

**Russian IT Sector Trends and Prospects -
Product, Sector Play via Synergistic Partnerships**

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Key macroeconomic trends driving IT sector development

Macroeconomic trends

- Economic growth remains lukewarm across the board, except plastics, online retail, tools and equipment, meat, electronics
- Most sectors are in or are approaching state of saturation
- Certain sectors have deeper cash pockets, e.g. transport, mining, construction, fertilizers, mobile telecoms
- Generally, funding has dried up for corporates (both debt and equity)
- Spending remains weak, as population income growth is slowing
- CPI inflation picking up again, further threatening consumption

Effect on companies

- Margins are declining in most sectors, as corporate profit is outgrown by nominal GDP
- Competition is toughening, further affecting earnings and investor confidence
- Most companies are hesitant to invest in business expansion
- Many market players are undertaking efficiency improvement and cost-cutting measures
- Most economic sectors are ripe for asset consolidation, as soon as capital markets reopen
- At the same time, many vertically integrated structures divest non-core assets, thus promoting horizontal integration

Effect on IT sector development

- IT sector growth is stimulated by companies' attempts to tackle inefficiency and gain a competitive edge
- Massive investments in IT are made mostly by more cash-rich government authorities and large corporations
- Companies seek answers to finite efficiency improvement questions, predominantly needing customized solutions

Key focus for market expansion

- Facing austere economic conditions, IT market players must place their focus on new growth points, e.g. eCommerce, transportation, warehouse and logistics sectors
- Also of interest are cash-rich entities operating in increasingly competitive markets, e.g. oil product manufacturing and retail
- Emphasis must be put on products and solutions that deliver measurable results in improving speed and effectiveness of business processes; strong brand name and comprehensive solutions are starting to be found less appealing

Major IT industry trends and Russian market players' needs

TRENDS

NEEDS

1	2	3	4	5
Efficiency improvement	New product, user experience creation	Tackling complexity	Market structure changes	Customized solutions
<ul style="list-style-type: none"> ■ BPM segment stays robust, driven also by companies' horizontal integration ■ BI solutions taking off from low base, but tools need sophistication ■ Cloud technologies spreading apace, but are held back by security concerns at LEs, pricing mismatch for SMEs ■ IT directors/CIOs not always inclined to make changes, fearing higher accountability 	<ul style="list-style-type: none"> ■ Content-rich services become increasingly important ■ BI solutions developing rapidly, but adoption slowed by lack of methodologies ■ UE turns into key element driving product enhancement, but execution not always convincing, as client-oriented approach yet to get entrenched ■ Growing interest in VoIP, virtual ATNs ■ IT consulting sees rising demand 	<ul style="list-style-type: none"> ■ Big Data management changes face of data centers, turning them into system integrators, and fragmenting company DBs ■ Customization in high demand, further solidifying local SIs' market standings ■ Interoperability, product integration become crucially important for installed products ■ Rising interest in portal technologies, virtual machines' integration 	<ul style="list-style-type: none"> ■ Government-funded IT projects become sweet spot for most market players ■ Infrastructure + IT projects on the rise, causing IT companies to do engineering and construction ■ Standalone services find it more and more difficult to survive ■ Mobile integration becomes emerging trend, but widespread adoption to take more time ■ IaaS, PaaS operating models starting to turn heads 	<ul style="list-style-type: none"> ■ Many companies order solutions for specific processes, situations, having had bad experience with launch of complex IT systems ■ Customization is in high demand, further strengthening local SIs' market standings ■ SIs good at developing complex service packages to meet clients' needs using vendors' technologies, but often lack coherent own products
<ol style="list-style-type: none"> 1. Orderly product development process 2. Product management leadership capable of ensuring commercially sustainable operations 3. Clear vision of required product/service concept 		<ol style="list-style-type: none"> 4. Improved sales & marketing techniques utilizing ROI calculation, success stories 5. Detailed understanding both of client's business and industry best practices 		

Most attractive market segments for Japanese IT companies



Top priority:

- ERP, CR, BPM, ECM software for eCommerce
- Electronic trade instruments and platforms; B2B matchmaking platforms; logistics and international trade process management systems
- Big Data and data center management systems
- Software for multi-functional process optimization
- Production of components and software for household and industrial electronics



Medium priority:

- B2C-oriented online services (e.g. online ticket and hotel booking and trip planning) that may be brought to the Russian market
- Mesh network solutions
- Software and solutions for managing P2P and M2M networks
- Games, including social and network games
- Solutions for complex IT integration projects



Lower priority:

- Healthcare IT, including mHealth and eHealth segments
- Internet of things (connecting and controlling various objects through the Internet)
- Software and solutions for energy efficiency (including smart home and smart building systems)
- Trade robots and IT systems for international financial markets

Main risks for business development

Market saturation

Growing number of market segments are in or are approaching state of saturation, eroding margins and creating risk of quick product replication by local competitors

Homologation issues

Tailoring products and services for Russian market may prove to be a major challenge, requiring competencies in adjacent product areas and uninterrupted access to customers for product upgrades and service

Limited access to clients

LE segment roughly divided among local vendors, including SIs providing complex service solutions, therefore reducing opportunities for penetration into companies with new products; while SME client base in most segments too shallow for massive sales and marketing effort

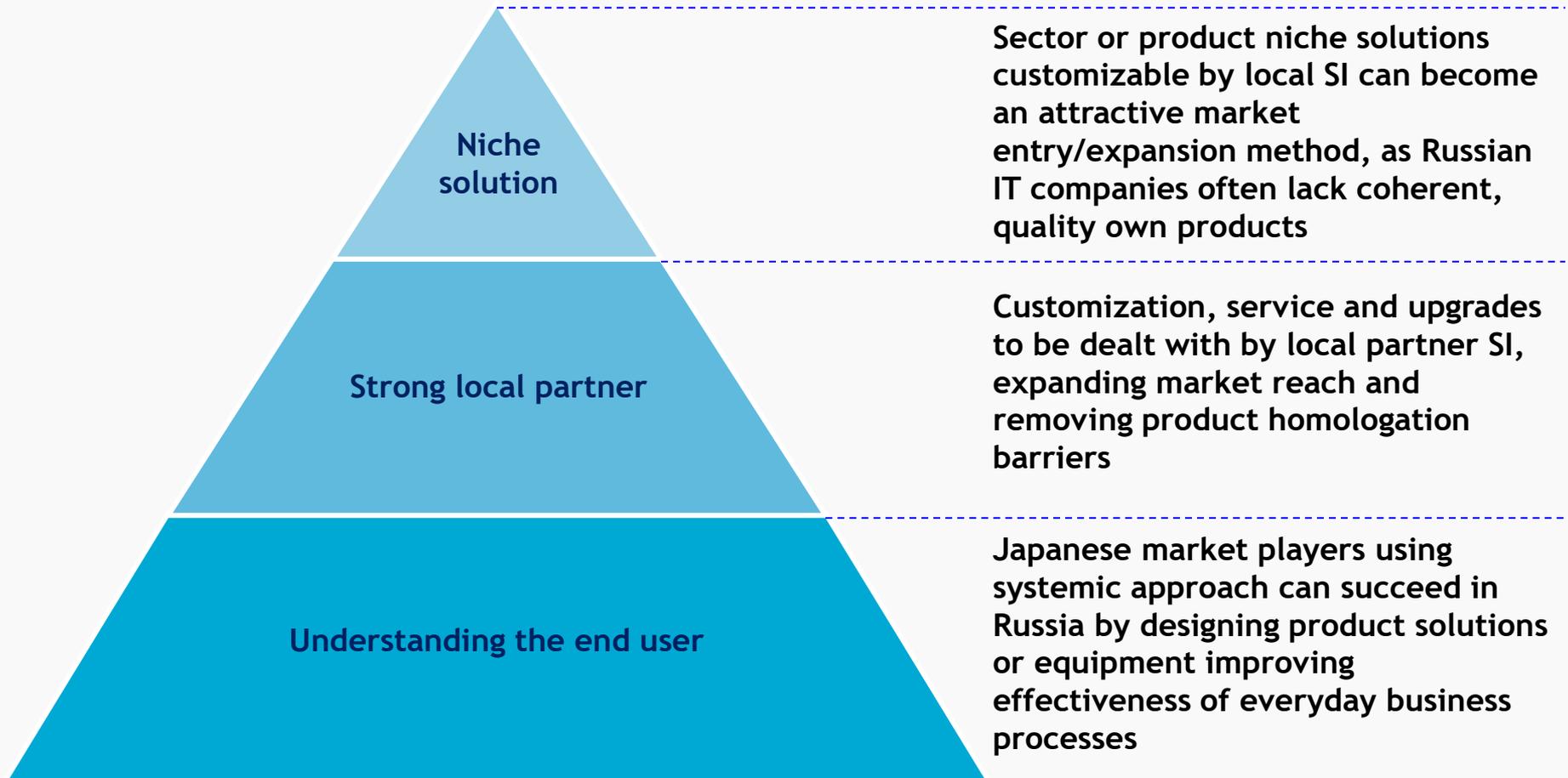
Lack of required competencies at Russian partners

Insufficient product development, product management, and sales & marketing skills of Russian IT companies can potentially reduce effectiveness of solutions developed by Japanese market players, unless complemented by proper training and assistance

Administrative barriers

Significant amounts of bureaucracy and widespread non-market compensation forms in government and corporate contracts can affect business development and product competitiveness

Key success factors for Japanese IT companies in Russia



Recommendations for market strategy and partnership format

Successful market entry and expansion requires selecting the optimal format for building local partnerships, maximizing the synergetic effect:

1 Partnership with local SI in development, sales, upgrade and service of focused sector or niche solution for Russian market

2 Opening own representative office/ branch in Russia and hiring local staff, simultaneously establishing partnerships with either local SIs or companies in adjacent service areas

3 Acquiring or creating JV with capable local company/ product team for developing and servicing products for the Russian market, ensuring sufficient motivation and market reach

4 Acquiring or creating JV with capable local company/ product team to bring Russian-developed products into Japanese and/or global markets

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