

Can Moscow be an International Financial Center?



What is Important for Developing a Financial Center?

According to the *Xinhua-Dow Jones International Financial Center Development (IFCD) Index* there are 5 important criteria

1) Financial Market

- Capital market
- Forex market
- Banking market
- Insurance market

2) General Environment

- Economic environment
- Political environment
- Openness

3) Growth and Development

- Capital market growth
- Economic growth
- City innovation output
- Creation potential

4) Services

- Government services
- Intellectual capital
- Urban

5) Industrial Support

- Business environment support
- Basic city conditions
- City infrastructure



How does Russia Rank?

Overall IFCD Index **35** /45, where Moscow is the only CIS representative

1) Financial Market **24**

- Capital market
- Forex market
- Banking market
- Insurance market

2) General Environment **42**

- Economic environment
- Political environment
- Openness

3) Growth and Development **15**

- Capital market growth
- Economic growth
- City innovation output
- Creation potential

4) Services **39**

- Government services
- Intellectual capital
- Urban

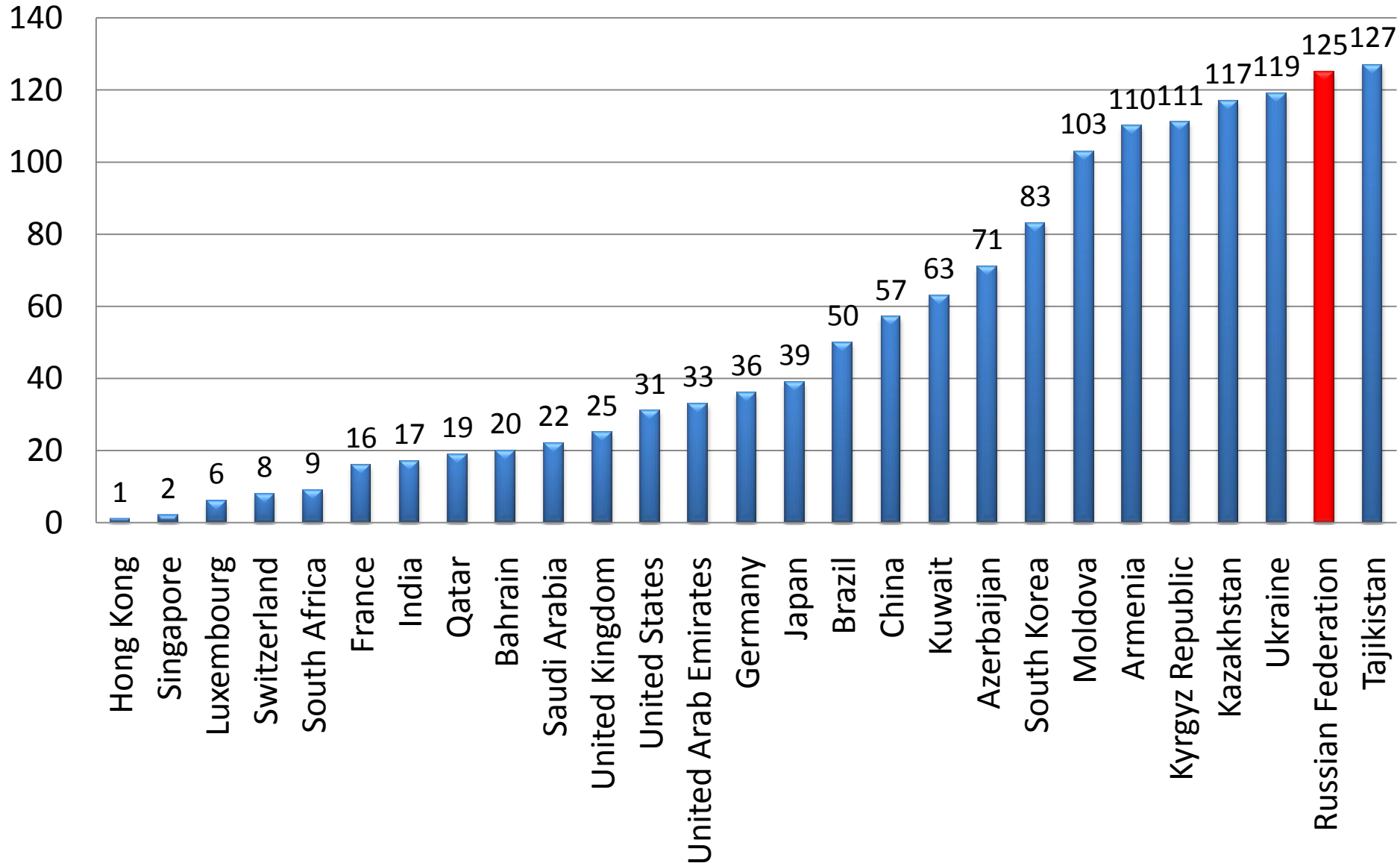
5) Industrial Support **23**

- Business environment support
- Basic city conditions
- City infrastructure



Financial Market Development

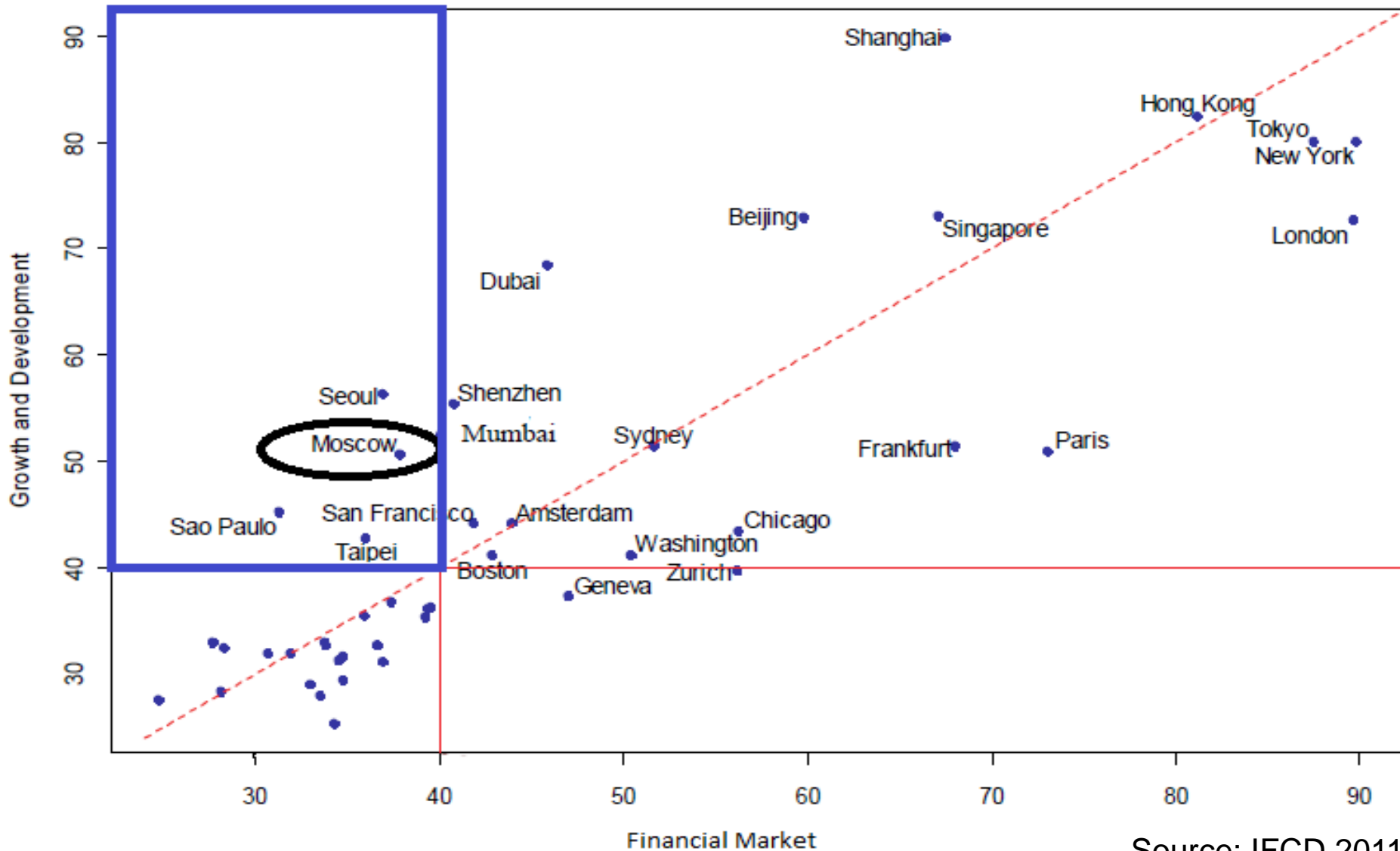
GCI 8th Pillar Ranking



Russia vs. Others (GCI 8th Pillar Ranking)

| | RUSSIA | Big 4 | BRICS | EU3 | Middle East | Other Asia | CIS |
|--|------------|------------|-------------|-------------|-------------|------------|------------|
| 8 Financial market development | 125 | 26 | 33 | 19 | 31 | 29 | 108 |
| | Difference | -99 | -92 | -106 | -94 | -96 | -17 |
| 8.01 Availability of financial services | 109 | 16 | 38 | 9 | 30 | 41 | 111 |
| | Difference | -94 | -72 | -100 | -79 | -68 | 2 |
| 8.02 Affordability of financial services | 92 | 16 | 44 | 14 | 22 | 30 | 110 |
| | Difference | -76 | -48 | -78 | -70 | -62 | 18 |
| 8.03 Financing through local equity market | 107 | 29 | 29 | 27 | 27 | 22 | 113 |
| | Difference | -79 | -79 | -80 | -80 | -85 | 6 |
| 8.04 Ease of access to loans | 107 | 44 | 49 | 36 | 9 | 44 | 110 |
| | Difference | -63 | -58 | -71 | -98 | -63 | 3 |
| 8.05 Venture capital availability | 95 | 30 | 39 | 30 | 15 | 34 | 101 |
| | Difference | -65 | -56 | -65 | -80 | -61 | 6 |
| 8.06 Restriction on capital flows | 119 | 33 | 93 | 25 | 28 | 34 | 100 |
| | Difference | -86 | -27 | -94 | -91 | -85 | -19 |
| 8.07 Soundness of banks | 129 | 91 | 26 | 60 | 40 | 39 | 118 |
| | Difference | -39 | -103 | -69 | -89 | -90 | -11 |
| 8.08 Regulation of securities exchanges | 118 | 39 | 21 | 20 | 30 | 30 | 121 |
| | Difference | -79 | -98 | -98 | -88 | -88 | 3 |
| 8.09 Legal rights index | 103 | 21 | 47 | 39 | 89 | 14 | 41 |
| | Difference | -82 | -56 | -64 | -14 | -89 | -62 |

Financial Markets vs. Growth and Development



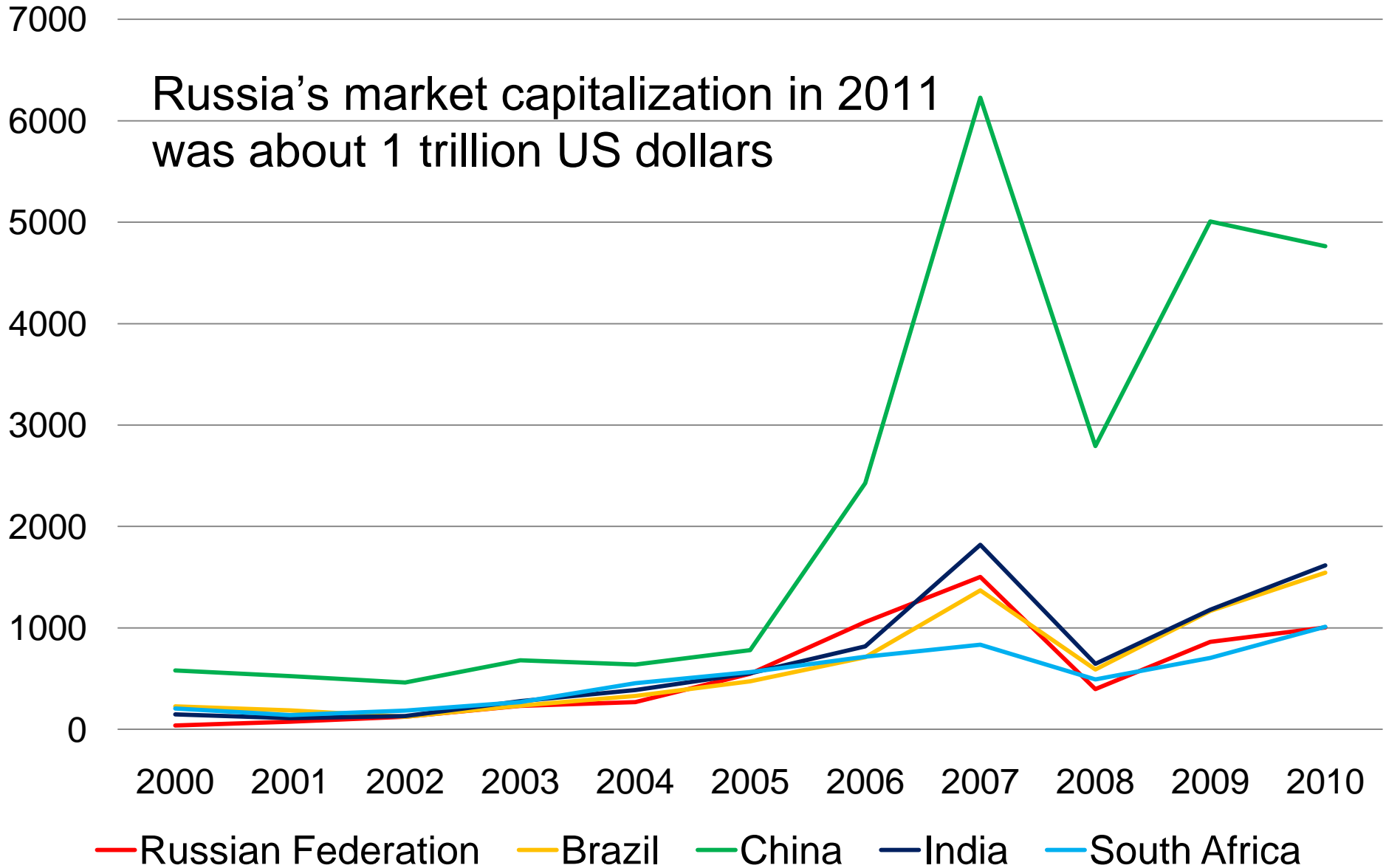
The BRICS

- IFCD 2011 special questionnaire regarding one city of each BRICS country

| City | Sao Paolo | Moscow | Mumbai | Shanghai | Johannesburg |
|--------------------------------|----------------|---------------|--------------|--------------|--------------------|
| Confidence in Becoming an IFC | 3 | 2 | 5 | 1 | 4 |
| Power to attract capital | 4 | 2 | 5 | 1 | 3 |
| Power to attract talent | 2 | 4 | 5 | 1 | 3 |
| Currency | Brazilian real | Russian ruble | Indian rupee | Chinese Yuan | South African rand |
| Familiarity with the currency | 4 | 2 | 3 | 1 | 5 |
| Country | Brazil | Russia | India | China | South Africa |
| FDI in 2009 (change from 1999) | 13% (-25%) | 19% (15%) | 17% (14%) | 48% (-5%) | 3% (1%) |

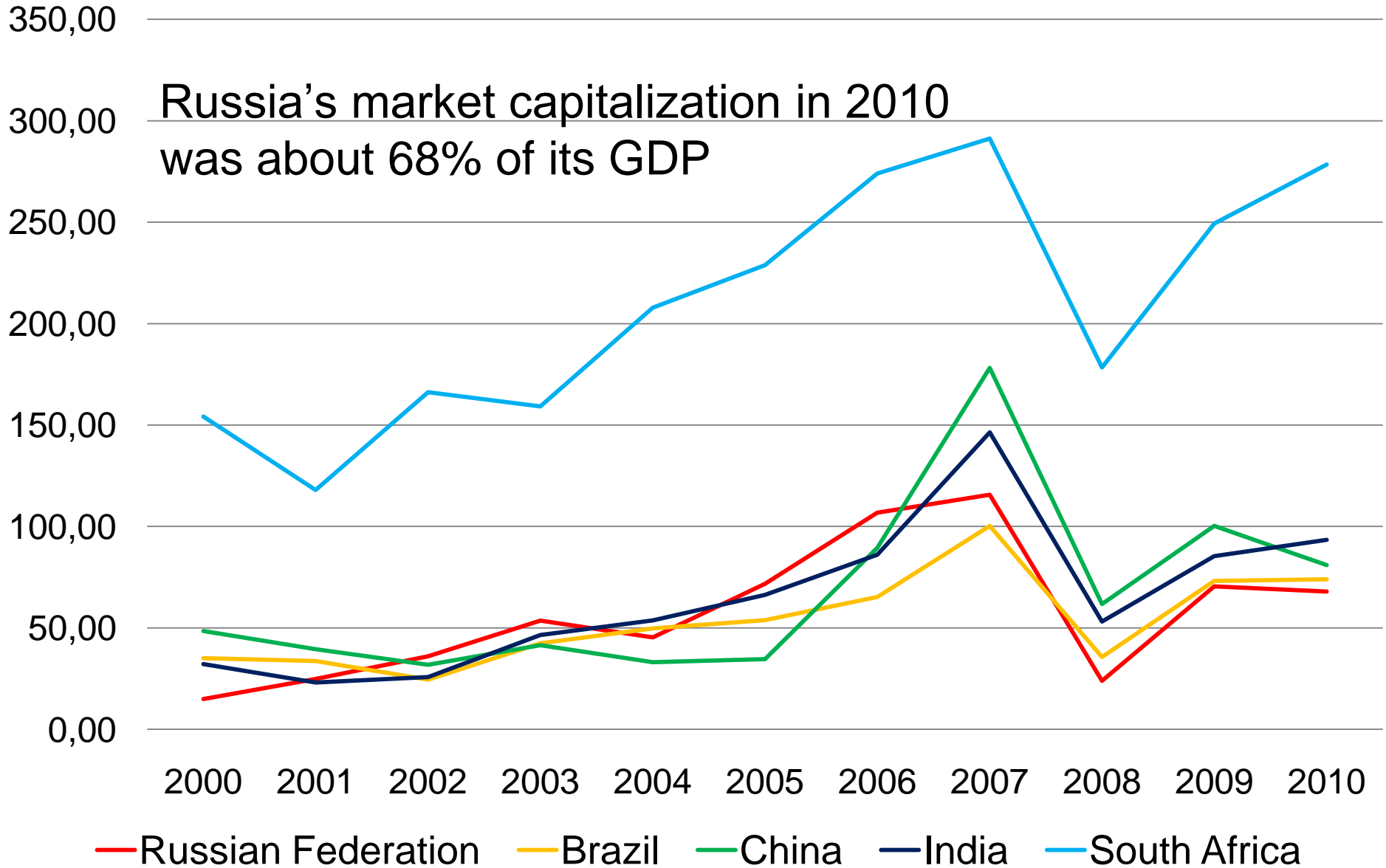
Market Capitalization (USD): The BRICS

Russia's market capitalization in 2011
was about 1 trillion US dollars



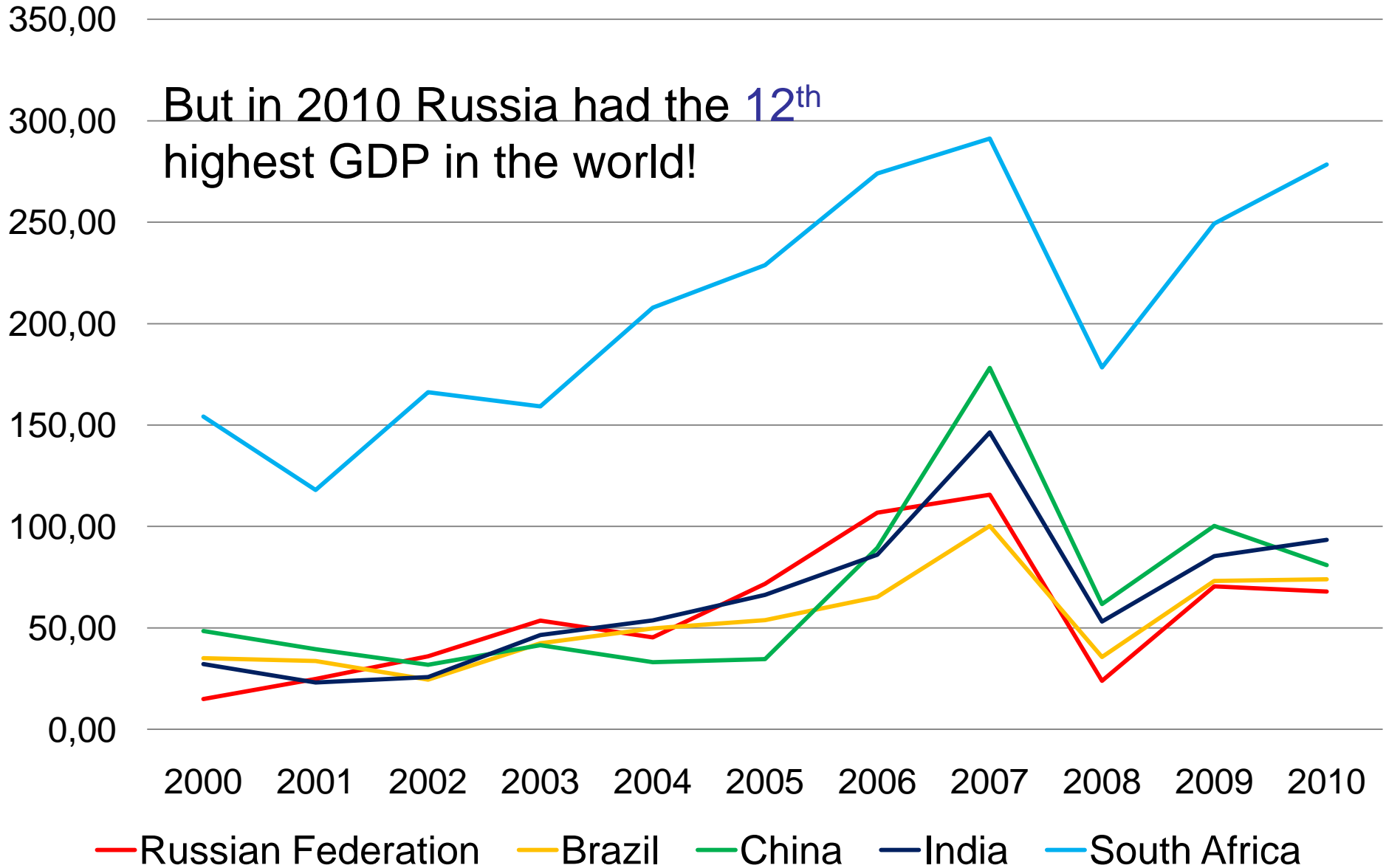
Market Capitalization as % of GDP: The BRICS

Russia's market capitalization in 2010
was about 68% of its GDP



Market Capitalization as % of GDP: The BRICS

But in 2010 Russia had the 12th
highest GDP in the world!



The Overall State of Russia

According to the Evidence So Far

- Moscow falls into the quadrant with high financial growth and development and low financial market development.
- Russia lags behind other emerging (and developed) economies.
- Regarding BRICS cities, Moscow has the second highest potential to become an IFC.
- Financial market development is necessary by all means.



Some Positive Facts

- The scale, sophistication, and financial liberalization of Russian financial market outperform other CIS countries.
- Historical background and cultural similarities provide significant comparative advantages in providing financial services to this region.
- Moscow has its role in the regional provision of financial service in the CIS area.



Moscow is not Russia

- Moscow is the largest city in Russia
- About **6%** of the total and **8 %** of the occupied population of Russia is concentrated in Moscow
- Also **20%** of those occupied in finance, credit, insurance and pension maintenance
- And **35%** of those occupied in science
- Moscow provides **16%** of Russia's GDP
- GDP per capita is more than **twice** that of Russia
- Extreme social stratification: richest 10%'s incomes exceed poorest 10%'s incomes 44 times

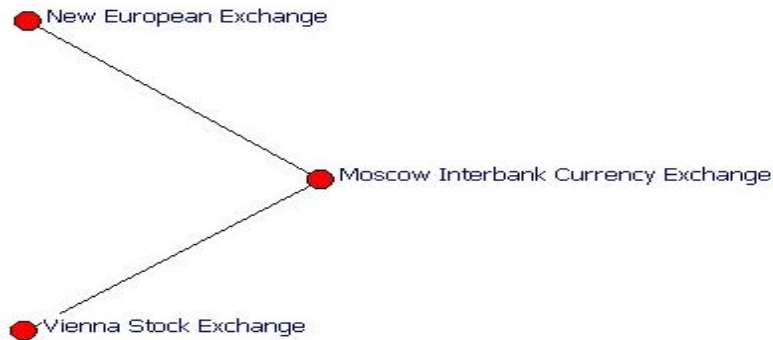


Strengths to Benefit From

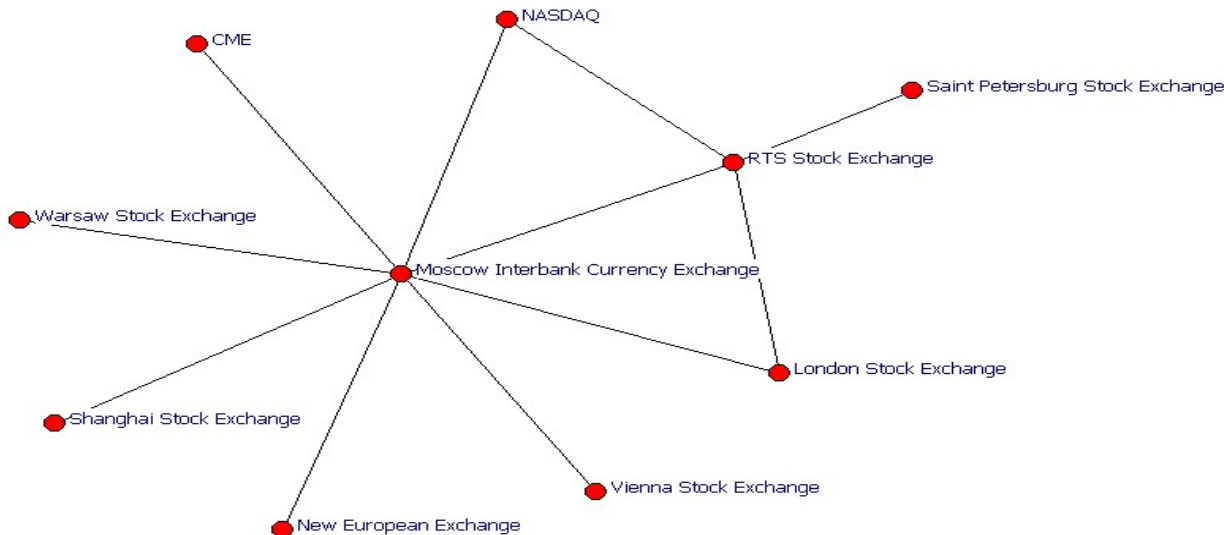
| Education | Rating | Score |
|--|---------------|--------------|
| Primary education enrollment | 3 | 99.8% |
| Secondary education enrollment | 77 | 84.8% |
| Tertiary education enrollment | 12 | 77.2% |
| Work Force | Rating | Score |
| Female-to-male participation in work force | 25 | 9 / 10 |
| Innovation | Rating | Score |
| Capacity for innovation | 38 | 3.5 / 7 |
| Company spending on innovation | 50 | 3.2 / 7 |
| Availability of scientists and engineers | 53 | 4.3 / 7 |

Strengths to Benefit From: Global Connections

- Collaborations with other financial centers as of 2002



- Collaborations with other financial centers as of 2009



Problems that Need to be Addressed

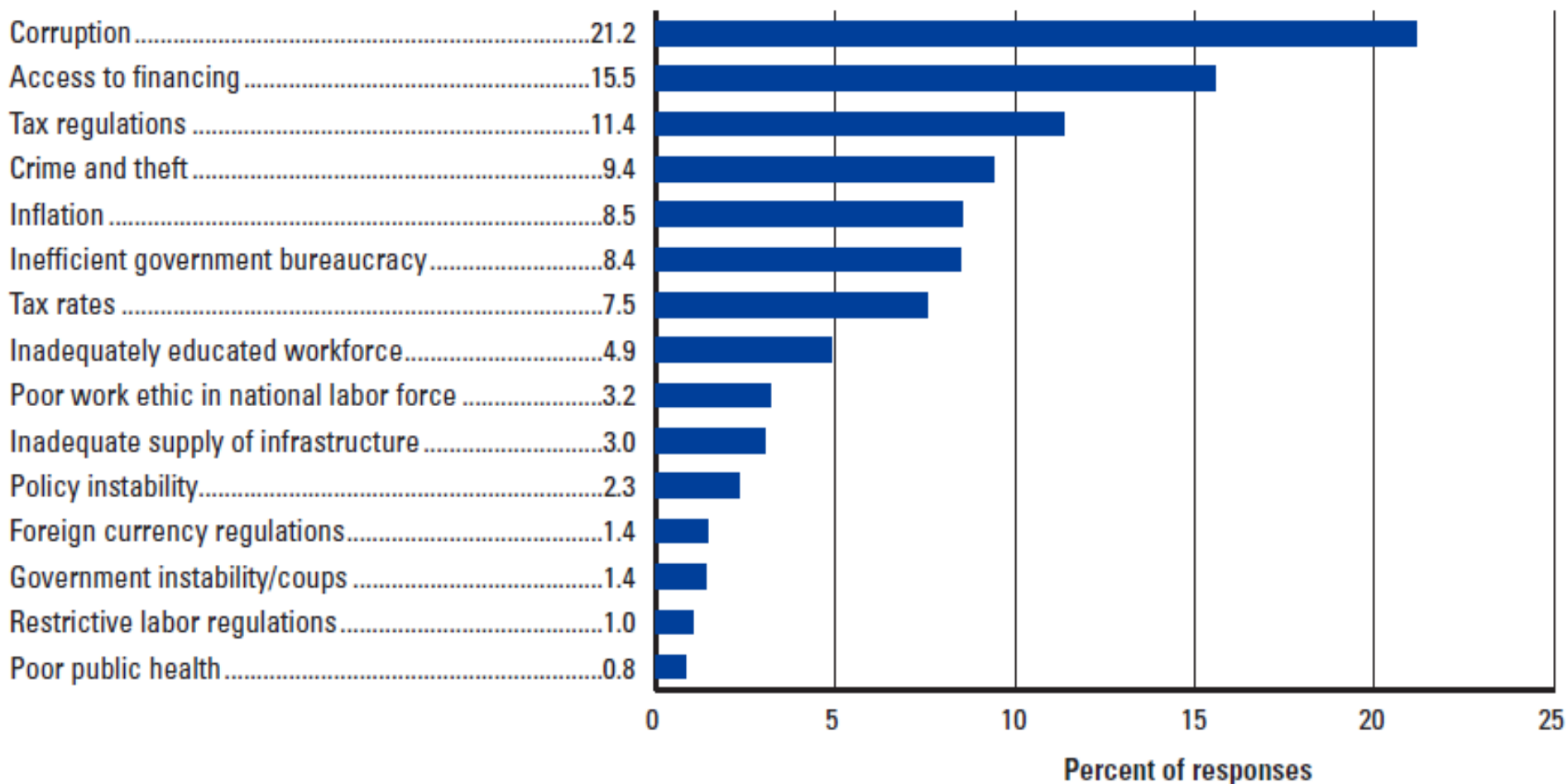
- **International Financial Center Development 2011**
 - General Environment:
 - Emerging economies have a strong development momentum
 - *“These cities are expected to rise up in rankings”*
 - Services:
 - The financial centers of emerging economies scored low
 - *“The service levels of these cities all face immense challenges in the days ahead, especially in the area of government service where they need to respect and adapt to the rules of the market economy.”*



Problems that Need to be Addressed

- Global Competitiveness Report 2011:

The most problematic factors for doing business



Problems that Need to be Addressed

- **Doing Business 2011:**

| Topic Rankings | DB 2011 Rank /183 | DB 2010 Rank /183 | Change in Rank |
|-----------------------------------|----------------------|----------------------|-------------------|
| Overall Ease of Doing Business | 123 | 116 | -7 |
| Starting a Business | 108 | 104 | -4 |
| Dealing with Construction Permits | 182 | 182 | No change |
| Registering Property | 51 | 45 | -6 |
| Getting Credit | 89 | 87 | -2 |
| Protecting Investors | 93 | 92 | -1 |
| Paying Taxes | 105 | 103 | -2 |
| Trading Across Borders | 162 | 162 | No change |
| Enforcing Contracts | 18 | 18 | No change |
| Closing a Business | 103 | 93 | -10 |

The Current Situation

- Political situation – stable
 - Power continues to be highly centralized and concentrated
 - *This can be used to initiate and implement the necessary reforms*
 - Economic and political reforms aiming for:
 - Political pluralism
 - Open society
 - Rule of law
 - Good governance
 - The direction is right, but much more is necessary



The Current Situation

- Governance and Integrity
 - *State bureaucracy* doubled from 1998 to 2008
 - *Corruption in the bureaucracy* also increased
 - This is unacceptable and hinders Russia's further financial development
- Legal Environment
 - Legislative reforms are taking place
 - Those must remain a priority
 - Particularly, investor protection
 - Implementation is inefficient and slow



The Current Situation

“Recent efforts to increase transparency, step up judicial reform and the rule of law and combat corruption are particularly encouraging, but implementation will be key”
(EBRD Report on Russia)



The Current Situation: Summary

- The highly educated population of Russia is a great asset that can be used towards achieving financial development goals
- Making promises and showing understanding of major problems is good, but timely action is essential for Russia's success in becoming an International Financial Center
- Concentration of power can be beneficial in setting up policies and ensuring their enforcement
- Corruption and bureaucracy are a great concern
- Doing business is hard



General Policy Guidelines

- Top **regulatory** changes desired:
 - 1) Taxation
 - 2) Transparency and predictability of regulation
 - 3) Economic and business freedom
 - 4) Regulatory simplification
- Best **signals of commitment** to financial services:
 - 1) Long term stability of regulation
 - 2) Investment in infrastructure
 - 3) Taxation
 - 4) Improving the quality of life for expatriates



Recommendations for Financial Reforms

- Creation of a monetary environment conducive to transition to inflation targeting
 - *Development of currency risk and oil risk hedging instruments*
 - *Unification of taxation regimes in FX forward contracts*
- Creation of an environment conducive to the mobilization of capital.
 - *Deeper government bond market*
 - *Privatisation/infrastructure bonds*
- Alignment of banking regulatory regimes with G20 decisions
 - *Further implementation of “Basel III”*
 - *Uniform international standard*



Conclusion

- Russia needs to improve the speed of its bureaucratic norms.
- Economic, political, and legislative reforms must be implemented timely and adequately
- Policies to enable doing business are needed
- Financial markets development in all aspect is required
- Russia has the resources to succeed
- Long term commitment and quick efficient actions will lead to success



Questions?

