto industry is in export development and in 2017, the Government of the Russian Federation adopted a special strategy in this area (Decree dated August 31, 2017 № 1877-r). Priority directions of the strategy:

- creation of favorable conditions for the development of export-oriented production of automobiles and their components;
- support for the promotion of Russian producers in new foreign markets;
- launching the production of models for global markets at existing plants;
- integration of Russian producers of auto components in supply chains of international manufacturers.

¹³²https://www.exportcenter.ru/services/subsidirovaniye/kompensatsiya_chasti_zatrata_na_transportirovku_produktovii/_kompensatsiya_chasti_zatrata_na_transportirovku_produktsii/

¹³³ http://minpromtorg.gov.ru/press-centre/news/#!minpromtorg_utverdil_plany_po_importozamesheniyu_v_19_otraslyah_promyshlennosti

¹³⁴ <http://mcx.ru/activity/state-support/measures/>

¹³⁵ Detailed order on the application of the

¹³⁶ <http://strategyjournal.ru/articles/lokalizatsiya-proizvodstva/>

Another example is the pharmaceutical industry which is supported under the State program “Development of pharmaceutical and medical industry in 2013-2020” (approved by the Decree of the Government of the Russian Federation dated April 15, 2014 № 305).

Regional measures

In addition to federal level measures, regions also provide incentives for import substitution, FDI, and localization of production. The support may take various forms including subsidies, tax benefits, etc. Regions may also provide support for investors in cooperation with the federal Industry Development Fund under the program “Joint loans”. The program is aimed at supporting import substitution and manufacturing of competitive products in the civilian industries. The loans are provided jointly by the federal Industry Development Fund and the regional industry/entrepreneurship infrastructure at the interest rate of 1 or 5% annually (70% of the federal funds and 30% of the regional funds).¹³⁷

Industrial infrastructure

Creation of industrial infrastructure is supported in order to provide sites for the localization of production in Russia by domestic and foreign investors. The main types of such infrastructure in Russia include:

Special economic zones. The federal program on the creation of special economic zones (SEZ) was launched in 2005. It is aimed at regional development by direct foreign and Russian investments. SEZs have been established for 49 years. SEZ residents retain the right to buy a land plot at a discounted rate after they start production activities. All SEZs are endowed by the state with special legal status that provides a set of tax and customs preferences to the residents and also guarantees the access to necessary hard infrastructure. The SEZs management companies undertake actions on investment attraction and provide support for investors in solving problems related to administrative procedures. The costs of the projects implemented in SEZ are on average 30% less compared to Russia general practice. At present there are 25 SEZs:¹³⁸

- 9 for industrial production;
- 6 for R&D and innovation;
- 9 for tourism;
- 1 for logistics (port zone).

Main results of the SEZ activity:¹³⁹

- more than 700 residents;
- about 30 000 jobs created;
- more than 120 foreign investors from 37 countries;
- more than 5 bln. USD of investments made by the residents.

¹³⁷ <http://frprf.ru/zaymy/regiony/>

¹³⁸ <http://economy.gov.ru/minec/activity/sections/sez/>

¹³⁹ <http://economy.gov.ru/minec/activity/sections/sez/>

Industrial parks. Such parks establish favorable conditions for the implementation of investment projects related to the development of production in Russia. Support for the creation of industrial parks is based on Article 19 of the Law «On industrial policy in the Russian Federation» dated December 31, 2014 № 488-FZ. The support provided for the park and its management company complies with the requirements established by the Government of the Russian Federation, and additional requirements established by the regions (if there are such requirements). Federal requirements for industrial parks are established by the Decree of the Government of the Russian Federation dated August 4, 2015 № 794, and by the National Standard (GOST R 56301 – 2014) “Industrial parks. Requirements”.

Support for the creation of industrial parks is coordinated by the Ministry of Industry and Trade. The Ministry launched a geoinformation system on the industrial parks, technoparks, clusters and other objects of industry support infrastructure in Russia – www.gisip.ru. According to the data of the system¹⁴⁰, in 2018 there were 176 industrial parks in Russia including 58 parks under creation. Among all parks, 41% are public, 58% are private and 1% have mixed ownership. Leaders by the number of parks are:

- Moscow region – 35
- Republic of Tatarstan – 19
- Kaluga region – 10
- Leningrad region – 7
- Republic of Bashkortostan - 6

Key advantages of locating production in the industrial parks for investors:

- Lowering administrative barriers;
- Better opportunities to get public support for the implementation of investment projects;
- Developed hard infrastructure.

In Russia, there also exists an Association of Industrial parks (<http://www.indparks.ru>) that provides support for foreign and Russian investors in the selection of industrial sites for production, and in the search for suppliers in Russia.

Technoparks. The state standard GOST R 56425 – 2015 “Technoparks. Requirements” defines two types of technoparks in Russia:

- Technoparks in the area of high technologies – technoparks aimed at ensuring the launch and market promotion of high technology products and services, including in cooperation with local research and/or educational organizations. The first technoparks of this kind were created in Russia under the program «Creation in the Russian Federation technoparks in the area of high technologies» approved by the Decree of the Government of the Russian Federation dated March 10, 2006 № 328-p.¹⁴¹
- Industrial technoparks – technoparks for the launch and market promotion of industrial products and technologies. Support for the creation of such technoparks is regulated by article 19.1 of the Law «On industrial policy in the Russian Federation» dated December 31, 2014 № 488-FZ. Support for the park and its tenants is provided if the park and its management company comply with the

¹⁴⁰ https://www.gisip.ru/stats_sum/pdf/ru/

¹⁴¹ <http://akitrf.ru/technoparks/about/>

requirements established by the Government of the Russian Federation, and additional requirements established by the regions (if there are such requirements).

According to the Russian Association of clusters and technoparks, there are 107 technoparks working or being created in Russia.¹⁴²

Territories of accelerated development (TAD). TAD is a territory that provides tax benefits and a simplified administrative regime to its residents. The goal of this support mechanism is to facilitate investment promotion in the territories characterized by an underdeveloped social and economic environment. Creation of such territories is based on the Federal Law dated December 29, 2014 № 473-FZ «On the territories of accelerated social and economic development in the Russian Federation». At present there are 100 TADs in Russia, including the ones that will be created in 2019.¹⁴³

Key advantages of TADs for investors:¹⁴⁴

- Tax benefits (profit tax, VAT, tax on the extraction of mineral resources, property tax, land tax);
- A significant reduction of the fees to the funds of social and medical insurance;
- Reduction of the cost of rent;
- Preferential access to engineering infrastructure.

An important aspect is that a private company may not only join an existing TAD, but may also initiate the creation of a new TAD with relevant favorable amendments to regional legislation. This may bring valuable benefits, provided the following points are taken into account:

- Outside the Russian Far East, the TADs must be located in a so-called "mono-city" (cities that were created around large enterprises). Unless the company is looking to locate in the Russian Far East, only regions with mono-cities may offer this program to the investor and each such mono-city should be prescreened for basic suitability criteria.
- Any investment that was made in a project prior to joining/initiating a TAD is unlikely to be counted towards the minimum investment amount required to become a TAD resident, so it is important to make a decision on whether to apply for a program as early as possible.
- If there is a very limited timeframe for establishing a factory, the length of the initiation process for the TAD might be an issue.

Based on the experience of companies that have already gone through the process of joining or initiating a TAD, there are other aspects that need to be looked at during the later stages of analysis. For example, if an investor started the construction process before becoming a resident of a TAD, it may need to consider undertaking certain restructuring steps before joining the TAD.

Skolkovo Innovation Center. Skolkovo was founded according to the Federal Law dated September 28, 2010 № 244-FZ, with the goal to create a sustainable ecosystem of entrepreneurship and innovation, engendering a startup culture and encouraging venture capitalism. Skolkovo identified five key areas of potential growth: energy efficiency, strategic computer technologies, biomedicine, nuclear technologies

¹⁴² <http://akitrf.ru/technoparks/about/>

¹⁴³ <https://www.kommersant.ru/doc/3883885>

¹⁴⁴ https://rosco.su/press/Igory_predprinimateljami_osushchestvlyayushchim_deyatelnost_na_territorii_operezha_yushchego_sotsialno/

and space technologies. The Center is located near Moscow and is composed of companies and startups developing innovative technologies (currently, numbering over 1,000), a Technopark, the Skolkovo Institute of Technology, a new graduate research University established in collaboration with the Massachusetts Institute of Technology, and Skolkovo city, located near Moscow.¹⁴⁵ Russian legal entities that are the Center's residents have tax benefits (VAT tax, profit tax, property tax), reimbursement of customs duties and import VAT, and reduced rates of fees to pension and insurance funds.¹⁴⁶

Innovative territorial clusters. The program for the support of innovative territorial clusters was launched in 2012 based on the Strategy for innovation development of the Russian Federation until 2020 (adopted in 2011). In addition, in November 2011, the President of the Russian Federation ordered a list to be created of existing Russian clusters. According to the official definition¹⁴⁷, an innovative territorial cluster is a group of enterprises and organizations in a certain location characterized by:

- a research and production chain in one or several sectors (key types of economic activity);
- a mechanism for coordination and cooperation of cluster members;
- synergy effect that leads to improvements in economic efficiency and performance of each enterprise or organization thanks to concentration and cooperation.

Key benefits to firms in the clusters:

- State support for cooperative projects
- Access to hard and soft infrastructure, information and technology exchange, and specialized training
- Proximity to markets, input, and equipment suppliers
- Lower transaction costs
- Institutional support from state bodies and cluster management organizations
- Ability to offer integrated solutions in cooperation with other cluster members

In 2012, the Governmental Commission on High Technologies and Innovations issued an order to the Ministry of Economic Development to design proposals on the selection of clusters and support for their development. The Ministry organized a competition for clusters and designed guidelines on the preparation of development programs of innovative territorial clusters. The list of pilot innovative territorial clusters was approved by the Prime Minister on August 28, 2012. It included 25 clusters eligible for support from the federal budget with higher priority (14 clusters) and lower priority (11 clusters). In 2014 and 2016, two more clusters were added.

In 2016, the MoED began an overhaul of the innovative clusters' support program. The legal basis for the new program was the Ministry's Order dated 27.06.2016 # 400 «On the Priority Project of the MoED of Russia «Development of innovative clusters – investment attractiveness world level leaders». On July 8, 2016, the Ministry approved a Strategy for the Priority Project, as well as a procedure for the selection of the clusters. The Ministry selected 11 clusters that would receive state support. One cluster was added later, thus there are 12 such clusters at present.

¹⁴⁵ <http://sk.ru/foundation/about/>

¹⁴⁶ <https://vc.ru/legal/42353-nalogovye-igoty-dlya-rezidentov-skolkovo>

¹⁴⁷ Regulations on the creation of a list of pilot programs for the development of innovative territorial clusters

Industrial clusters. Support for the industrial clusters is regulated by article 20 of the Law «On industrial policy in the Russian Federation» dated December 31, 2014 № 488-FZ. According to the Law, an industrial cluster is a group of stakeholders in the area of the industry, connected by the relationships in this area due to geographic proximity and functional interdependence, and located in the territory of one region of the Russian Federation or several regions of the Russian Federation. Support for the clusters and their members is provided if a cluster and its management company comply with the requirements established by the Government of the Russian Federation, and additional requirements established by the regions (if there are such requirements). Such requirements at the federal level are established by the Decree of the Government of the Russian Federation dated July 31, 2015 № 779. The program for the support of industrial clusters is supervised by the Ministry of Industry and Trade. As the first step, a potential cluster should submit an application to the Ministry. In case the cluster meets the requirements, it is then included in the list of industrial clusters. Companies which are members of the clusters may receive state support for the implementation of cooperative projects approved by the Ministry. At present there are 30 industrial clusters in Russia.¹⁴⁸

Apart from above-mentioned support measures for FDI localization, a lot of activities are conducted by various institutions at the federal and regional levels with a view to facilitating the implementation of FDI-related projects and the protection of foreign investors' rights in Russia. The key institutions are the following:

Russian Private Equity Fund.¹⁴⁹

The Fund is the sovereign investment fund of the Russian Federation with reserved capital of 10 bln. USD. The Fund invests in the leading and most-promising Russian companies in cooperation with foreign investors thus catalyzing new inward investment. The Fund was created in 2011. The total volume of investment is more than 1.4 trln. RUR, including more than 100 bln. RUR provided by the Fund and more than 1.3 trln. RUR provided by the partners. In addition, the Fund attracted more than 40 bln. USD of foreign capital into Russia thanks to a number of strategic partnerships. The Fund has also created a web portal, Invest in Russia (<http://investinrussia.com>), with information about the regions, promising sectors, and public support measures.

Agency for Strategic Initiatives (ASI).¹⁵⁰

The Agency implements a number of projects aimed at the creation of favorable conditions for business, investment promotion in the Russian regions and regional investment team's capacity building. The work is organized under the special roadmaps, prepared by the working groups of the National Entrepreneurship Initiative. The goal of the roadmaps is to improve the country's investment climate thanks to the simplification, acceleration and cost reduction of business-related procedures. The roadmaps are approved by the decrees of the Russian government. The target indicators of the implementation of the roadmaps are based on the Doing Business ranking, OECD indicators of competitive product market environment, and the World Bank indicator of entrepreneurial activity on New Business Density. ASI has created a special web portal with information on the regional investment opportunities and support measures for investors, including foreign ones (<https://investinregions.ru>). The Agency also designed and introduced the Regional Investment Standard. The Standard includes the best investment

¹⁴⁸ <https://umatex.com/news/klaster-kompozity-bez-granits-v-klyuchen-v-reestr-minpromtorga-rossii/>

¹⁴⁹ <https://rdif.ru>

¹⁵⁰ <https://asi.ru/investclimate/>

promotion practices used by the most successful regions. It also offers businesses an opportunity to influence state decisions and participate in the discussion of investment climate issues.

Project office for FDI attraction to Russian regions.

The office is created by the Russian Private Equity Fund and ASI on the basis of an agreement signed by these institutions in 2018.¹⁵¹ Priority tasks of the office:

- Development of competencies on the attraction of investment to Russian regions on the basis of the best Russian and foreign practices;
- Designing a model of cooperation with the regions for initiating investment projects and their follow-up during the implementation;
- Joining efforts and resources between the federal and regional development institutions;
- Creation of a «front-office» for working with investors.

The office will also work actively with those foreign investors that have not yet taken a decision about investment in Russia, or a decision about a country for business expansion. **National Association of Agencies for Development and Investment** (<http://naair.ru>).

The Association unites regional investment promotion agencies and development corporations. Its main functions:

- Creation of a community of professionals in the area of investment promotion;
- Support for investment promotion and the development of business contacts;
- Stimulation of cooperation and best practices exchange among the development institutions;
- Coordination of regional projects with state bodies and the federal development institutions;
- Promotion of the investment image of the Russian regions abroad;
- Organization of information exchange between investment agencies in Russia and foreign countries;
- Information support for potential investors;
- Organization of training in the area of investment promotion.

Investment commissioners in federal districts.

The activity of investment commissioners is based on the Decree of the President of the Russian Federation dated August 3, 2011 № 535-p, and is aimed at the introduction of priority measures for the improvement of the investment climate and support for the implementation of investment projects. The investment commissioners coordinate the interaction of state bodies and municipalities with investors and protect the investors' rights. In the federal districts, investment commissioners are deputies of relevant Presidential Plenipotentiaries. In many of the Russian regions, such investment commissioners were also appointed. This responsibility is usually assigned to regional or municipal officials.¹⁵²

Council on investment under the Chairman of the State Duma.

The Council's activity is aimed at the enhancement of investment activity in the national economy through relevant changes in the legislation.¹⁵³

¹⁵¹ <https://asi.ru/news/95222/>

¹⁵² <http://young.smb.gov.ru/support/protect/633851.html>

¹⁵³ https://1prime.ru/press_release/20131121/771083550.html

Governmental Commission on the monitoring of foreign investment in the Russian Federation.

The Commission was created to monitor the foreign investment going into enterprises that are strategic for the defense and security of the state. The Commission approves the deals related to the sale of shares in such enterprises to foreign investors.¹⁵⁴

At the regional level, support for FDI attraction and localization is usually provided by **regional development corporations** and/or **investment promotion agencies**. Regional development structures of various organizational and legal forms have been set up across the Russian regions with the goal of finding investors for the regions, support, and coordinate investment projects important at the regional level. The key functions of regional investment promotion agencies usually include the presentation of regional investment potential to foreign investors through road-shows and missions, creation and maintenance of the regional investment web portals, hands-on support for foreign investors on the preparation and implementation of investment projects, and assistance in the improvement of investment climate at the regional level. In some regions, the functions of investment agencies are performed by regional development corporations.

Apart from the institutions created by the state bodies, support for FDI attraction and the implementation of FDI projects is provided by a number of non-governmental, international and bilateral organizations, such as the following:

Foreign Investment Advisory Council (FIAC; <https://fiac.ru>). The Council was created in 1994. The main goals of the Council are to facilitate FDI attraction in Russia and the improvement of the investment climate for foreign investors. The Council's chairman is the Russian Prime Minister Dmitry Medvedev. In 2019, the Council will focus on the following priority directions:¹⁵⁵

- digitalization of the economy and the introduction of advanced technologies;
- localization and regional development;
- improvement of tax and customs administrative procedures;
- Development of the consumer market and technical regulations;
- Development of the healthcare and pharmaceutical industries;
- Natural resources and the environment;
- Development of the banking sector and financial markets.

Intergovernmental commissions on cooperation with foreign countries (including committees and working groups under the commissions). These commissions are established for effective cooperation between business and the state at the international level, creation of favorable conditions for external economic relations of Russia, and support for Russian companies in cooperation with foreign partners. The commissions prepare proposals and projects on economic cooperation, including that of FDI localization. For example, the Russian-French Council on Economic, Financial, Industrial and Trade Affairs designed a program that includes 14 projects in 5 sectors. The program envisages the use of the localization mechanism to widen the range of auto-components produced in Russia.¹⁵⁶ The goal of the Russian-German Strategic Work Group on Cooperation in the area of Economics and Finance is joint

¹⁵⁴ <http://government.ru/department/8/about/>

¹⁵⁵ <http://government.ru/news/34437/>

¹⁵⁶ <http://strategyjournal.ru/articles/lokalizatsiya-proizvodstva/>

stimulation of activities of German companies in Russia and Russian companies in Germany. The Group works on the improvement of the investment climate, contributes to solving problems hampering cooperation between Russia and Germany, and facilitates the preparation and implementation of joint projects.¹⁵⁷

Association of European Businesses (<http://www.aebrus.ru>). The Association was founded in 1995 and includes more than 500 European and Russian companies. It is a representation of foreign investors in Russia, with 60 committees, subcommittees and working groups that are engaged in lobbying in various business areas including energy, transport and customs, agriculture, air travel, passenger cars and commercial vehicles production, legislation, taxation, banking, real estate, crop protection products and many others. These committees work closely with the European and Russian authorities and provide comments on drafted legislative acts of the Russian Federation.

Russian Chamber of Commerce and Industry (<https://tpprf.ru/en/>). The Chamber represents interests of SMEs and large companies in all business sectors – manufacturing, domestic and foreign trade, agriculture, financial systems, and services. It also conducts activities aimed at developing economic cooperation between Russia and other countries, including that in the area of FDI attraction and localization. The Chamber includes a number of international business councils that promote trade and investment between Russia and other countries. A network of 30 Chamber's representative offices abroad helps to establish direct contact with potential foreign partners, provide information outside Russia and provide access to new markets.

An important role is played by **bilateral trade chambers**. The largest ones organize a lot of activities aimed at improving economic cooperation between relevant countries and Russia. For example, the **American Chamber of Commerce in Russia** (<https://www.amcham.ru>) includes more than 500 members. It seeks solutions to trade and investment problems to promote the legitimate common economic interests of the member companies. There are 18 committees in the Chamber's structure, including the Localization and Procurement Committee which serves as a platform to support companies on localization and procurement issues across all business sectors. The **Russian-German External Trade Chamber** (<https://russland.ahk.de>) represents the interests of German companies in Russia and supports Russian companies in cooperation with German firms in Russia and in Germany. The Chamber includes a Committee on Localization and Industrial Production. The Committee analyzes the experience of the implementation of infrastructure and industrial projects in Russia, studies the best cases and engages in a dialog with relevant state bodies. The Committee members discuss important aspects such as obtaining the «Russian product» label, use of SPICs, measures on the development of the system of suppliers in Russia, staff training, and localization of production in various industry sectors. The companies share practical experience and prepare proposals for the state bodies on the elimination of barriers for the activity of German companies in Russia.¹⁵⁸ The **French-Russian Chamber of Commerce and Industry** (<https://www.ccifr.ru>) performs functions of the Trade Representation Office of France in Russia (the state representation office was closed in the summer of 2018). It also provides services to French companies working in Russia: organization of business missions to regions in order to analyze local conditions and meet with the regional authorities/companies to reach agreements on economic

¹⁵⁷ <https://russland.ahk.de/ru/infothek/news/detail/strategische-arbeitsgruppe-fuer-wirtschaft-und-finanzen-tag-in-moskau/>

¹⁵⁸ <https://russland.ahk.de/ru/vtp/komitety-i-rabochie-gruppy/lokalizacija/>

cooperation, market studies in Russia, and analysis of the Russian economy and its sectors. In addition, the Chamber organizes road-shows representing Russian regions in France, conducts events (seminars, conferences, meetings) and includes committees that work on key problems/areas. The Chamber's Committee on localization includes French companies that discuss problems related to the production localization in Russia and cooperation with the Russian suppliers.

Annex 3. Results from the survey of regional investment agencies and development corporations

The survey was conducted in April 2019, in the format of an online questionnaire (the questionnaire is presented in Annex 2). The goal of the survey was to find out if the development of FDI linkages is a priority task for business support infrastructure in the regions (especially those having a high number of foreign investors localized on their territory), what problems prevent more intensive cooperation among local SMEs and foreign investors, and what kind of support is necessary for the surveyed institutions to improve FDI linkages in their regions. For the survey, there were specifically selected investment promotion agencies and development corporations, as they are usually responsible for cooperation with foreign investors and supporting their localization activities. Assistance in the organization of the survey was provided by the National Association of Agencies for Investment and Development that unites 50 regional investment promotion agencies and development corporations. The Association's support included help in the preparation of the questionnaire, sending the link to the online questionnaire to the members of the Association, and assistance in collecting answers. Apart from the institutions that are the members of the Association, the questionnaire was sent to other organizations that represent regions with a high number of FDI localization projects.

In total, the link to the questionnaire was sent to more than 30 organizations, most of which are Association members. The focus of the survey was on the top 20 regions by the number of FDI localization projects in the period of 2008-2018 (according to the above-mentioned data from the fdiMarkets). Answers were collected from 20 organizations representing 18 regions (in two regions – Kaliningrad region and Leningrad region – the questionnaires were filled in by 2 organizations). Organizations that provided the answers:

1. Development corporation of the Samara region
2. Development corporation of the Krasnodar region
3. Development corporation of the Ulyanovsk region
4. Altay center of PPP and investment promotion (Altay region)
5. Development corporation of the Republic of Bashkortostan
6. Development corporation of the Kamchatka region
7. Department of investment, Saint-Petersburg
8. Agency of investments and strategic projects of the Voronezh region
9. Development foundation of the Khanty-Mansiysk region
10. Investment agency of the Tyumen region
11. Development corporation of the Nizhny Novgorod region
12. Moscow city investment agency
13. Development corporation of the Lipetsk region
14. Agency for regional development of the Kaluga region
15. Agency for investment development of the Republic of Tatarstan
16. Agency for investment development of the Rostov region
17. Agency for regional economic development (Kaliningrad region)

18. Development corporation of the Kaliningrad region
19. Agency for the economic development of the Leningrad region
20. Industry development center of the Leningrad region

Out of these 18 regions, 13 are among the top 20 in Russia by the number of FDI localization projects (see table below). Thus, the survey may be considered as representative and will allow for drawing conclusions about the activities of the regional business support infrastructure in the area of FDI localization and the development of FDI linkages. The list of the regions is given below:

Table 8. List of the regions participated in the survey

No	Region	The region's position in Russia by the number of FDI projects in 2008-2018 / total number of projects
1.	Saint-Petersburg	1 / 71
2.	Kaluga region	3 / 62
3.	Republic of Tatarstan	4 / 62
4.	Nizhny Novgorod region	5 / 41
5.	Leningrad region	6 / 40
6.	Lipetsk region	7 / 39
7.	Moscow	8 / 39
8.	Ulyanovsk region	9 / 33
9.	Voronezh region	11 / 27
10.	Samara region	12 / 24
11.	Krasnodar region	14 / 22
12.	Rostov region	16 / 19
13.	Republic of Bashkortostan	20 / 14
14.	Kaliningrad region	21 / 14
15.	Tyumen region	35 / 7
16.	Altay region	50 / 3
17.	Khanty-Mansiysk region	52 / 3
18.	Kamchatka region	63 / 2

By the number of employees, the organizations are distributed as the following:

Table 9. Number of employees at the surveyed organizations

Range	Number of organizations indicated the option	Share of the total number of organizations
Less than 10	2	10
From 11 to 20	2	10
From 21 to 35	9	45
From 36 to 50	3	15
From 51 to 70	1	5
71 and more	3	15

The answers show that most of the organizations are quite large (more than 20 employees) and may potentially have enough human resources for supporting FDI linkage programs in their regions.

The surveyed organizations mainly work with medium-sized enterprises (50% of responses) and large companies (35% of responses). One of the institutions works mainly with municipal authorities to support them in the design of development strategies and programs, and the implementation of trans-border cooperation programs. Target groups of clients for the surveyed institutions are mainly those companies that implement investment projects in the territory of the regions including large and medium-sized companies in various sectors, and foreign investors. Small businesses are not the priority for most of the organizations as their focus is on the companies that implement relatively large investment projects.

The organizations provide most of their services for free (see the table below; the variants with the highest number of responses are highlighted in bold). They mainly provide services related to information and technical support for the clients:

- Provision of information about the region, including information about the sectors and potential partners;
- Selection of a land plot and organization of a deal on the sale and purchase of the land plot;
- Assistance with administrative procedures (for example, obtaining permissions and licenses);
- Help with receiving state support (including that from the federal development institutions).

About half of the organizations also provide support for the preparation of investment projects, the attraction of financial resources and promotion of goods/services in the Russian market. The share of the organizations providing services with higher added value (business planning, market studies, training, support for the preparation of innovative projects) is much lower. Only 45% of the surveyed institutions provide support in the organization of sales of products/services to foreign companies (including foreign companies localized in Russia). These results lead to a possible conclusion that organizations serve only as technical support offices to investors and local companies and have little competencies/willingness to provide services that would lead to enhancing the competitiveness of local companies with a view of their promotion to the supply chains of large MNCs.

Table 10. Services provided by the surveyed organizations to foreign investors

Services	Number of organizations providing the service for free / share in the total number of responses	Number of organizations providing the service on a fee basis / share in the total number of responses	Number of organizations that do not provide the service / share in the total number of responses
Help with receiving state support (including that from the federal development institutions)	19 / 95%	1 / 5%	0 / 0%
Provision of information about the region, including that about the sectors and potential partners	19 / 95%	0 / 0%	1 / 5%
Selection of a land plot and organization of a deal on the sale and purchase of the land plot	16 / 80%	2 / 10%	2 / 10%
Assistance with administrative procedures (for example, obtaining permissions and licenses)	16 / 80%	2 / 10%	2 / 10%
Support in the preparation of investment projects (including cooperative projects)	12 / 60%	4 / 20%	4 / 20%
Attraction of financial resources (investments, loans)	10 / 50%	2 / 10%	8 / 40%
Support in the promotion of goods/services in the	10 / 50%	1 / 5%	9 / 45%

Russian market

Support in the organization of sales of products/services to foreign companies, including foreign companies localized in Russia	8 / 40%	1 / 5%	11 / 55%
Support in the promotion of products/services in the foreign markets	7 / 35%	1 / 5%	12 / 60%
Design of business plans	3 / 15%	9 / 45%	8 / 40%
Market studies	5 / 25%	9 / 45%	6 / 30%
Help in the preparation of innovative projects (including cooperative projects)	7 / 35%	3 / 15%	10 / 50%
Training	5 / 25%	4 / 20%	11 / 55%
Support in the development of management systems	1 / 5%	1 / 5%	18 / 90%
Support in the search for personnel	5 / 25%	3 / 15%	12 / 60%
Support with accounting / legal issues	7 / 35%	5 / 25%	8 / 40%
Provision of premises	1 / 5%	5 / 25%	14 / 70%
Provision of equipment	0 / 0%	1 / 5%	19 / 95%

The majority of institutions (95%) provide support for foreign investors in the preparation and/or implementation of manufacturing localization projects in their regions. The typical services, provided by the surveyed organizations, are:

- Provision of information about a region, industrial sites/infrastructure, projects and support measures;
- Support in the preparation of business plans and market studies, and in the selection of the promising investment directions;
- Assistance in receiving state support;
- Assistance in the selection of a site for production localization;
- Organization of investor visits, presentations of the regional industrial infrastructure;
- Assistance in connecting the investor's industrial site to engineering infrastructure;
- Coordination of the investor's interaction with the state authorities and the local business community (as well as regional clusters), and helping with administrative procedures (including that related to obtaining the status of a resident of the regional industrial infrastructure - SEZs, industrial parks, technoparks, etc.);
- Support for the investor in finding potential partners (suppliers) and buyers in the region.

For example, in the Voronezh region, the local agency of investments and strategic projects assisted in the attraction of a number of foreign investors such as Siemens (Germany), PepsiCo (US), Bionorica (Germany), Claas (Germany), Nutreco (Netherlands), Vaderstad (Sweden), Lesaffre (France), TongTai (Taiwan), etc. The Agency for investment development of the Rostov region supported the localization of Guardian, PepsiCo, Mars, Praxair, Coca-Cola, Air Products, Enel, Danone and others. In Moscow, the city investment promotion agency provided assistance to a joint enterprise with the participation of a large German company NILES-SIMMONS HEGENSCHIEDT in obtaining the SEZ resident status and receiving a land plot. The company Renault-Russia received tax benefits on the taxes paid to the Moscow budget (profit tax, property tax, land lease payments). The agency also supported a joint Russian-Japan company «AAT» in the selection of a land plot for the construction of a new plant and provided assistance to the company in receiving the land plot without a tender and under a preferential lease rate.

An interesting example is in the Krasnodar region. They created a multifunctional center for foreign investors (<http://www.welcomecenter.ru/eng>). It provides the following services to companies:

- Legal support
- Accounting and audit
- HR
- IT & web-services
- Marketing services
- Nominal office
- Banking services

The center also provides services to highly qualified foreign individuals and their families:

- Migration services
- GR Services
- Notarial services
- Concierge
- Educational programs
- Insurance

- Real estate

The surveyed organizations were asked to evaluate the importance of constraints hampering the development of cooperation between foreign companies localized in Russia, and their potential suppliers from the regions where the organizations are located (from 1 to 5 where 5 is the maximum importance). The summary of the answers is given in the table below. According to the answers received, three of the most critical constraints are the following:

- Lack of communication with foreign companies in order to get information about their demands;
- Cooperation with foreign companies requires large investments into the modernization of production at the regional enterprises;
- Regional companies do not meet the requirements of foreign companies related to the quality of products/services.

The fact that many of the organizations do not know the problems indirectly shows that they have not analyzed the situation in this area, and do not provide targeted support in the development of FDI linkages in their regions.

Table 11. Constraints for the development of the supply linkages between MNCs and their potential suppliers

Constraint	Number / share of organizations answered						Total result = sum of the number of responses for each point multiplied by the points on the scale
	1	2	3	4	5	Do not know	
Lack of communication with foreign companies in order to get information about their demands	2/10%	3/15%	6/30%	6/30%	1/5%	2/10%	55
Cooperation with foreign companies requires big investments to the modernization of production at the regional enterprises	1/5%	2/10%	6/30%	3/15%	4/20%	4/20%	55

Constraint	Number / share of organizations answered						Total result = sum of the number of responses for each point multiplied by the points on the scale
	1	2	3	4	5	Do not know	
Regional companies do not meet the requirements of foreign companies related to the quality of products/services	2/10%	5/25%	1/5%	6/30%	3/15%	3/15%	54
Regional companies do not meet the requirements of foreign companies related to the level of staff skills	1/5%	5/25%	5/25%	2/10%	3/15%	4/20%	49
The search for foreign companies – potential buyers – and organization of cooperation with such companies require too much time	2/10%	2/10%	4/20%	4/20%	2/10%	6/30%	44
Regional companies do not meet the requirements of foreign companies related to the price of products/services	2/10%	8/40%	4/20%	2/10%	1/5%	3/15%	43
Material inputs, required by foreign	2/10%	2/10%	2/10%	5/25%	2/10%	7/35%	42

Constraint	Number / share of organizations answered						Total result = sum of the number of responses for each point multiplied by the points on the scale
	1	2	3	4	5	Do not know	
companies, cannot be supplied by the regional enterprises							
Low volumes of procurement by foreign companies	3/15%	3/15%	4/20%	4/20%	1/5%	5/25%	42
Regional companies do not meet the requirements of foreign companies related to the certification of products/services	2/10%	2/10%	5/25%	2/10%	2/10%	7/35%	41
Regional companies do not meet the requirements of foreign companies related to the management competencies	4/20%	6/30%	3/15%	2/10%	1/5%	4/20%	38
Low volumes of production of the regional enterprises to meet the requirements of foreign companies	4/20%	6/30%	4/20%	2/10%	0/0%	4/20%	36
Regional enterprises do not	3/15%	5/25%	4/20%	0/0%	2/10%	6/30%	35

Constraint	Number / share of organizations answered						Total result = sum of the number of responses for each point multiplied by the points on the scale
	1	2	3	4	5	Do not know	
have enough capacity in the area of design and innovation to become effective partners for foreign companies							
Regional companies do not meet the requirements of foreign companies related to the time of delivery of products/services	3/15%	5/25%	6/30%	1/5%	0/0%	5/25%	35
Regional companies do not meet the requirements of foreign companies related to the certification of management systems	3/15%	4/20%	4/20%	1/5%	1/5%	7/35%	30

At the same time, only half of the surveyed organizations provide support for the development of cooperation between foreign companies and their potential suppliers among local enterprises. It shows that the development of FDI linkages is not among the key priorities for the regional business support infrastructure in the regions (moreover, taking into account the fact that many of the surveyed organizations represent regions with a high number of FDI localization projects). In the cases when such support is provided, it takes the form of irregular and non-systematic actions, such as:

- organization of B2B matchmaking events with the participation of foreign companies and potential suppliers,

- promotion of regional companies at various events and through publications/catalogs, organization of business missions to other countries
- organization of delegations abroad.

For example, the Center for Public-Private Partnership and Investment Promotion in the Altay region provided support for PepsiCo in the search for suppliers of raw materials for the company's cheese production plant. The center also assisted the company Grundfos in the selection of local suppliers for cast iron pump casings and packaging materials.

Thus, there may be a need for the provision of intensive assistance to the regional business support organizations in order to help them to introduce well-designed and systematic action plans aimed at the development of FDI linkages. To analyze the demand of the regional business support infrastructure in such ways, the organizations were also asked if they need external non-financial support for the development of cooperation between foreign companies localized in Russia and their potential suppliers from the regions where the organizations are located. Most of the respondents (85%) answered that they need such support. The surveyed organizations also indicated the importance of various directions of external support on a scale from 1 to 5 (where 5 is the maximum), as per the table below (the variants that received the highest number of responses are highlighted in bold):

Table 12. External non-financial support necessary for the surveyed organizations

Support direction	Number / share of organizations answered					Total result = sum of the number of responses for each point multiplied by the points on the scale
	1	2	3	4	5	
Collection / analysis of information about the demand of foreign companies localized in Russia in the supplies of raw materials, material inputs, and services	1/5%	0/0%	3/15%	5/25%	11/55%	85
Analysis of global markets (value chains) for the search of priority segments for the companies of your region in the long-term perspective	1/5%	1/5%	1/5%	9/45%	8/40%	82
Support in the organization of meetings of the regional enterprises and foreign companies	1/%	1/5%	3/15%	8/40%	7/35%	81

Support direction	Number / share of organizations answered					Total result = sum of the number of responses for each point multiplied by the points on the scale
	1	2	3	4	5	
Search for information about foreign companies	1/5%	2/10%	3/15%	5/25%	9/45%	79
Collection / analysis of information about the requirements of foreign companies localized in Russia related to the quality of purchased material inputs, and services, requirements to management systems, etc.	1/5%	4/20%	1/5%	6/30%	8/40%	76
Creation / development of a database of potential regional suppliers for foreign companies (or entering the data about the potential suppliers to other databases)	2/10%	2/10%	2/10%	6/30%	8/40%	76
Support in the organization of B2B events for the development of cooperation with foreign companies	1/5%	1/5%	4/20%	9/45%	5/25%	76
Development of cooperation with international organizations (including bilateral trade chambers) in this area	2/10%	2/10%	4/20%	2/10%	10/50%	76
Development of cooperation with the federal authorities and development institutions on the work in this area	1/5%	3/15%	2/10%	7/35%	7/35%	76
Training in the area of developing cooperation with foreign companies	3/15%	3/15%	2/10%	4/20%	8/40%	71

Support direction	Number / share of organizations answered					Total result = sum of the number of responses for each point multiplied by the points on the scale
	1	2	3	4	5	
Support for the development of the export activity of companies in your region	3/15%	0/0%	8/40%	5/25%	4/20%	67
Support in the search for highly-qualified specialists for the work in the area of developing cooperation between foreign companies and the enterprises of your region	2/10%	5/25%	5/25%	4/20%	4/20%	67
Support in the implementation of supplier development programs in your region	3/15%	4/20%	6/30%	3/15%	4/20%	61

The answers show that the most demanded support directions for the regional business support institutions in the area of FDI linkages are:

- Collection / analysis of information about the demand of foreign companies localized in Russia in the supplies of raw materials, material inputs, and services;
- Analysis of global markets (value chains) for the search of priority segments for the companies of the region in the long-term perspective;
- Support in the organization of meetings of the regional enterprises and foreign companies.

It is remarkable that many of the institutions need support in developing cooperation with international organizations and more surprisingly with the federal authorities and development institutions as well. It may indicate problems in coordination of activities between the regional and federal levels, and with international organizations such as bilateral trade chambers. In general, all activities aimed at the development of cooperation with MNCs are demanded by the surveyed institutions. This supports the conclusion that these institutions do not have enough information (including information about the global markets), competencies, contacts and resources to provide effective assistance in the development of FDI linkages.

Most of the surveyed organizations also expressed their opinion on possible measures that the federal authorities could introduce to facilitate the development of cooperation between foreign companies localized in Russia and their potential Russian suppliers. The recommendations include:

- Dissemination of the best Russian practices of work with foreign investors (for example, the multifunctional center for investors www.welcomecenter.ru).
- Providing subsidies for the creation of ready standard production facilities for foreign investors and their suppliers. The subsidies should be provided to the regional development institutions as the main entry points for foreign investors in working with the Russian regions.¹⁵⁹
- Implementing programs to support the outsourcing of components' production in Russia for foreign companies. These programs may include activities aimed at technological upgrading, development of staff skills, and increasing the production volumes (for example, thanks to export promotion).¹⁶⁰
- Informing Russian suppliers about the opportunities of cooperation with foreign companies (for example, creation and promotion of a specialized B2B Internet platform at the federal level to facilitate communication and provide information and analytical materials).
- Design of simple and clear localization criteria and requirements to products produced under the "Russian product" label.
- Improve the communication with the Russian trade representation offices abroad (this problem is especially acute when communicating with the offices in Arab countries).
- Analysis of the demands of foreign companies.
- Development of cases related to the creation of new or upgrading of existing companies to satisfy the demands of MNCs.
- Organization of business missions, presentations, B2B events.
- Training for Russian companies, for example, in the area of design and innovation.
- Export development (coordination of export support under the Russian Export Center; providing support for regional export support centers; motivating Russian trade representation offices abroad to export development on the basis of clear KPIs – growth of volume of export to a given country, and growth of foreign investment to Russia from a country where the office is located).
- Creation of special divisions in regional governments that are responsible for interaction with foreign companies.
- Visa support.
- Analysis of goods and services of foreign markets to support/inform potential investors.
- Implementation of programs to stimulate manufacturing upgrades, and subsidize regional costs for the development of industrial infrastructure.

¹⁵⁹ In the situation of sanctions, foreign investors need ready high-quality brown-field production sites, in order not to risk long-term capital investments in main assets.

¹⁶⁰ Russia lacks suppliers able to produce components with good quality and low prices, and in many cases, foreign companies have to import such components.

- Harmonization of the Russian legislation with the legislation of primary trade partners.
- Softening of the state's external policy and sanctions;
- Improvement of relationships with other countries.
- Participation of the country leaders in inviting foreign companies to the Russian regions (and not only to Moscow and the Moscow region).

Thus, recommendations of the surveyed organizations cover many areas such as foreign policy issues, export development, support for the creation of infrastructure for investors, and development of the competitiveness of Russian suppliers. The surveyed organizations also provided some examples of the best practices of the business support infrastructure in their regions on the development of FDI localization and cooperation between MNCs and Russian suppliers:

- Multifunctional centers (single windows) for foreign investors (Krasnodar region).
- Creation of an industrial park for the Austrian company "Kronospan" and the provision of support for local companies – partners of Kronospan (Republic of Bashkortostan).
- Creation of databases/catalogues of products/services of the regional companies (example - Voronezh region) to inform MNCs about the potential suppliers.
- Cooperation with a foreign company (PepsiCo) to substitute foreign suppliers with local ones (Rostov region).
- Creation of a coordination and expert center for a given sector – the case of the Republic of Tatarstan. The center (Tatneftekhiminvest-holding) supports the enhancement and effectiveness of the regional oil and gas sector, designs measures for the exploitation of the region's scientific potential in the area of oil and gas, actively cooperates with Russian and foreign scientific institutions, and informs local companies about new technological solutions.
- Establishment of a center on the coordination of activities for the competitiveness enhancement of the regional enterprises (Leningrad region). The center works in the following directions: development of clusters and industrial cooperation, export support, development of productivity and staff skills.
- B2B meetings with foreign companies localized in Russia.
- Informational promotions of regional companies through mass media.
- Creation of industrial clusters and development of cooperation in the clusters.
- Organization of the Days of Suppliers (MNCs localized in the regions invite Russian and foreign companies to participate in these events and consider the opportunities to enter the supply chains of such MNCs).
- Cooperation between MNCs and local educational institutions to train staff for their plants and conduct contract R&D.

Annex 4. Questionnaire for the online survey of regional investment agencies and development corporations

1. Please, provide the full name of the organization.
2. Please, provide the name of the region where the organization works.
3. Please, indicate the number of staff at the organization:
 - 10 and less
 - from 11 to 20
 - from 21 to 35
 - from 36 to 50
 - from 51 to 70
 - 71 and more
4. Please, provide your contact details for the clarification of additional questions (if any) on the subject of the survey:
 - Full name
 - Phone
 - E-mail
5. Please, indicate the companies your organization works with the most actively:
 - Large companies
 - Medium-sized companies
 - Small companies (including micro-companies)
 - Other _____
6. Please, describe the target groups of clients of your organization (for example, SMEs, enterprises of a certain sector, etc.).
7. Please, describe briefly the main services provided by your organization to the target groups of clients.

8. Please, indicate, which services are provided by your organization on a fee basis, for free or not provided at all?

Services	Provided for free	Provided on a fee basis	Not provided
Provision of information about the region, including that about the sectors and potential partners			
Selection of a land plot and organization of a deal on the sale and purchase of the land plot			
Assistance in the undergoing of administrative procedures (for example, obtaining permissions and licenses)			
Help with receiving state support (including that from the federal development institutions)			
Attraction of financial resources (investments, loans)			
Design of business plans			
Market studies			
Help in the preparation of innovative projects (including cooperative projects)			
Support in the preparation of			

investment projects
(including cooperative
projects)

Training

Support in the
development of
management systems

Support in the search
for personnel

Support with
accounting / legal
issues

Provision of premises

Provision of equipment

Support in the
promotion of
goods/services in the
Russian market

Support in the
organization of sales of
products/services to
foreign companies,
including foreign
companies localized in
Russia

Support in the
promotion of
products/services in
the foreign markets

Other (please, describe)

9. Please, indicate, if your organization has the status of a specialized organization in your region responsible for the development of cooperation with foreign companies (including those that localized in Russia):

- Yes, the status is given only to our organization
- Yes, but this status is given also to other organizations in the region
- No, we do not have such an organization in the region
- No, the status is given to another organization

10. Does your organization provide support for foreign investors in the preparation and/or implementation of investment projects on manufacturing localization in your region??

11. If yes, please indicate the directions of such support and provide the examples of foreign companies that received this support.

12. Does your organization provide support in the development of cooperation between foreign companies (including the companies that localized the production in your region) and their potential suppliers among the enterprises of your region?

13. If yes, please describe the directions of such support and provide the examples of your organization's work in this area (for example, organization of B2B events, preparation of a catalogue of suppliers, etc.).

14. Please, indicate how many specialists of your organization are involved in the development of cooperation between foreign companies and potential suppliers from your region:

- 0
- 1-3
- 4-6
- 7 and more

15. Please, evaluate (on a scale from 1 to 5, where 5 is the maximum) the importance of constraints, hampering the development of cooperation between foreign companies, localized in Russia, and their potential suppliers among the companies of your region:

Constraint	Scale
	1
	2
	3
	4
	5
	Do not know

Regional
companies do not
meet the
requirements of
foreign companies

related to the
quality of
products/services

Regional
companies do not
meet the
requirements of
foreign companies
related to the price
of
products/services

Regional
companies do not
meet the
requirements of
foreign companies
related to the time
of delivery of
products/services

Regional
companies do not
meet the
requirements of
foreign companies
related to the
certification of
products/services

Regional
companies do not
meet the
requirements of
foreign companies
related to the
certification of
management
systems

Regional
companies do not
meet the
requirements of
foreign companies

related to the
management
competencies

Regional
companies do not
meet the
requirements of
foreign companies
related to the level
of staff skills

Lack of
communication
with foreign
companies in order
to get information
about their
demands

Low volumes of
procurement by
foreign companies

Cooperation with
foreign companies
requires big
investments to the
modernization of
production at the
regional
enterprises

Material inputs,
required by foreign
companies, cannot
be supplied by the
regional
enterprises

The search for
foreign companies
– potential buyers
– and organization
of cooperation
with such

companies require
too much time

Regional
enterprises do not
have enough
capacity in the
area of design and
innovation to
become effective
partners for
foreign companies

Low volumes of
production by the
regional
enterprises to
meet the
requirements of
foreign companies

Other (please,
describe)

16. Does your organization need external non-financial support for the development of cooperation between foreign companies, localized in Russia, and their potential suppliers among the regional companies?

17. If yes, please indicate the importance of each direction of such support on a scale from 1 to 5, where 5 is the maximum:

Support direction	Scale
	1 2 3 4 5
Analysis of global markets (value chains) for the search of priority segments for the companies of your region in the long-	

term
perspective

Support for
the
development
of the export
activity of
companies in
your region

Development
of cooperation
with
international
organizations
(including
bilateral trade
chambers) in
this area

Development
of cooperation
with the
federal
authorities and
development
institutions on
the work in
this area

Training in the
area of
developing
cooperation
with foreign
companies

Support in the
search for
highly-
qualified
specialists for
the work in the
area of
developing

cooperation
between
foreign
companies and
the enterprises
of your region

Search for
information
about foreign
companies

Collection /
analysis of
information
about the
demand of
foreign
companies,
localized in
Russia, in the
supplies of raw
materials,
material
inputs, and
services

Collection /
analysis of
information
about the
requirements
of foreign
companies,
localized in
Russia, related
to the quality
of purchased
material
inputs, and
services,
requirements
to
management
systems, etc.

Creation/
development
of a database
of potential
regional
suppliers for
foreign
companies (or
entering data
about the
potential
suppliers into
other
databases)

Support in the
organization of
B2B events for
the
development
of cooperation
with foreign
companies

Support in the
organization of
meetings
between the
regional
enterprises
and foreign
companies

Support in the
implementation
of supplier
development
programs in
your region

Other (please,
describe)

18. Please, provide your recommendations for the federal authorities on the support measures that may facilitate the development of cooperation between foreign companies, localized in Russia, and their potential suppliers among the companies of your region.
19. Please, briefly describe the best practices (in your opinion) of the business support infrastructure in your region on the development of FDI localization and cooperation of foreign companies and Russian suppliers.

Annex 5. FDI Linkages Questionnaire: MNC Demand Analysis

About Interviewer and Survey Background

Full name of Interviewer:

Interview begins at _____ and ends at _____ Total time: ____ mins

QID:

Date of Interview: Day: _____ Month: _____ Year: 2019

If any, calls made to follow up on questions:

Name of supervisor:

Comments:

Signature and Date of Approval by Supervisor:

Introduction: Hello, my name is_____ I am working for the World Bank to conduct a study on linkages between foreign investors and SMEs in Russia. Thank you for participating in this interview.

This survey aims to determine the potential scope to increase local sourcing by foreign investors in Russia, of course, while appreciating the realities of global production networks and sourcing needs of foreign firms. The survey analysis should serve three purposes:

- 1) Help foreign investors to capture the local production capacity, improve their sourcing experience and share their thoughts on what government services should be provided
- 2) Help local companies to understand in what areas they have to improve performance to meet the requirements of foreign investors and what market opportunities this would create
- 3) Help the Government of Russia and the regions in the design of a concrete action plan to remove any remaining barriers faced by foreign investors interested in sourcing locally and to extend targeted support to local companies to ultimately increase linkages and business between foreign investors and Russian companies.

The information obtained through this survey will be handled as strictly confidential and no individual company data will be presented or released in any form as part of the analysis or final reports. Data obtained will be aggregated and analyzed for the above mentioned purposes only. Participants will receive an email copy of the final report.

The interview should take about 45 minutes. With your permission, can we begin now?

Instruction to Interviewer:

- Please be alert to actively use the “Other”-category to get more detail and also ask if there are responses missing in the list provided
- Collect interesting remarks, statements or references mentioned by the firm that can be quoted in the final report and the case studies to substantiate the findings and highlight concrete issues.

A. Current Sourcing Pattern

Q1. a) Please indicate the **main product(s)/service(s) that this facility produces** and please rank them according to the sales volume:

1 Product/Service	2 What sector does this product feed into?	3 Is it a final product/service? (underline the answer)	4 HS (4 digits)
1.		1= Yes 2= No	
2.		1= Yes 2= No	
3.		1= Yes 2= No	
4.		1= Yes 2= No	
5.		1= Yes 2= No	

b) Where do you **sell your products to**? Please indicate share of output sold:

1 Destination of output	2 Estimate share of total sales (2018) in %
1. To consumers in Russia	_____ %
2. To firms in Russia	_____ %
3. To other countries (consumers and/or firms in total)	_____ %
TOTAL	100%

Q2. What are the **primary markets** for the output of this facility?

Destination	Estimate of total sales (2018) in %
(1) Domestic sales in Russia	
(2) Exports to the CIS countries	
(3) Exports to the EU	
(4) Exports to North America	
(5) Exports to China	
(6) Exports to India	
(7) Exports to other Asian countries	
(8) Exports to Africa	
(9) Exports to South America	
(10) Other:	
TOTAL	100%

Q3. Why did the company set up in Russia?

Please name your top 3 reasons:

1) _____

2) _____

3) _____

Q4. a) Do you expect to expand your operations in the next three years? 1= Yes 2= No

b) Why? (OPEN): _____

Q5. a) Would you mind to tell us the estimated total - both imported and domestic - purchase value of material inputs in 2018?

US\$

b) What is the share of each item?

1	2	3
Material	HS (4 digits)	% Total purchase of material inputs in 2018
(1)		
(2)		
(3)		
(4)		
(5)		

[for interviewer: Q5 is particularly relevant for the manufacturing industries, especially:
automotive components, bicycle assembly, electronic/electrical components and machinery,
household appliances, machinery & equipment, rubber & plastic parts, steel processing]

Q6. What material **inputs** do you import?

1	2	3a	3b	3c
Material	Share (% total purchase of material inputs)	Main sourcing countries		
1-				
2-				
3-				
4-				
5-				
6-				

Q7. What material **inputs** do you source **locally**?

1	2	3	4
Material	Share (% total purchase of material inputs)	Foreign supplier in Russia (% in-country)	Russian suppliers (% in-country)
1-			
2-			
3-			
4-			
5-			
6-			

Q8. a) Would you mind to tell us the estimated total - both imported and domestic - purchase value of services in 2018?

US\$ _____

b) What is the share of each item?

1	3
Service	% Total purchase of services in 2018
(1)	
(2)	
(3)	
(4)	
(5)	

Q9. What services do you import?

1	2	3a	3b	3c
Type of services	Share (% total purchase of services)	Main sourcing countries		
1-				
2-				
3-				
4-				
5-				
6-				

Q10. What services do you source locally?

1	2	3	4
Type of services	Share (% total purchase of services)	Foreign supplier in Russia (% in-country)	Russian suppliers (% in-country)
1-			
2-			
3-			
4-			
5-			
6-			

Q11. Which specific material inputs/services currently being imported would your company prefer to source locally or increase its share of local sourcing? (list in order of priority)

1	2	3	4
Product/Service	HS (4 digit)	Preferred domestic share (%)	Actively looking for local suppliers? (y/n)
(1)			
(2)			
(3)			
(4)			
(5)			

Q12. If applicable, what **processing method** do local suppliers have to be capable of?

Processing method	1	2
	Yes/no?	Actively looking for local suppliers? (y/n)
(1) Sheet work/welding		
(2) Casting		
(3) Forging		
(4) Press/stamping work		
(5) Plastic/rubber moulding		
(6) Precision moulding		
(7) Glass working		
(8) Assembling of parts/components		
(9) Surface treatment/electro plating		
(10) Machining		
(11) Heat treatment		
(12) Others: Please specify		

Q13. a) Are you sourcing any supporting services in Russia?

1= Yes 2= No

b) If yes, what **supporting services** are relatively difficult to find in Russia (with an appropriate quality/price ratio)?

Service	Rating <i>(1 = no difficulty; 2 = difficult; 3 = very difficult; 4 = not applicable)</i>
1. Transport & Logistics	1 2 3 4
2. Customs brokers	1 2 3 4
3. Packaging materials	1 2 3 4
4. Financial services	1 2 3 4
5. Repair & Maintenance	1 2 3 4
6. Engineering services	1 2 3 4
7. Warehousing & Storage	1 2 3 4
8. ICT services	1 2 3 4
9. Other services (please specify)	1 2 3 4

Q14. Where is the **sourcing decision** for procuring main inputs or services made?

Product/Service	1- Core inputs (what goes into the product)	2- Generic inputs (e.g. packaging, support material, etc.)
1. At facility/company		
2. At regional HQ		
3. At global HQ		
4. At buyer's firm		
5. Other, please specify		

Q15. a) Does your company **contract-out work to other companies**, such as manufacturing operations or business services in this country?

1= Yes

2= No

b) If yes, what products/services or activity specifically?

c) *If yes, please indicate the approximate total value (US\$) of contracted out work in the last financial year (2018):*

d) *Please also provide the nationality of these companies:*

Q16. a) Does your facility currently enjoy **customs duty exemptions on all imports** of raw materials, components or machinery? 1= Yes 2= No

b) *If yes, please specify type/input categories*

Q17. a) Does your **company currently pay VAT** on locally purchased raw materials, components or machinery? 1= Yes 2= No

b) *Please specify type/input categories*

c) If yes, please specific whether you can reclaim VAT expenses or VAT is deducted at the time of purchase:

(1) Reclaim (2) Deducted (3) None of above

B. Finding local suppliers

Q18. a) Is **increasing local sourcing considered a corporate priority** for your HQ and/or local plant management? 1= Yes 2= No

b) Why? (pls elaborate)

Q19. Which of the following factors have been **barriers for increasing sourcing from Russian companies?**

Barrier	Rating (1 = no barrier; 2 = some barrier; 3 = critical barrier; 4 = n/a)			
(1) The inputs I need are simply not available from Russian firms	1	2	3	4
(2) It is too time consuming to identify potential Russian suppliers	1	2	3	4
(3) Russian suppliers lack basic certifications needed to do business with us	1	2	3	4
(4) Potential Russian suppliers don't meet our Quality Cost Delivery (QCD) standards	1	2	3	4
(5) Russian suppliers don't have the right management capabilities to be long term suppliers	1	2	3	4
(6) Potential Russian suppliers don't have the design or innovation capabilities to be effective partners	1	2	3	4
(7) Russian suppliers don't have the production volume to meet your minimum requirements	1	2	3	4
(8) Fiscal incentives make importing a more competitive option than engaging with local suppliers	1	2	3	4
(9) Dealing with Russian suppliers is cumbersome due to VAT issues	1	2	3	4
(10) Other, please specify	1	2	3	4

Q20. a) In just a few words, what is the **company's typical approach to search, review and approval** of new suppliers? [OPEN]

b) What are the **3 most important minimum requirements** that Russian companies have to meet in this process? [OPEN]

1) _____

2) _____

3) _____

[List for guidance in case respondent does not understand or have no ideas]

- *International certifications: Please list:* _____
- *Technology and machinery*
- *General management capability*
- *Language fluency of management: Please specify:* _____
- *Financial stability*
- *Current QCD performance]*

Q21. What is your **main source of information** when searching for potential in-country suppliers?

- (1) Internet search
- (2) Other investors
- (3) Special economic zone management
- (4) Commercial owned company database

- (5) Government owned company database
- (6) Local chamber of industry/commerce
- (7) Sector association
- (8) Foreign bi-lateral chamber of commerce (e.g. Amcham, German chamber, etc)
- (9) Other, please specify _____

Q22. a) Have you provided or planned to provide any support to Russian firms?

1= Yes 2= No

b) If yes, please indicate what kind of support you provide.

[for interviewer: options of support generally are

- technical assistance: training, advisory services, help with drawing/design, R&D
- financial assistance: credit or equity participation,
- managerial assistance: training, advisory services
- supply assistance: material and parts, die and mould, facilities, etc.]

Q23. What do you believe are the **5 most critical development needs of Russian firms**/suppliers?

[UNPROMPTED, Referencing to Q19 above]

Development needs of local firms	Listing
(1) Management skills	
(2) Quality management	
(3) Technical skills of employees/workers	
(4) Production efficiency (productivity)	
(5) Cost competitiveness	
(6) Upgrade equipment and/or technology	
(7) Customer service	
(8) Innovation capacity	
(9) Scale of production	
(10) Other: Please specify	

Q24. a) Are you encouraging any of your current **overseas suppliers to consider relocating to Russia?** 1= Yes 2= No

b) If yes, please elaborate what inputs (material and services) specifically (HS code if possible)?

c) If yes, what is their feedback? Please elaborate

C. Government support services

Q25. a) Are you aware of the existing support infrastructure or **received any support from government and/or donor partners** to help sourcing from Russian companies in your operations? 1= Yes 2= No

b) Are you in particular familiar with the following support instruments:

Support policies / programs / instruments

1 = Yes, 2 = No

Special investment contracts

Funds provided by the Industry Development Fund

Guarantees etc. (also linked with IDF products) provided by SME (MSP) Corporation

Certification for the label "Russian product"

Industrial infrastructure (industrial parks, etc.)

Special economic zones / Territories of accelerated development

Industrial information system

Regional development organizations

c) If yes, please indicate the most useful support, programs or policies you benefitted from?

Q26. If the government would like to encourage you to increase sourcing from Russian firms, what **type of support services** would you need? [open]

Intervention	List
(1) Availability of a high quality supplier database	
(2) Organisation of targeted B2B matchmaking events (meet the buyer, speed dating, etc.)	
(3) Introduction of supplier capacity development programs	
(4) Financial benefits to foreign investor to encourage local sourcing	
(5) Financial benefits to foreign investor for training of local suppliers	
(6) Financial benefits for local suppliers to invest in upgrading	
(7) Other, please specify	

Q27. If the government decided to design a **program to upgrade** the capacity of Russian firms to meet the requirements for supplying to foreign investors, would you be willing to **work in partnership with Government agencies, for example** by participating in workshops, providing quality know-how to companies, identifying opportunities for local supply or running trial orders, etc.?

1= Yes

2= No

Q28. a) Would a **national supplier database** (to minimize effort and cost for finding prospective local suppliers) be **useful** for you?

1 = Yes; 2= No

b) *If yes, what information* should be provided for each supplier profile to make it a helpful tool from a procurement manager standpoint?

Information included in database	List
(1) Main products/services produced	
(2) Main clients/buyers (domestic and abroad)	
(3) Certification	
(4) Core machinery and equipment used	
(5) Year of establishment	
(6) Production capacity per year	
(7) Number of employees	
(8) Annual turnover	
(9) Tax payer number	
(10) Other: Please specify	

Q29. a) Are you willing to **participate in future B2B matchmaking events**? (e.g. Meet-the-buyer, factory tours, trade fair, speed-dating, etc.)

1= Yes 2= No

b) *If yes, please elaborate how this event should be organized to be most useful:*

Q30. What would be the **most impactful and realistic policies, actions or strategies** you would suggest to the Government of Russia in order to increase sourcing from and competitiveness of Russian suppliers? [Based your opinion, what are the most effective strategies for the government to increase local sourcing and competitiveness of Russian suppliers?]

Please elaborate:

D. General firm characteristics for follow-up

Q31. Full name of the MNC:

Q32. Established in Russia in the year: _____

Q33. Location of the Company:

Q34. a) What is the nationality of the majority shareholder? *Please indicate nationality:*

b) Percentage of Russian ownership: _____ %

Q35. Where is the HQ of your parent company located? Country: _____

Q36. What are the parent company's main services or products sold globally?

Q37. How many permanent employees do you have?

Location	No. (2016)
1 In this facilityemployees
2 In the countryemployees

Q38. Would you primarily classify yourself as an assembly or production facility?

1- Assembly	
2- Production	

Q39. Does your firm hold ISO certification (e.g. 9000, 9001, 14001, 22000), other internationally recognized certifications (e.g. HACCP), or report on compliance (e.g. apparel: SEDEX, BSCI)?

(1) None

(2) ISO 9000

(3) ISO 9001

(4) ISO 14001

(5) ISO 22000

(6) HACCP

(7) Other, specify:

Q40. If the government decided to support a supplier development program (targeted and competitive interventions to upgrade the skills and capacity of suppliers to meet your needs), what Russian suppliers would you recommend as priority for inclusion?

1	2	3
Company name	Input (product/service)	Location
(1)		
(2)		
(3)		
(4)		
(5)		

Q41. If possible, please provide the following information on your most important local suppliers or sub- contractors for main inputs and services for inclusion in a national supplier database:

[if this is sensitive information especially regarding foreign suppliers, please ask to give the information at least answer for local suppliers]

1	2	3	4	5
Company name	Input (product or service)	Location	Nationality	Contact details
(1)				
(2)				
(3)				
(4)				
(5)				

Q42. If possible, please provide us the name of supplier company recognized by your buyers (e.g. YKK for zipper, etc.)

- (1) _____
- (2) _____
- (3) _____

E. Afterinterview

Notes to interviewer:

Please write down any interesting quotes, remarks, or statements made by the interviewee that will help substantiate the data and can be included in the final report.

Request business card of the person interviewed for records and potential follow-up questions when processing data.

--- **End** ---

Annex 6. Background information from the SME Corporation

JSC RSMB Corporation implements activities in order to facilitate the integration of Russian SMEs into the supply chains of FDIs with the support of foreign chambers of commerce, agencies for promotion of enterprises on foreign markets and other development institutions. These activities are aimed at market expansion, as well as at increase in the competitiveness of Russian SMEs.

RSMB Corporation implements the following procedure, in compliance with the approved internal regulations, according to the requests of foreign companies:

- Scouts for the potential suppliers among Russian SMEs using the Unified Register of SMEs of the Russian Federation, information from the executive authorities of constituent entities of the Russian Federation, regional SME support organizations, public organizations, and other sources;
- Analyzes the information received to determine the base of high potential suppliers among the SMEs;
- Organizes B2B matchmaking events for initial negotiations with potential suppliers - SMEs;
- If necessary, provides credit, financial, informational, and other support to SME development projects to help them meet the requirements for the suppliers determined by FDIs.

It is important to note that the particular emphasis of the abovementioned ongoing work is put on finding and attracting SMEs mostly from those regions of the Russian Federation that require additional assistance in the realization of their underdeveloped potential in the field of industrial cooperation of SMEs with large companies.

To date, RSMB Corporation, together with the following companies with foreign participation, has signed 12 "roadmaps" of integrating SMEs into their supply chains:

- in the production of building materials with Saint-Gobain Building Products Rus LLC (France);
- in the field of engineering with LLC WILO RUS (Germany), LLC GEA Refrigeration RUS (Germany), JSC WIKA MERA (Germany), LLC CLAAS (Germany);
- in the automotive industry with Schaeffler Manufacturing Rus LLC (Germany),
- in the metalworking industry with Heunisch GUSS GmbH (Germany),
- in the food industry with Unilever Rus LLC (Great Britain / Netherlands) and LLC Symrise Rogovo (Germany).
- in the chemical industry with BASF LLC (Germany)),
- in the production of medical devices with ABISS (France),
- in the production of container structures: LLC ELA Container RU (Germany).

A road map has also been signed with the Japan Foreign Trade Development Organization (JETRO), which interacts with 8 Japanese companies involved in the automotive industry and mechanical engineering.

As a result of financial and non-financial support provided RSMB Corporation in 2017-2018, many SMEs implemented projects of expansion of the existing enterprises and created new industries. These included:

- LLC Fragaria implemented an import-substituting project for the cultivation of garden strawberries and the subsequent production of frozen products for such prominent clients as Danone (France);
- LLC MagistralInvestBor built a plant for the broken glass recycling in the Moscow region, which supplies its products to LLC Saint-Gobain Building Products Rus (France);
- LLC Hermes-Ural implemented a project for the organization of the capacitive equipment production, which allowed the company to become a certified supplier of GEA Refrigeration RUS LLC (Germany);

- Cooperative Yagody Karelii implemented a project for the production expansion and, as a result, became a Nestle (Switzerland) supplier.

RSMB Corporation expands its activity in the field of facilitating the integration of Russian SMEs localizing their production in the Russian Federation into the supply chains of foreign companies. Future activities will be carried out in the following areas:

- expanding the base of potential suppliers by facilitating the localization of foreign small and medium enterprises in the territory of the Russian Federation, of traditional suppliers of MNCs that localized their production in Russia, including through the SPIC mechanism with legislative novelties allowing its use by small and medium enterprises;
- Improving the efficiency of the foreign SMEs' decision-making on the localization of their production in Russia through the expansion of the functionality of the information and analytical portal SME Business Navigator, developed by RSMB Corporation. As part of the integration of the State Industry Information System (GISP) and the SME Business Navigator, a new production module for calculating market niches and sample business plans for 40 types of production business with 84 types of industrial products, has been developed. The new production module includes businesses in the chemical, medical industry, metallurgy, machine building, timber industry, building materials industry, electronics, and waste processing;
- providing financial and non-financial measures to support existing suppliers of foreign companies that localized enterprises on the territory of Russia, to expand their production and/or the range of their products for subsequent supply to other foreign companies having production in Russia;
- dissemination of the mechanisms of the supplier development program implemented by JSC RSMB Corporation jointly with the constituent entities of the Russian Federation. This is aimed at forming a pool of potential regional suppliers of foreign companies and creating a productive work system in the regions and municipalities to conduct activities for their development;
- use of leasing tools let by the RSMB Corporation Regional Leasing Companies (JSC RLC of the Republic of Tatarstan, JSC RLC of the Republic of Bashkortostan, JSC RLC of the Yaroslavl Region, JSC RLC of the Republic of Sakha (Yakutia)). This will aid at the quick meeting of the demand in new production equipment for the potential or existing suppliers of foreign companies. It is important to note that these leasing companies can process projects from any Russian region;
- Expansion of cooperation with partner organizations from the EAEU¹⁶¹ countries resulting in the selection of potential suppliers from these countries and organization of their interaction with foreign companies localizing their production in the Russian Federation.

¹⁶¹ EAEU – The Eurasian Economic Union – is the economic union of such countries as Armenia, Belarus, Kazakhstan, Kyrgyzstan and the Russian Federation

Annex 7. Report on the interviews with SMEs

KEY FINDINGS

- According to the analysis, many **small and medium companies that operate in machine building also mention motor industry as the distribution area for their products / services**. This industry specifics is manufacture of software, simple products / parts, design services etc.
- For chemical industries it is typical to manufacture paint, varnish and lacquer for construction, petrochemistry, shipbuilding, carriage building, nuclear and power industries, chemical agents for biotechnologies and diagnostics, chemical raw materials and industrial chemistry, main organic and inorganic chemicals etc.
- **This sector's specifics is manufacture of raw materials as an end product.** According to the research results, in the chemical industry the market of FDI companies is growing in general, however it is a market of low technological products and services. The companies manufacture end products that are distributed in the local market.
- As for machine building and motor industry their end products are less demanded due to low purchasing power of individuals and legal entities.
- Only three respondents mention, that they do not supply their products / services to FDI companies or export. **However they all confirmed, that they are absolutely ready to export and/or work with global companies operating in the territory of Russia.**
- The majority of the respondents either work with FDI companies or export their products / services or both.
- According to the research, **the experts do not mention any special requirements to cooperation with FDI companies. However they identify several specific features of such cooperation.** They are as follows: certification, scheduled auditing, registration in Provider Identifiers, compliance with labor condition requirements etc. It should be noted, **that similar requirements are also mentioned by global companies in case of exporting products / services from the Russian Federation.**
- **Among the key advantages** that help Russian companies to cooperate successfully with FDI companies are as follows: **good value for money, logistics, fast responding to clients' requests.**
- Among the barriers that prevent from working with FDI companies the respondents mentioned the following: **some types of products are not in demand** (this refers basically to hi-tech products /services, e.g. software, compound products and their components, design etc.) Also, **some Russian companies do not pass audit of FDI companies.** Among other barriers we could mention **insufficient communication and information about such companies.**
- However, some part of businesses not working with FDI companies expressed their opinion, that **exporting would be more attractive to them vs. work with FDI companies in RF**, as **FDI market is rather limited.**
- So, **in terms of development, Russian companies pursue entering a broader and more promising global market**, because export means revenues in foreign currency, which helps to neutralize the results of the local crisis

- **As for exporters they believe their key advantages to be as follows:** high quality and/or uniqueness of their products, good value for money, cutting-edge scientific developments, scientific potential.
- Some part of TA mentions various barriers they have to face in the process of exporting their products/services. **The most significant are such barriers as anti-Russia policy in general, economic sanctions, blocking of foreign currency accounts, problems with customs authorities, paperwork etc.**
- According to the research, **the majority of surveyed companies do not obtain any technical or financial support from the state, NGO or other structures for the purposes of raising their potential in the sphere of cooperation with global companies.** Some companies have a negative experience of communication with government structures in the process of obtaining potential state support or subsidies.
- Only a small part of companies mentioned a positive experience in this area. Among the mentioned support the following examples were given: subsidies of the Ministry of Industrial Development, Skolkovo grants, Bortnik Fund program. **The utmost support from the state is the companies' residency in Skolkovo.**
- Talking about increasing potential opportunities as global vendors, the respondents mention different kinds of government support. The most demanded are as follows: events, where you might meet global companies' representatives / introduce yourself to potential clients. One of the mentioned measures is financial benefits (to global companies that purchase resources from local vendors, to local vendors for investments into modernization (which is critical for small and medium companies). Among other measures they mention VAT return procedure for supplies to global companies and improvement of business environment for local companies in general.
- **Among the key barriers that small and medium companies face in Russia**, the experts mentioned access to finances, lack of understanding of state regulations, problems with following regulation requirements, high operational costs, lack of qualified employees, strong competition etc.
- **So the most efficient and realistic measures to be implemented by the government are investments, support by the government, financial benefits, simplified taxation, simplified customs procedures and certification, simplified currency control.**
- It should be noted, that **small and medium companies take some measures that help them to work with global companies.** Among them ISO certification could be mentioned, as well as participation in global conferences, organization of English classes for employees, customer management trainings, other qualification events.
- However, the companies mention a number of restricting factors of global partnership potential development. They are training costs, off-the-job trainings, concerns about staff turnover/poaching incl. to other countries.
- **As for various trade costs in case of selling products or buying resources, time is the biggest restriction.** Among the key reasons for delay during export / import operations in case of delivery within Russia the respondents mentioned customs and export control, currency control and bank transaction delays as well as holidays and a human factor.
- Based on the analysis, **the most popular and demanded channels for marketing and advertising communication are as follows:** website, fairs / exhibitions. Among the important info channels the respondents also mentioned other companies' references, specialized print media, industry magazines, online ads, scientific events, work with industry associations.

Approved
General Director, MAGRAM MR.

Malykhina M.A. _____



ANALYTICAL REPORT

Study of industrial interaction and cooperation between global investors operating in Russia's market and their vendors, i.e. local small and medium companies



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RESEARCH DESCRIPTION

METHODOLOGY



Goal – identify the growth potential of local suppliers' share in procurement of global companies that have manufacturing facilities in the territory of Russia

Objectives:

- Collect opinions of small and medium companies about the problems that prevent their entering supply chains of major global companies in Russia
- Formulate the current key problems of industrial cooperation with global manufacturers, from the SMB positions; in what areas the efforts of the process participants incl. state authorities are needed

Data collection method: 15 IDIs

- Duration of 30-40 minutes. Audio recording with further transcribing and analysis
- Interviews are performed by an experienced moderator with the deep knowledge of the subject, based on the specially developedIDI guide (scenario)

Target audience, sample and geography

- Small and medium companies in the following sectors: motor industry, chemical industry, machine building
- The companies are suppliers of global companies operating in Russia
- The companies would like to become suppliers of global companies operating in Russia

PARTICIPANTS DESCRIPTION

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TARGET AUDIENCE

INDUSTRY	AREA OF FOCUS	COVERAGE
MOTOR INDUSTRY / MACHINE BUILDING	Computer simulation and high end calculation	GLOBAL + FDI
MOTOR INDUSTRY / MACHINE BUILDING	Software development for engineering design	GLOBAL + FDI
MOTOR INDUSTRY / MACHINE BUILDING	Manufacture of 3D printers	GLOBAL + FDI
MACHINE BUILDING	Design, manufacture, modernization, maintenance of CNC for all processing machines' groups	RF
MACHINE BUILDING	Manufacture of oil products, special grease for motor industry, defense industry, machine building	RF + FDI
MACHINE BUILDING	Manufacture of components for metal industry, heavy machine building	GLOBAL + FDI
MACHINE BUILDING	Manufacture of industrial machinery	GLOBAL
CHEMICAL INDUSTRY	Manufacture of paint, varnish and lacquer for construction, petrochemistry, shipbuilding, carriage building, nuclear and power industries	RF + FDI
CHEMICAL INDUSTRY	Manufacture of chemical agents for biotechnologies and diagnostics	GLOBAL + FDI
CHEMICAL INDUSTRY	Software development	RF
CHEMICAL INDUSTRY	Development and commercialization of unique hydrometallurgical technologies	RF + FDI
CHEMICAL INDUSTRY	Manufacture of chemical raw materials and industrial chemistry	RF
CHEMICAL INDUSTRY	Manufacture of the main organic and inorganic chemicals	GLOBAL + FDI
CHEMICAL INDUSTRY	Manufacture of chemical products and ad hoc solutions for the construction materials' market	GLOBAL + FDI
CHEMICAL INDUSTRY	Development and manufacture of a full range of household chemicals/industrial chemicals	GLOBAL + FDI

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RESEARCH FINDINGS



TA TYPES

TA TYPES

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MACHINE BUILDING

- Computer simulation and high end calculation
- Software development
- Design, manufacture, modernization, maintenance of CNC for all processing machines' groups
- Development and commercialization of unique hydrometallurgical technologies

MOTOR INDUSTRY

- Software development for engineering design
- Manufacture of oil products, special grease for motor industry, defense industry, machine building
- Manufacture of components for metal industry, heavy machine building

CHEMICAL INDUSTRY

- Manufacture of paint, varnish and lacquer for construction, petrochemistry, shipbuilding, carriage building, nuclear and power industries
- Manufacture of chemical agents for biotechnologies and diagnostics
- Manufacture of chemical raw materials and industrial chemistry
- Manufacture of main organic and inorganic chemicals

KEY INFO ABOUT SMB

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ISO CERTIFICATION

- The majority of surveyed companies have been certified according to ISO standards, mainly ISO 9001 and 9000
- One third of the surveyed companies have no ISO certification for the following reasons:
 - ✓ No need, as we sell components, not end products
 - ✓ No ISO certification, but it does not have any negative impact



ANNUAL TURNOVER AND SIZE

- 2018 annual turnover varies from 35 MIO to 650 MIO
- The number of employees – from 10 to 100 people, except GK (supplier of special chemicals in Russia and CIS), with 400 employees



GEOGRAPHY

- The majority of surveyed companies have global coverage



RESOURCES

- Only three companies mentioned, that they use 100% of domestic resources. The vast majority import some part of resources (from 30% to 80%)

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INDUSTRY SPECIFICS

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MACHINE BUILDING / MOTOR INDUSTRY

- Many small and medium companies that operate in machine building also mention motor industry as the distribution area for their products / services. This sector's specifics is software development, manufacture of simple products/ parts, design services etc.

- ✓ Aviation and space takes over 50%. Some 20% - motor industry. The main part of motor industry is represented by Japan. I mean such companies as Toyota, Mitsubishi, Honda, Nissan. The third position is occupied by continuous operation, as we call it, and manufacturing equipment. I mean petrochemistry, metallurgy, heavy machine building. And we have clients in shipbuilding too.
- ✓ First of all, we develop software for machine building industry. Secondly, we rent computers and develop software. I mean IT sector, machine building, construction, motor building and oil industry. We offer design and resolve design issues of different companies. Computer simulation too.
- ✓ Our clients are machine building companies. They manufacture all kinds of products starting with pots & pans and finishing with jet wings or car panels. RosCosmos companies, Volkswagen Group, Transmashholding companies, it's carriage building. Russian Railways is also a part of this structure.

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INDUSTRY SPECIFICS

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CHEMICAL INDUSTRY

- Those companies are focused on manufacture of paint, varnish and lacquer for construction, petrochemistry, shipbuilding, carriage building, nuclear and power industries as well as manufacture of chemical agents for biotechnologies and diagnostics, chemical raw materials and industrial chemistry, main organic and inorganic chemicals etc.
- This sector's specifics is manufacture of raw materials as an end product.

- ✓ First of all, we provide raw materials mainly for its further processing in cosmetics industry and partially in oil industry. We also provide raw materials to the household chemicals sector. Our clients are big companies focused on cosmetics industry and household chemicals. One of the biggest companies are Henkel or Unilever.
- ✓ All our products are reactive synthetic dyes, chemical agents for biotechnologies and diagnostics. We partner with Research and with Medicine too, but in Medicine I mean those, who are focused on development of medications or wish to mark, identify and visualize some agents.
- ✓ We work with manufacturing companies, plants. Our main turnover is formed via manufacture of paint, varnish and lacquer. Manufacturers of OSB, construction, mixtures, adhesives. Food industry, confectioneries. Also raw materials for cosmetics industry and household chemistry manufacture.
- ✓ Our primary and major clients are construction sites, municipal reconstruction programs. Also new house construction across the country. Our third area of focus is end users, plants, and finally – social and state institutions, schools, kindergartens, medical centers, we provide non-combustible materials for them. This areas is developing very fast today, as the control over application of such materials is becoming more and more strict today. So it is a very good niche, quite profitable, its sales volumes are growing annually. Another product type is metal paint.

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COMPANY STATUS

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- Only three of all surveyed companies mentioned, that today they do not provide their products / services to FDI (Foreign Direct Investments) companies in RF and do not export. But they confirmed that they are ready to export and partner with global companies operating in the territory of the Russian Federation
- The rest of the companies were split as follows:

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WORK WITH FDI COMPANIES AND EXPORT

▪ 6 of all surveyed companies

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WORK WITH FDI COMPANIES

▪ 3 of all surveyed companies

3

EXPORT

▪ 3 of all surveyed companies

WORK WITH FDI COMPANIES

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SPECIFICS OF WORK WITH FDI COMPANIES

- The top managers of the surveyed companies do not mention any special requirements to cooperation with FDI companies. However they identify several specific features of such cooperation. It should be noted, that similar requirements are also mentioned by global companies when they export products / services from the Russian Federation. They are as follows:

- Certification
- Timely and scheduled audit
- Vendors should be registered in Provider Identifiers
- Vendors should comply with labor condition requirements

- ✓ First of all, we should comply with ISO and all global requirements to cosmetic products. We should be registered in the Cosmetic Ingredients Provider identifier. It is a must. The second requirement is auditing. Our clients require, that we should comply with labor regulations: no overwork, all employees should wear medical caps. They require compliance with global standards, as they are parts of global businesses and have very strict compliance rules, especially with respect to raw material suppliers.
- ✓ You should prove, that you are a reliable supplier and provide a top quality product. They also require certification and appropriate company level to prove that you are a reliable supplier. Quite regular requirements: I would not say there is something extraordinary about it.
- ✓ FDI company requested our product samples and then they considered our value for money. It was an internal bidding. They were focused on our compliance with fire protection rules and ecology. As soon as they valued our quality and reproducibility and liked our prices, they had no more questions. Actually we first had to sign some funny documents, some convention. It was about kids' labor, human rights, something like that.
- ✓ FDI companies studied our certificate, they inspected our manufacture facilities to see how well it was modernized in terms of technologies. How technologies and formulas are followed, how our accounting is maintained. Nothing extraordinary. They also work and try to fit the market, their partners and clients.

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WORK WITH FDI COMPANIES

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ADVANTAGES OF RUSSIAN PRODUCTS FOR FDI COMPANIES

- Among the advantages that help Russian companies to cooperate successfully with FDI companies are as follows:



GOOD VALUE FOR MONEY



LOGISTICS



FAST RESPONDING TO CLIENTS' REQUESTS

- ✓ Our key advantages are logistics and value for money. Our advantage is the fact that we are here. I can make pricing decisions myself. I can respond to my clients' requests fast. We have a very simple product. And our labor is cheaper here vs. Europe. The same saw or filter could be sent from China, but the quality will be lower. We have a medium quality, but the price is more interesting.
- ✓ Our prices are significantly lower vs. other companies that deliver their products from other countries, e.g. Europe. Another thing, we are fully responsible for transportation. We are responsible for delivery, schedules etc. We have our own laboratory. All claims are considered and all requirements are fulfilled. I think those factors resulted in our successful cooperation.
- ✓ We are exclusive suppliers of some kinds of products. Some kinds of products could be found in our company only. We also develop some formulas specifically for our clients. We have enough product engineers. And we have a broad line of ingredients that we are ready to provide.
- ✓ Our products comply with all parameters and quality characteristics that are required by our clients. Our products are cheaper vs. imported ones, and our clients are cost-conscious. And finally we set the whole technological process for them. If something happens, we will come and resolve all their issues. There are not so many manufacturers providing such technological support as we do.

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BARRIERS TO WORK WITH FDI COMPANIES

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BARRIERS TO WORK WITH FDI COMPANIES

- **SOME TYPES OF PRODUCTS ARE NOT IN DEMAND**
(THIS REFERS TO HI-TECH PRODUCTS / SERVICES, e. g. SOFTWARE, COMPOUND PRODUCTS AND THEIR COMPONENTS, DESIGN ETC.)
- **RUSSIAN COMPANIES DO NOT PASS AUDIT OF FDI COMPANIES**
- **INSUFFICIENT COMMUNICATION AND INFORMATION ABOUT SUCH COMPANIES**

- ✓ The reason is as follows: our products are not so well demanded by global companies that operate in Russia, as they are involved in low qualification manufacture here, i.e. assembly etc. But our mainstream is development and design of new products, parts etc. We have no market for our products here, we would rather export our product abroad. (T)
- ✓ If we take Boeing, for example, they have a narrow range of goals in the territory of Russia, and their operations here are regulated rather strictly. Major global companies would hardly approve any serious developments of vendors. They have their own super PCs, their own software and here in Russia there are no R&D centers owned by global companies. (T)
- ✓ The key barrier is auditing. Every year we communicate with them, provide our samples, they say or do not say 'OK', it depends, we are ready to work out our developments. But then they send their auditors to our company and the auditors say 'No'. That is the end of the story.
- ✓ Those companies do not need our products that much. Our products refer to hi-tech, research and development. It is our specifics. But FDI companies are focused on some other niche here. But we have a lot of export, all our products are exported. (B/D)
- ✓ We have failed to introduce ourselves to each other yet. But we believe, that our products are quite competitive.

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READINESS TO WORK WITH FDI

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READINESS OF RUSSIAN BUSINESS TO WORK WITH FDI COMPANIES

- All surveyed top managers (who do not work with FDI companies) confirmed, that **their businesses are absolutely ready to work with such companies**.
 - Some part of the respondents believe, that **exporting is more attractive to them vs. cooperation with FDI companies**, because FDI companies form rather limited market. So in terms of development, **Russian companies pursue entering a broader and more promising global market**.
-
- ✓ We are absolutely ready to work with them: we have opened our foreign currency accounts – we are ready. We expect that FDI companies should get interested in our products. And we are also ready for exporting. We had some ideas to work with Chinese companies, with DMG from Germany. We work with DMG very actively today, we have signed our agreement of intent. Another client is DANOBAT from the North of Spain. They are all manufacturers of machines and equipment.
 - ✓ I do not see any specific needs and requirements here. If you have a competitive product, you will have no problems at all. There are some companies here, working with such major players as Pepsi, Unilever etc. They just offer competitive solutions and that's it.
 - ✓ We would rather prefer exporting. In Russia — yes, it is interesting, but it would hardly evoke our investors' interest. And we do not identify FDI companies as a separate segment of Russia's market. We have ISO certification. In terms of safety and business conducting, we comply with global standards.
 - ✓ Actually we perceive them as Russian companies. The fact that they have foreign investments is their internal affair. They operate under the Russian laws. They have no restrictions to cooperation with us even in case of sanctions.

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EXPORTING

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SPECIFICS OF EXPORTERS

- Nine of fifteen surveyed companies export their products / services
- The advantages that help to export are as follows:



HIGH QUALITY OF PRODUCTS



GOOD VALUE FOR MONEY



CUTTING-EDGE SCIENTIFIC DEVELOPMENTS

- ✓ If we take aviation, for example, there is a severe competition between Airbus and Boeing. That is why our products are good to them. As for motor industry, it is the market with the strongest competition. So manufacturers pursue lower costs and faster launch of their new products in the market. That is why our products are demanded in those markets. But not in Russia's market, which is strongly monopolized.
- ✓ Our key advantage is our software topics. In this respect Russia is still a good country and a place where top scientists live and work. And the algorithm that we use for our products is faster and more efficient vs. our competitors. That is why our products are demanded.
- ✓ Today we export a lot to Europe, France, Germany, Austria, Switzerland, Belgium, Netherland and Great Britain. We have our own U.S.P – it is a new topic, the competition is small and we offer products that are needed by the clients. Everything depends on the products that are offered. Comparing to US products, we offer some specifics, which are important to our clients. Americans fail to do that, but our specialists do it easily.

BARRIERS TO EXPORTING

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- Some part of TA mentions various barriers they have to face in the process of exporting their products/services. The most significant are such barriers as anti-Russia policy in general, economic sanctions, blocking of foreign currency accounts, problems with customs authorities, paperwork etc.

ANTI-RUSSIA POLICY

- One of the recent trends of the global market is the obstruction to everything that is Russian. Even our super loyal clients, with whom we have been working for many years, start feeling uneasy about our Russian origin.*
- One of our clients can't expand our cooperation, because our software is not developed in a NATO country. However our cooperation potential is huge. Whatever you say, it is a huge problem for us. We work in the hi-tech sector with strict confidentiality rules.*
- We used to think, that we could export our products. But actually when we started our currency operations and economic sanctions were announced, it turned out, that we can't. Some of our payments were blocked, frozen and returned. The gaps in payment stopped manufacture and we missed several weeks. (ChM)*
- The key barrier is their understanding of national policy. UN understanding. And we will be interfering with their work, as our products are cheaper. I should say that machines and equipment manufacture is a very conservative sector. They have their monsters here. And it is very hard to shift this conservative segment to something really new. (ChM)*

PROBLEMS WITH CUSTOMS

- Customs authorities should be just cancelled. It does not make any sense to waste time and money comparable with the cost of our products so as to prepare an absolutely useless pack of documents for our products export.*
- It is interesting that all parties of this process know in advance, that the party requesting all that paperwork, i.e. customs authorities, knows nothing about it. I don't understand, why a local manufacturer should bear any costs with export. Export is a process that brings money to this country. (BIO)*

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GOVERNMENT SUPPORT



SUBSIDIES – POSITIVE AND NEGATIVE USER EXPERIENCE

- The majority of surveyed companies do not obtain any technical or financial support from the state, NGO or other structures for the purposes of raising their potential in the sphere of cooperation with global companies. Some companies have a negative experience of communication with government structures in the process of obtaining potential state support or subsidies.
- Only a small part of companies mentioned their positive experience in this area. Among the mentioned support measures the following examples were given: subsidies of the Ministry of Industrial Development, Skolkovo grants, Bortnik Fund program.
- The utmost support from the state is the companies' residency in Skolkovo.

- ✓ Yes, we obtain subsidies from Minprom. Within those subsidies we were developing monitoring systems. We managed to make a good competitive system. The development stage is over, but we keep working on it. If some more state programs of the kind were available, it would be a good support for such companies as we are. (T)
- ✓ We got a Skolkovo grant in 2011, on parity conditions, 50X50. It was the only one direct support we were offered. (DATA)
- ✓ We tried to, we contacted with the export center, but it was useless. Nobody helped us, we were just given advice. Once we went to the exhibition, but we did not like it all. Today we get a huge support of the state as Skolkovo residents, good tax benefits and other things. (ZD)
- ✓ We participated in some Bortnik Fund's programs. But they are not interesting for us now. The rules are changing, too much paperwork. Prepayment is charging for post payment. There are such tools as Skolkovo, but we failed to get anything from them, we tried though. They have a deformed assessment system (BIO)
- ✓ We have not got anything from the state yet. We think about such opportunities. Maybe by autumn. We might try entering Skolkovo. (CLAUD)
- ✓ We have exceptional terms and conditions of doing business. As a Skolkovo company we are freed from many taxes. We do not pay income tax, property. It is a very good support.

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SUPPORT NEEDED BY COMPANIES

TYPES OF STATE SUPPORT NEEDED BY COMPANIES

- Talking about increasing potential opportunities as global vendors, the respondents mention different kinds of government support. The most demanded are as follows:



EVENTS, WHERE YOU MIGHT MEET GLOBAL COMPANIES' REPRESENTATIVES / INTRODUCE YOURSELF TO POTENTIAL CLIENTS / VISIT COMPANIES



FINANCIAL BENEFITS (TO GLOBAL COMPANIES THAT PURCHASE RESOURCES FROM LOCAL VENDORS) / LOCAL VENDORS FOR INVESTMENTS INTO MODERNIZATION



VAT RETURN PROCEDURE FOR SUPPLIES TO GLOBAL COMPANIES



IMPROVEMENT OF BUSINESS ENVIRONMENT FOR LOCAL COMPANIES

- ✓ We need to expand our manufacturing. So as to do it we need to obtain financing. But to obtain financing, we need to go crazy. And it does not guarantee that you get it. You should search for some private investments or have some connections and resources so as to get a bank loan for development. (PAL)
- ✓ They need to be aware of such companies as ours, I mean providing info about us. Participation in some mutually profitable propositions. It might be efficient. And also the status at the market, the company's position.
- ✓ It is necessary to improve the business environment for local companies. And marketing opportunities too. We have used the services of REC – Russian Export Center. And we keep cooperating with them. (CHM)
- ✓ At minimum – well organized sites with real selection of both suppliers and potential clients. Everything should be organized very well to make the meetings efficient for potential contracts. It often happens, that one party has products, and the other party has money, but those two parties will never meet. (F)

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NECESSARY MEASURES

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THE MOST EFFICIENT AND REALISTIC MEASURES TO BE IMPLEMENTED BY THE GOVERNMENT

INVESTMENTS, SUPPORT BY THE GOVERNMENT

- ✓ *No investments, state support on development. Actually in the Western if you wish to get accreditation and develop manufacture, you don't have to pay anything, you are given a subsidy and you just repay it. We have nothing of the kind here. It is absolutely unreal to get such financing. (PAL)*
- ✓ *If tomorrow they say 'give us big volumes but we'll pay by installments', it will be crucial for us. We don't have own funds in big volumes or some good credit limits. Special terms & conditions for crediting are necessary. (F)*

FINANCIAL BENEFITS / SIMPLIFIED TAXATION

- ✓ *Financial benefits, simplified taxation, affordable credit lines are necessary. We have no opportunity to take big loans with small interests so as to increase our turnover, to grow. (BEST)*
- ✓ *Obtaining financial benefits or donation should be easier. It is not about reporting. You should report fully and seriously afterwards, it's OK. But you should have more opportunities to use them and less bureaucratic hurdles in the process of obtaining. (AMINO)*

SIMPLIFIED CUSTOMS PROCEDURES AND CERTIFICATION

- ✓ *It is necessary to simplify customs procedures. It is rather hard to export products. The procedures is rather complicated. Also the certification procedure should be simplified and made cheaper. In our country 2 monopolists are responsible for it, they might spend half a year on research. (AMINO)*

SIMPLIFIED CURRENCY CONTROL

- ✓ *What is important for small and medium business in the process of export – it is a simplified currency control. Today it is a real pain. Especially if you have to fulfill your contract obligations. It should be simplified. (DATA)*

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PROBLEMS OF SMALL AND MEDIUM COMPANIES

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BARRIERS OF SMALL AND MEDIUM COMPANIES

- Among the key barriers that small and medium companies face in Russia, the respondents mentioned access to finances, lack of understanding of state regulations, problems with following regulation requirements, high operational costs, lack of qualified employees, strong competition etc.
- Nevertheless almost all respondents mentioned the following barriers as the most critical:

ACCESS TO FINANCES

- ✓ *A new Resolution has been issued recently, devoted to loan rates subsidizing for small and medium companies. This measure does not work basically, because we can't take a loan. We have nothing except our non-material assets. We have nothing to pawn.*

TAX LOAD

- ✓ *High taxes. Lack of good banking products. Impossible to take interesting loans. Sometimes everything is neutralized by costs. Inflation too. Small and medium business lacks investments, money.*

HIGH OPERATIONAL COSTS

- ✓ *High operational costs, including high rents. Also communication costs. Exhibitions. Everything is rather expensive. (ETC)*

UNDERSTANDING OF STATE REGULATIONS

- ✓ *Hard to understand state regulation acts. The system is rather complicated. Nobody will explain it. You will have to figure it out on your own.*

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RAISING OF SMB POTENTIAL

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MEASURES THAT HELP TO WORK WITH GLOBAL COMPANIES

- According to the survey small and medium companies take some measures that help them to work with global companies. Among them ISO certification could be mentioned, as well as participation in global conferences, organization of English classes for employees, customer management trainings, other qualification events.

ISO CERTIFICATION

- ✓ We have ISO certification, and another thing is participation in global conferences. We participate in them on a regular basis, incl. those devoted to normative documents development. We used to have English classes too. But it all depends on the budget. If you have enough budget, you can do whatever you want. But all our employees are well qualified specialists, each in his area of focus. (T)
- ✓ Every year we have ISO 9001 audit. It is not a formal thing for us, we really believe it is a good opportunity. We have tried to acquire this vision for the last years. We annually try to analyze the errors of the previous year, reclamations, delays, and take the necessary measures. (BIO)

EMPLOYEE TRAINING

- ✓ We have trainings twice a year, we invite different specialists. They hold webinars too. We discuss new products, clients' requests. We certainly work on that. (BEST)
- ✓ We have trainings on a regular basis. We also send our specialists abroad at our own expense. We also visit our competitors' facilities, if we reach agreement. We also visit raw materials' suppliers, if they offer something new. It is an ongoing work. Competition is typical for any market. If you ignore this fact, you might miss a good contract. (F)
- ✓ Our office staff have product trainings, development strategy trainings, market reviews. We motivate our employees and increase their professional level, we also discuss scientific developments of our industry.

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RAISING OF SMB POTENTIAL

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RESTRICTING FACTORS OF GLOBAL PARTNERSHIP POTENTIAL DEVELOPMENT

- TRAINING COSTS
- OFF-THE-JOB TRAININGS
- CONCERN ABOUT STAFF TURNOVER / POACHING

- ✓ Among the important factors we could mention training costs and off-the-job trainings. We also have concerns about our staff turnover.
- ✓ Training costs is a problem, off-the-job training is a problem too. Each our specialist has 110% workload. Another thing is lack of necessary training programs, our subjects are too narrow and specialized.
- ✓ We are rather loyal, when we have requests from our employees about their need to get extra trainings at the company's expense. The trainings we organize are applicative: some specific program language, system administration.
- ✓ Value for money: if we see that it is useful, we will say «yes». But if it is useless, why should we do it?

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SALES COSTS

TRADE COSTS

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TRADE COSTS' IMPORTANCE: TIME OR MONEY

- According to the majority of respondents, in case of selling products or buying resources, time is the biggest restriction in terms of trade costs.

TIME **V** **MONEY**

- Time is really important. Global suppliers try to work with our clients setting their requirements and conditions to them.
- Time is a more serious restriction, because the financial result depends on the time of delivery. The longer the product is delivered, the later the client receives it, the later he will pay for it. Everything will be shifted: sales, margins, income, tax payments, salary payments, raw materials purchase.
- Time of course. At the customs. Suppliers are not ready to deal with our customs.
- The need to forecast time at exporting – it is just awful. It is even more difficult at importing. We are a small company, even one day means a lot of time for us. We can't always say, what we'll need tomorrow, and each delay might be harmful to our development cycle. Delays at importing are as bad as at exporting. And it is all about paperwork. And in the end of the story it means lost time and of course lost money.

TRADE COSTS

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THE EXPERTS MENTION THE FOLLOWING REASONS FOR DELAYS OF TRADE OPERATIONS AT EXPORT/IMPORT AND TRANSPORTATION ACROSS RUSSIA:

CUSTOMS / EXPORT CONTROL

- ✓ It is mainly about customs operations. And electronic payments that have not been delivered in time for the reason unknown.
- ✓ We can't forecast the time spent on operations. Until you see your load with your own eyes, you will never be confident, that everything goes smoothly. They always find some errors in paperwork at the customs. The rules are constantly changing and you will never do it seamlessly.

HOLIDAYS

- ✓ We have failed forecasting time lately. For example, we are waiting for a composition of some component, we expect it to arrive on May, 11 but it is actually delivered on May, 30. We all go crazy, because the client goes crazy, because it should be turned into the end product. It means deadlines, nerves.
- ✓ During May, 1 holidays they do not wish to work at all. All operations are delayed, uploading, downloading. We get money from the client later. And the same problems are in early June. It is a human factor, it is Russia.

CURRENCY CONTROL

- ✓ Delays with accounting, currency control and customs. It sometimes happens, that the goods are kept for several days, we are waiting for money for several days, and the driver is just standing by the door, because we can't pay.

BANK TRANSACTION DELAYS

- ✓ Money delays stop manufacture, we might miss several weeks. When we work with global companies and delay payments for several weeks, we might miss our positions in the conveyor. And that means delays of manufacture for even more time.

- * According to the experts, delays in trade operations might reach from 20% to 100%.

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COMMUNICATION CHANNELS

MARKETING CHANNELS FOR ADVERTISING

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- Based on the analysis, the most popular and demanded channels for marketing and advertising communication are as follows:



WEBSITE

- We have a website. We have pages in social networks.
- We have a website, it is like our business card.



FAIRS / EXHIBITIONS

- Trade fairs and specialized exhibitions. We participate in the annual Metalwork exhibition in Moscow. The second exhibition is Innoprom.
- The key channel is participation in industry forums, events, conferences.



OTHER COMPANIES' REFERENCE

- Other companies' references or customers' recommendations.
- Face-to-face meetings by reference, we have five companies here and we all know each other. Our clients refer to us as a rule.
- It sounds strange, but I would say – 'word of mouth'



OTHER CHANNELS

- SPECIALIZED PRINT MEDIA/ INDUSTRY MAGAZINES
- ONLINE ADS
- SCIENTIFIC EVENTS
- WORK WITH INDUSTRY ASSOCIATIONS

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FINDINGS AND RECOMMENDATIONS

KEY FINDINGS (1)

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- According to the analysis, many small and medium companies that operate in machine building also mention motor industry as the distribution area for their products / services. This industry specifics is manufacture of software, simple products / parts, design services etc.
- For chemical industries it is typical to manufacture paint, varnish and lacquer for construction, petrochemistry, shipbuilding, carriage building, nuclear and power industries, chemical agents for biotechnologies and diagnostics, chemical raw materials and industrial chemistry, main organic and inorganic chemicals etc.
- This sector's specifics is manufacture of raw materials as an end product.** According to the research results, in the chemical industry the market of FDI companies is growing in general, however it is a market of low technological products and services. The companies manufacture end products that are distributed in the local market.
- As for machine building and motor industry their end products are less demanded due to low purchasing power of individuals and legal entities.
- Only three respondents mention, that they do not supply their products / services to FDI companies or export. However they all confirmed, that they are absolutely ready to export and/or work with global companies operating in the territory of Russia.
- The majority of the respondents either work with FDI companies or export their products / services or both.

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KEY FINDINGS (2)

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- According to the research, the experts do not mention any special requirements to cooperation with FDI companies. However they identify several specific features of such cooperation. They are as follows: certification, scheduled auditing, registration in Provider Identifiers, compliance with labor condition requirements etc. It should be noted, that similar requirements are also mentioned by global companies in case of exporting products / services from the Russian Federation.
- Among the key advantages that help Russian companies to cooperate successfully with FDI companies are as follows: **good value for money, logistics, fast responding to clients' requests.**
- Among the barriers that prevent from working with FDI companies the respondents mentioned the following: **some types of products are not in demand** (this refers basically to hi-tech products /services, e.g. software, compound products and their components, design etc.) Also **some Russian companies do not pass audit of FDI companies.** Among other barriers we could mention **insufficient communication and information about such companies.**
- However some part of businesses not working with FDI companies expressed their opinion, that **exporting would be more attractive to them vs. work with FDI companies in RF**, as FDI market is rather limited.
- So in terms of development, Russian companies pursue entering a broader and more promising global market, because export means revenues in foreign currency, which helps to neutralize the results of the local crisis.

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KEY FINDINGS (3)

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- As for exporters they believe their key advantages to be as follows: high quality and/or uniqueness of their products, good value for money, cutting-edge scientific developments, scientific potential.
- Some part of TA mentions various barriers they have to face in the process of exporting their products/services. The most significant are such barriers as anti-Russia policy in general, economic sanctions, blocking of foreign currency accounts, problems with customs authorities, paperwork etc.
- According to the research, the majority of surveyed companies do not obtain any technical or financial support from the state, NGO or other structures for the purposes of raising their potential in the sphere of cooperation with global companies. Some companies have a negative experience of communication with government structures in the process of obtaining potential state support or subsidies.
- Only a small part of companies mentioned a positive experience in this area. Among the mentioned support the following examples were given: subsidies of the Ministry of Industrial Development, Skolkovo grants, Bortnik Fund program. The utmost support from the state is the companies' residency in Skolkovo.
- Talking about increasing potential opportunities as global vendors, the respondents mention different kinds of government support. The most demanded are as follows: events, where you might meet global companies' representatives / introduce yourself to potential clients. One of the mentioned measures is financial benefits (to global companies that purchase resources from local vendors, to local vendors for investments into modernization (which is critical for small and medium companies). Among other measures they mention VAT return procedure for supplies to global companies and improvement of business environment for local companies in general.

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KEY FINDINGS (4)

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- Among the key barriers that small and medium companies face in Russia, the experts mentioned access to finances, lack of understanding of state regulations, problems with following regulation requirements, high operational costs, lack of qualified employees, strong competition etc.
- So the most efficient and realistic measures to be implemented by the government are investments, support by the government, financial benefits, simplified taxation, simplified customs procedures and certification, simplified currency control.
- It should be noted, that small and medium companies take some measures that help them to work with global companies. Among them ISO certification could be mentioned, as well as participation in global conferences, organization of English classes for employees, customer management trainings, other qualification events.
- However the companies mention a number of restricting factors of global partnership potential development. They are training costs, off-the-job trainings, concerns about staff turnover/poaching incl. to other countries.
- As for various trade costs in case of selling products or buying resources, time is the biggest restriction. Among the key reasons for delay during export / import operations in case of delivery within Russia the respondents mentioned customs and export control, currency control and bank transaction delays as well as holidays and a human factor.
- Based on the analysis, the most popular and demanded channels for marketing and advertising communication are as follows: website, fairs / exhibitions. Among the important info channels the respondents also mentioned other companies' references, specialized print media, industry magazines, online ads, scientific events, work with industry associations.

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