

The following brief analysis examines what factors local businesses consider as their performance and success. The analysis was based on the database of the IEER April 2014 Business Climate Survey, which is Hungary's largest company-wide survey of its kind. The April survey is based on the responses of 2,606 company executives. The sample was made up of 58% micro enterprises (less than 10 people), 17% of small businesses (between 10-49 persons), 16% of medium-sized enterprises (between 50-249 persons), and 10% of large enterprises (250 persons and above). Thus, our study primarily applies to micro-enterprises. Our results show that the majority of domestic enterprises are proud of the positive characteristics (e.g. quality, uniqueness) of their products and services. The second most common response was that entrepreneurs considered the very survival of their company as a major success. A majority of respondents were proud that they managed to retain customers or attract new ones, and the fact that customers were satisfied with their work. Nearly one in ten respondents pointed out that they managed to maintain or increase staff numbers. Also, nearly one-tenth of interviewees viewed as one of their major achievements the fact that revenue remained the same or even increased.

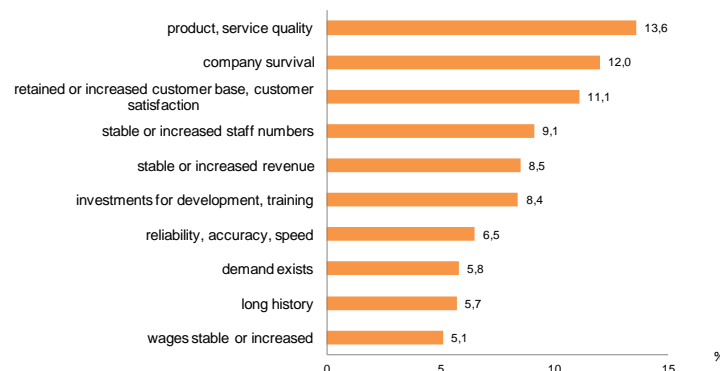
What is considered as the main achievement for local enterprises?

Most of the companies surveyed (13.6%) highlighted the positive features of a product or service as a result for which they were proud. More than one tenth (12%) of firms believe their greatest achievement is that it had not disappeared, that is, they were able to survive despite difficult economic conditions. Another 11% of them were proud that they were able to retain or increase their customer numbers. Nearly one tenth (9.1%) answered that they managed to keep staff numbers steady or even raised their number. The fifth most common (8.5%) response as a company achievement was that there was revenue growth or at least stagnation. For another 8.4% of businesses one of their main results was that they were able to undertake innovations, investments or trainings. Additionally, 6.5% of respondents pointed out that their work was reliable, accurate and fast. A further 5.8% of them consider it a success that there is adequate demand for their products and services. Finally, 5.7% of them responded that one of their main achievements is that their company has a long history.

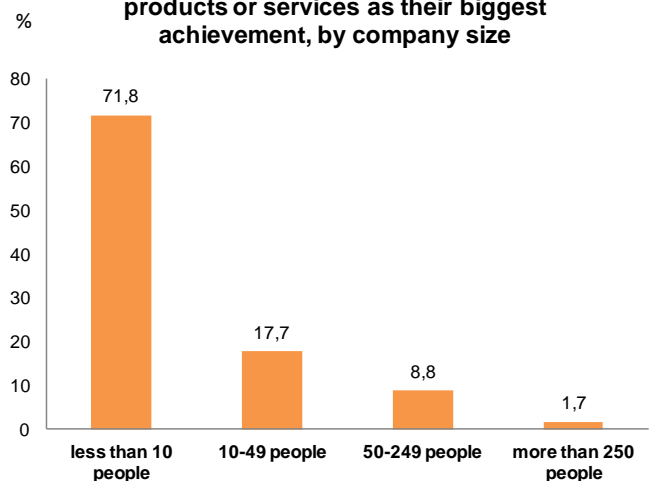
It is important to point out that 60.5% of respondents were unable or unwilling to consider any factors as a business achievement.

A 2012 survey of small and medium-sized enterprises in the United Kingdom included a question about the meaning of success to local entrepreneurs. The results of this research is similar to the Hungarian data in that in both countries a substantial number of businesses regard it as an important achievement if they were able to retain or increase customer numbers and customer satisfaction. Furthermore, entrepreneurs from both countries regard it as important as an indicator of success to maintain and increase staff numbers as well as maintain and increase revenues. An interesting difference between the two countries is while

What do entrepreneurs regard as their main achievement?



Ratio of firms with positive features of their products or services as their biggest achievement, by company size



Hungarian respondents pointed out achievements that were closely related to their businesses, in the UK some personally associated success factors were considered, such as the entrepreneur's personal satisfaction, accomplishment or better quality of life.

The positive characteristics of company products and services

One of our main results was that 13.6% of respondents viewed the positive characteristics of their products and services as their foremost achievement.

By company size, it can be observed that the largest proportion (71.8%) of those which mentioned the positive qualities of their company's products or services as their major achievement were micro companies (below 10 persons). In terms of economic sectors, we can state that service firms had a significantly higher proportion (52.7%) highlighting these factors compared to retail (17.2%), industrial (16.3%), or construction (13.8%) businesses. Domestic-owned firms and companies producing only for the domestic market also mentioned these factors in a higher proportion than those companies with an entire or part foreign ownership background, as well as those that produce for foreign markets.

Company survival

More than one in ten (12%) Hungarian entrepreneurs feel that simply company survival is an achievement.

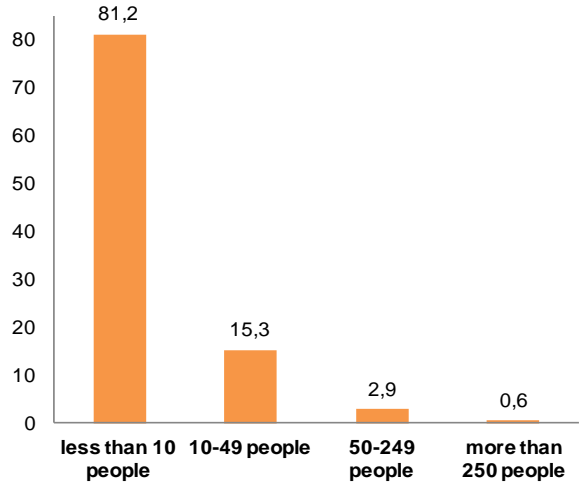
By company size, the fact that a business has not yet gone bankrupt was mentioned the most often by the smallest businesses (81.2%) with maximum 10 employees and a significant proportion of those with between 10-49 employees (15.3%). For companies with between 50-249 persons, this proportion is only 2.9%, compared with 0.6% for the largest firms. Thus, proportion of those who mentioned this factor decreases when increasing company size. In terms of ownership structure, it can be seen that the vast majority (96.7%) were purely domestic-owned firms which felt that company survival was one of their main achievements. Significantly different proportions mentioned this factor based on economic sectors and export ratio, with 48.4% firms being in the services sector and 75.8% of those producing only for the domestic market.

Retain or increase customers, customer satisfaction

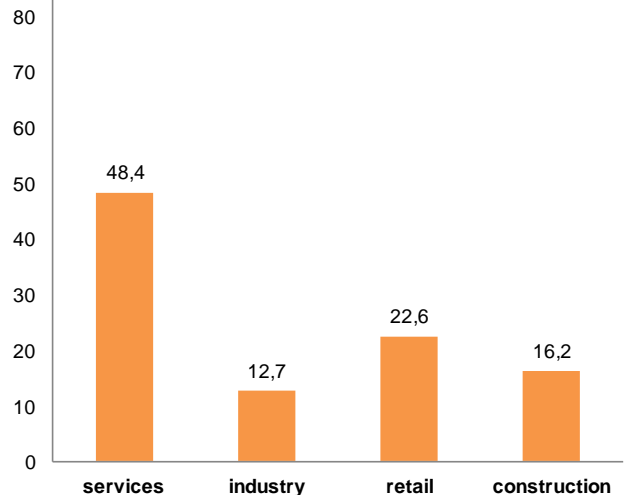
To retain or increase the number of customers and customer satisfaction was reported by roughly one in ten (11.1%) respondents.

As before, the largest proportion (80.8%) of firms which consider this as one of their main achievements comes from the smallest companies, whereas by economic sectors it's once again the services sector (61.0%) which is the highest. As for ownership structure, predominantly domestic companies (98.2%) mentioned this category, while by export

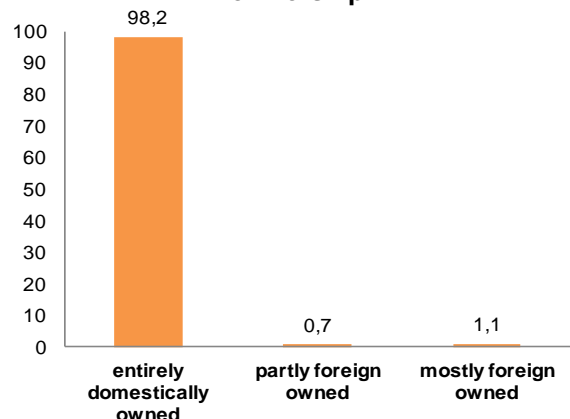
Ratio of firms referring to survival, by company size



Ratio of firms referring to survival, by economic sectors



Ratio of firms referring to retained or increased customer base and customer satisfaction, by foreign ownership



activity this was true of producers for only the internal market (74.7%).

Steady or increased staff numbers

A total of 9.1% of respondents considered that one of their main achievements is that they were able to maintain steady staff numbers or even increased the number of their employees.

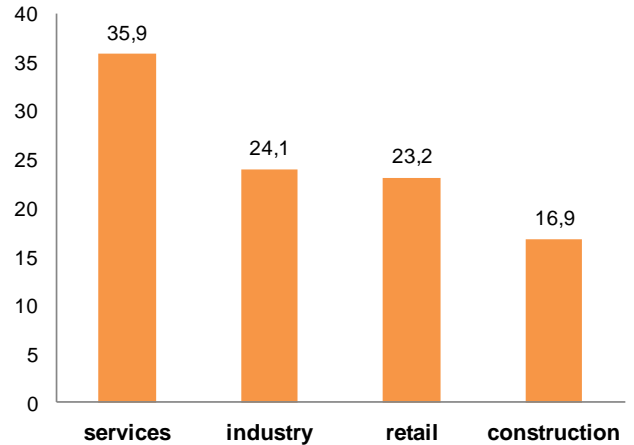
In terms of company size, a higher proportion was reported by firms with less than 10 persons (40.9%) and among those with 10-49 persons (31.2%). As for economic sectors, services (35.9%) reported a higher proportion; by ownership structure this was true for purely domestic-owned companies (87.1%); finally in terms of export activity, this was apparent for those that produce for the internal market only (64.1%).

Revenue is maintained or increased

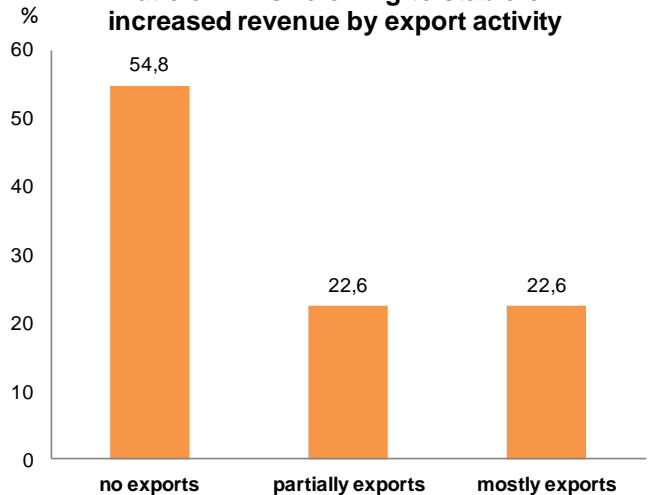
In all, 8.5% of firms were most proud of a maintained or increased turnover. In terms of company size, the highest proportion was among the smallest firms (45.2%) whereas with regard to economic sectors industrial firms (30.5%) and the services sector (36.4%) reported this in the highest proportion; in terms of share of foreign ownership, this was true for those with a purely domestic ownership structure (76.1%); as for export ratio, this was so for producers for the internal market only (54.8%).

Source: Gray – Saunders – Goregaokar (2012): *Success in challenging times: Key lessons for UK SMEs*.
https://www.surrey.ac.uk/sbs/files/Success_in_Challenging_Times_Full_Findings.pdf

Ratio of firms referring to stable or increased staff numbers, by economic sectors



Ratio of firms referring to stable or increased revenue by export activity



Macroeconomic trends: The Russian financial crisis in light of world oil prices and economic sanctions

The 2014 Russian financial crisis including a 59% devaluation of the Russian ruble was directly caused by a sharp decline in world prices for crude oil and the resulting budgetary problems caused by the loss of export earnings. However, the conditions for the financial crisis were already in place long before the collapse of oil prices, and are mainly due to the economic sanctions imposed on Russia. The ruble crisis peaked on 15-16 December 2014, when the US dollar exchange rate exceeded 75 rubles. However, the mid-year central bank interventions and the raise of interest rates three times managed to have temporarily stabilized the ruble exchange rate. Yet the central bank's efforts at sustainability largely depends on whether the Russian government will succeed in finding a solution to replace dwindling foreign reserves, as well as a replacement for the loss of foreign investments. This is difficult to implement, however, because of the sanctions and record low oil prices. Therefore, the question concerning the successful consolidation of the Russian economy is how long the sanctions remain in force, as well as the direction and extent of world oil price changes in the next few months.

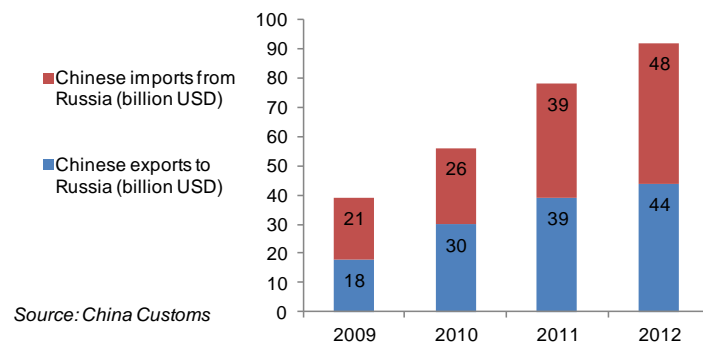
Economic sanctions against Russia

Initially the economic sanctions imposed on Russia after the annexation of the Crimean peninsula in March 2014 enacted by the United States, Canada and the European Union limited travel to only a restricted group of officials, businessmen and politicians. However, with the intensification of the crisis in April, further sanctions were imposed which tightened the previous restrictions. Despite all efforts the conflict worsened in eastern Ukraine, so together with many other states (Japan, Norway, Iceland, Switzerland, Montenegro, etc) new sanctions came into force between July 17 and December 18 in which foreign deposits were frozen as well as limits extended to dominant energy companies (Rosneft, Novatek) and banks (Gazprombank, Vnyesekonombank). These actions have caused significant negative economic effects, thereby triggering a continuous fall in the exchange rate of the ruble.

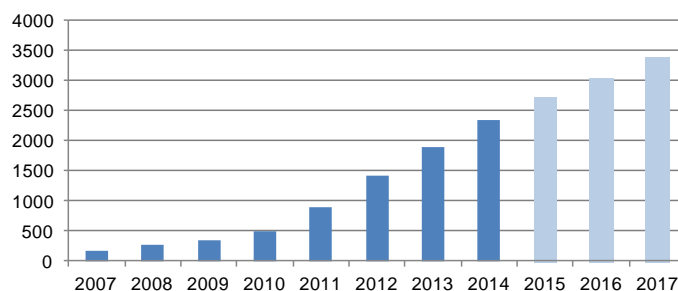
The sharp devaluation of the ruble

The conditions for the depreciation of the ruble against the US dollar were created by the economic sanctions. However, an important role in spreading the crisis was a large reduction in world market prices for crude oil, which was due to two reasons: because of global oversupply due to the pick-up in emerging shale gas and shale oil extraction and a stagnating world economy as a result of decreasing global energy demand. Since mid-summer there has been a steady decline in oil prices, in which the world market price fell from a high of 110 / barrel to 45 USD / barrel, thus the position of the Russian economy became more exposed, because its sustainability is not possible if the oil price level is below 80 USD / barrel. The replacement of lost foreign exchange earnings is a difficult challenge confronting the Russian government, because

Chinese-Russian trade by exports and imports, 2009-2012



USA shale oil production (1000 barrels/day), 2007-2017

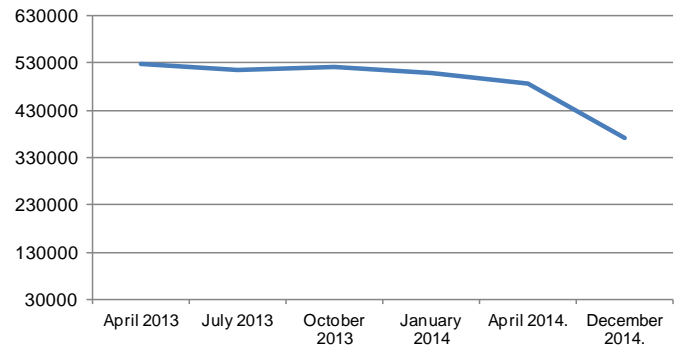


as a result of increasing risks to investors, in 2014 alone funds amounting to USD 80 billion were withdrawn from the country. However, despite these deteriorating conditions foreign currency revenues from other industrial areas of the export sector (chemical, wood, metal, military) as well as limits on substitutable foreign import goods by the Russian government has maintained for now a positive trade balance, albeit the surplus is declining. Currently USD 370 billion is available to the Russian government to hedge the loss of energy revenue, which seems to be sufficient protection. However, currently there is no realistic chance for increasing the state's foreign exchange reserves. In addition, of the current USD 370 billion USD 100 billion is invested in two large pension funds, which can't be used to consolidate the economy. Therefore, it can be stated that Russian foreign exchange reserves can be applied only to a limited extent for crisis management, thus to remedy the deterioration of the exchange rate and to make up for the loss of energy revenue a new solution is necessary – if it is possible taking into account current oil prices.

Shale oil and shale gas

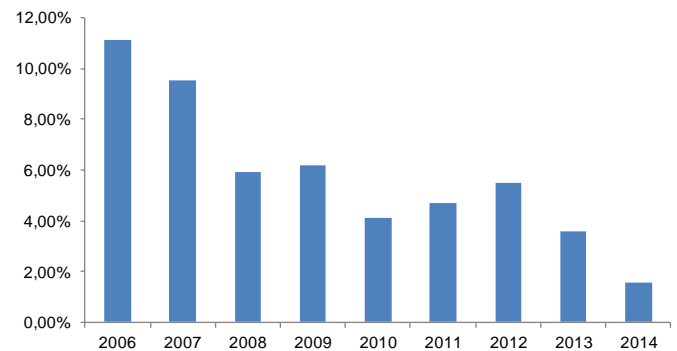
Since 2008 the United States has placed great emphasis on the production of shale oil and shale gas. The production process is based on a new method using hydraulic fracturing (fracking), in which cost-effectiveness and the system of small oil wells could revolutionize the global energy markets. As a result of the application of the emerging shale technology, there has been a significant drop in prices leading to a surplus for consumers, while for major oil and gas producing countries, including Russia, it has caused a loss of revenue. However, in the global price-setting the OPEC, especially Saudi Arabia also plays an important role, since a change in production levels can also affect global crude oil prices. However, OPEC members decided to maintain the current level of supply since they don't want to cause a decline in their market share by cutting production. In fact, the drop in crude oil prices has increased the effects of existing sanctions on Iran, which is fully in line with Saudi Arabia's regional power interests. The new technology of shale gas and shale oil have further untapped potential; indeed, because the hydraulic fracturing extraction techniques have relatively low production costs compared to the traditional forms of mining processes, especially in difficultly approachable areas, mainly in underwater deposits. Therefore, the future global market position of states with traditional sources of energy will be significantly affected by the American innovations implemented in the sector through changing the oil price.

Change in Russian foreign currency reserves (billion USD), April 2013-December 2014



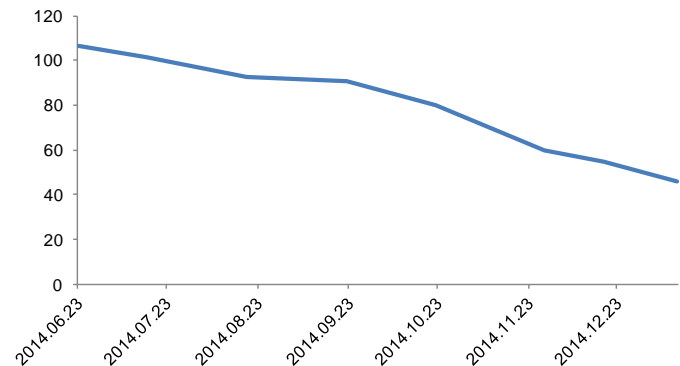
Source: CBRF

Change in the balance of payments in Russia as a percentage of GDP, 2006-2014



Source: Trading Economics

Change in world oil prices (USD), June-December 2014



Source: FOREX

Russian central bank policy

Due to changes in crude oil prices Russian foreign exchange reserves are significantly decreasing thus the management of the crisis can't be based on them for very long. In recognition of this, the Russian central bank began a restrictive monetary policy in order to curb inflation and improve investor confidence, using bank interventions in 2014 to balance the USD 80 billion deficit in its foreign exchange reserves. To this end, the Russian central bank raised interest rates three times since October, with the result that the base rate on 16 December from the initial 8% increased to 17%. As a result, the ruble exchange rate fell to consolidate around the 66 RUB / USD level, but the deterioration in investor confidence and all the conditions for a further drop are still apparent. The biggest danger is that debt repayment conditions of firms are worsening, causing a rise in non-performing loans, to the extent that large companies such as industry leader Rosneft have lobbied the central bank for assistance, which in turn significantly decreases foreign investor confidence.

Crisis management options

There are not many tools at Moscow's disposal to deal with the crisis, which makes the use of external assistance necessary. Currently China is able to provide major financial support, and signed a USD 400 billion worth petroleum agreement and a 150 billion Yuan (24 billion USD) worth currency exchange agreement with the Russian government. The latter would replenish the loss of Russian foreign exchange reserves, and would make the Yuan a trade settlement currency between the two countries, which could reduce the exposure of Russia against the USD. The Chinese initiatives however, unable to change the two most important challenges facing the Russian economy: the western economic sanctions and the negative impact of low oil prices on the world market, even with a growing trade volume to China. Therefore, it is projected that Russia's future opportunities for development will foremost be affected by these two cardinal factors, while closer financial and trade co-operation developed with China will only be secondary.

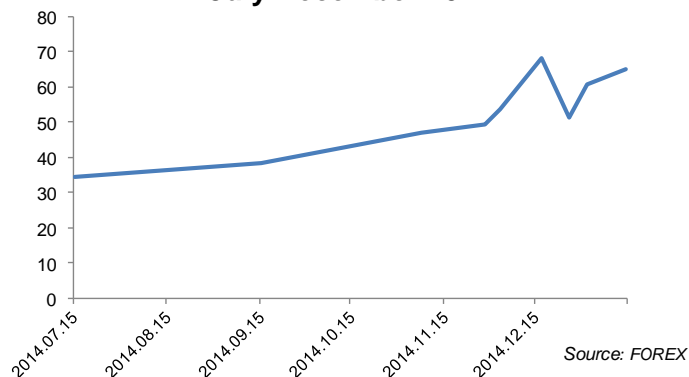
Source:

Economist – Russia: a wounded economy
<http://www.economist.com/news/leaders/21633813-it-closer-crisis-west-or-vladimir-putin-realise-wounded-economy>

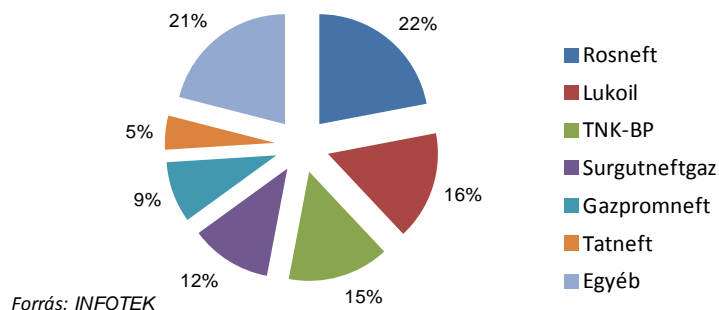
Economist: The new economics of oil – Sheiks vs. Shale
<http://www.economist.com/news/leaders/21635472-economics-oil-have-changed-some-businesses-will-go-bust-market-will-be>

EIA Drilling Productivity Report
<http://www.eia.gov/petroleum/drilling/>

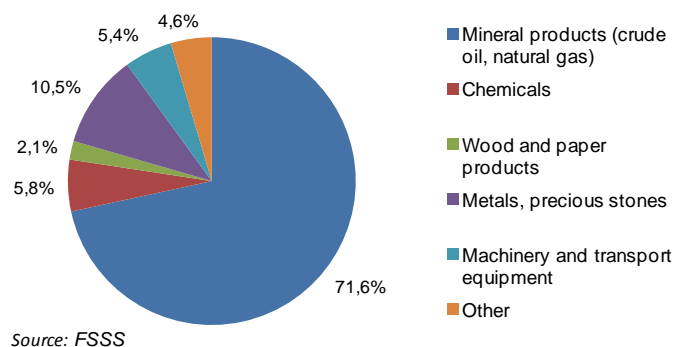
Change in the USD/RUB exchange rate, July-December 2014



Distribution of Russian oil and natural gas by companies, percentage (2011)



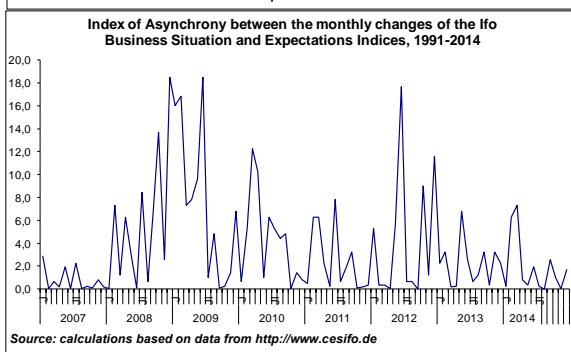
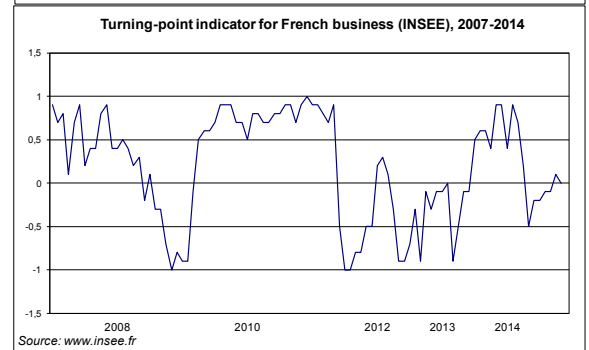
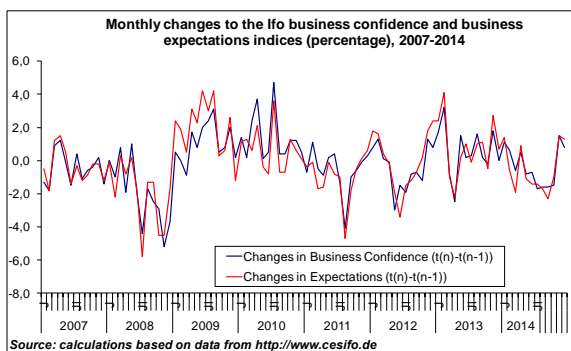
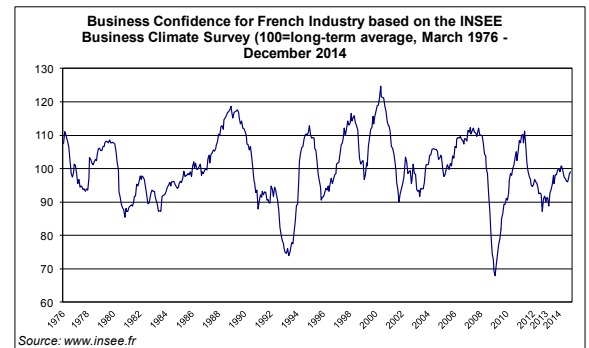
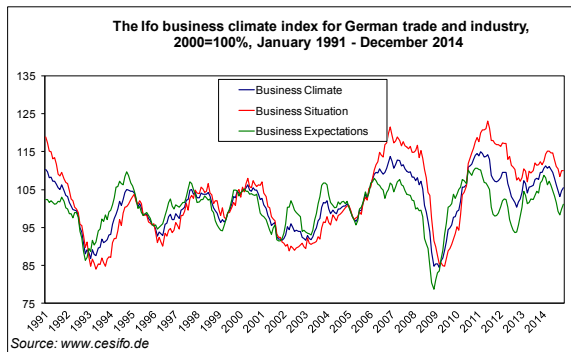
Distribution of Russian exports by type, percentage (2013)



International trends

The Ifo Business Climate Index for industry and trade in Germany rose in December to 105.5 points from 104.7 points in November. The business climate index has reached a turning point in November. Assessments of the current business situation are similar to last month's data. Expectations with regard to the months ahead are also brighter. The gap between the current business situation and the expected developments, as calculated by the IEER Index of Asynchrony, increased in December, so the business confidence index showed higher uncertainty than in the previous month. According to Ifo analysts, the dropping oil prices and a falling euro exchange rate are seasonal gifts to the German economy. (Source: Ifo, <http://www.cesifo-group.de>)

Results from the December survey by the French statistical office (INSEE) show that the business climate of industry in France has slightly risen compared to the previous month. The composite indicator which measures it increased by 1 point (after 1 point in November) and stands at 1 point below its long-term average. The turning-point indicator is in the zone indicating an economic uncertainty. The balance of opinions on past change in production has increased by 4 points and is closer to its long-term average. The balance of opinions on personal production expectations has decreased compared to the previous month and it is closer to its long-term average. The balance of general production expectations, which represents business managers' opinion on French industry as a whole, is still sluggish and has not changed compared to the previous month. (Source: INSEE, <http://www.insee.fr>)



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