HSBC *Purchasing Managers' Index*™ Press Release

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compiled by markit

HSBC Russia Services PMI® (with Composite PMI data)

Services drove Russian private sector growth in July

Key points

- Services activity growth accelerates while manufacturing edges closer to stagnation.
- Overall output growth faster than in June, but weaker than long-run trend.
- Input price inflation weaker than historic survey average.

Summary

The latest *PMI*® data compiled by Markit for HSBC showed that Russian service sector growth quickened slightly in July. In contrast, manufacturing output growth slowed to near stagnation as new orders fell.

The headline figure for the survey is the seasonally adjusted Services Business Activity Index, a single-figure measure designed to track changes in total Russian services activity compared to one month previously. Readings above 50.0 signal growth of activity compared to the previous month, and below 50.0 contraction. The Index rose in July to 56.9, from 55.1 the previous month. The rate of growth signalled was the second-fastest in the current 11-month sequence. Manufacturing production rose only marginally (50.6), while a Composite Output Index covering both sectors posted 54.6, up from 53.8 in June and remaining weaker than the pre-crisis trend.

Gains in new business supported the latest increase in services activity. The rate of expansion in new contracts was solid, but weak in the context of historic survey data. Manufacturing new orders fell marginally, and new business growth at the composite level slowed to an eight-month low.

Russian service providers continued to reduce their levels of incomplete business in July, attributed to both improved productivity and spare business capacity. Backlogs fell at a similarly marked rate in manufacturing.

Services employment increased for the ninth month in a row in July. The pace of workforce growth eased further from May's high, and was slightly weaker than the survey's long-run average. Manufacturers registered only marginal workforce growth during the month.

Input price inflation in the Russian service sector increased slightly in July. Sources of rising costs included salaries, marketing, renting and telecommunications. Transport & Storage registered the fastest overall rate of inflation. Input price inflation in manufacturing was little-changed from June. Meanwhile, prices charged by service providers rose at the fastest rate since February, while output price inflation in manufacturing eased to a 12-month low.

Comment

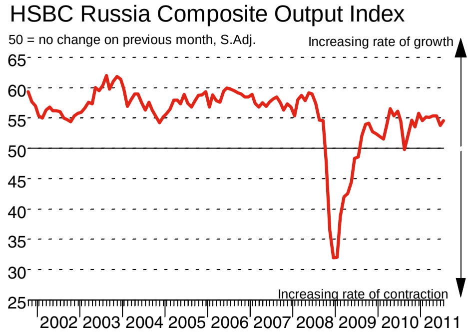
Commenting on the Russia Services and Composite *PMI* data, Alexander Morozov, Chief Economist (Russia and CIS) at HSBC, said:

"Once more, faster output growth in the service sector has more that offset the weakening of manufacturing growth, pushing up overall economic growth in Russia in July, the HSBC Russia PMI report says. Thereby, the diversion in dynamics of the service sector and manufacturing that emerged a few months ago has further widened in July. In essence, domestic consumer demand has become the key and the only growth driver in Russia. There would be nothing wrong in this growth model in an environment of stable global economic outlook and steady exports growth. Yet, high commodity prices, sovereign debt problems in the Eurozone and the US and policy tightening in China weighs negatively on the global economy while Russian exports stagnate. Therefore, expecting output growth in the service sector to keep getting momentum for some time providing further boost to GDP growth, we believe that economic growth in Russia will moderate in two or three quarters from now toward its potential rate of about 3%, on our estimate.

Importantly, stronger growth in the service sector has intensified cost pressures in the economy and pushed up output prices too. This points to a likely reversal of the recent inflation moderation trend, although it is worth waiting for another month or too before this finding can be validated. Interestingly, the composition of cost growth drivers has changed this time. Higher energy, fuel and transportation costs used to be the key drivers of cost pressures in the service sector, but were not widely reported as factors in July. Instead, the intensification of cost pressures - according to anecdotal evidence provided by companies - comes from higher wages, marketing, renting and telecommunication costs. This new group of leading cost-push factors reflects the needs of expanding business and should be easier to deal with as compared to energy costs, for instance. Expanding business can pass on its costs on consumers. This explains the narrowed gap between Input Prices and Output Prices PMI Indexes.

That said, we expect y-o-y headline CPI growth to continue improving. The ongoing food deflation, in anticipation of good agricultural output this year, and a strong positive base effect, appear to prompt a deceleration of consumer price growth despite faster price growth in the market services sector."

Historical Overview



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Notes to Editors:
The HSBC Russia Services *PMI* is based on data compiled from monthly replies to questionnaires sent to purchasing executives in over 300 private service sector companies. The panel has been carefully selected to accurately replicate the true structure of the services economy.

The HSBC Russia Composite *PMI* is a weighted average of the Manufacturing Output Index and the Services Business Activity Index, and is based on original survey data collected from a representative panel of over 600 companies based in the Russian manufacturing and service sectors.

Survey responses reflect the change, if any, in the current month compared to the previous month based on data collected mid-month. For each of the indicators the 'Report' shows the percentage reporting each response, the net difference between the number of higher/better responses and lower/worse responses, and the 'diffusion' index. This index is the sum of the positive responses plus a half of those responding 'the same'.

Diffusion indexes have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change. An index reading above 50 indicates an overall increase in that variable, below 50 an overall decrease.

The *Purchasing Managers' Index* (*PMI*) survey methodology has developed an outstanding reputation for providing the most up-to-date possible indication of what is really happening in the private sector economy by tracking variables such as sales, employment, inventories and prices. The indices are widely used by businesses, governments and economic analysts in financial institutions to help better understand business conditions and guide corporate and investment strategy. In particular, central banks in many countries use the data to help make interest rate decisions. *PMI* surveys are the *first* indicators of economic conditions published each month and are therefore available well ahead of comparable data produced by government bodies.

Markit do not revise underlying survey data after first publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series. Historical data relating to the underlying (unadjusted) numbers, first published seasonally adjusted series and subsequently revised data are available to subscribers from Markit. Please contact economics@markit.com.

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HSBC Group operates in Russia through OOO HSBC Bank (RR). HSBC Russia provides a wide range of corporate banking, investment banking and financial markets products and services to corporate and institutional customers.

About Markit:
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About PMIs:
Purchasing Managers' Index™ (*PMI*®) surveys are now available for 32 countries and also for key regions including the Eurozone. They are the most closely-watched business surveys in the world, favoured by central banks, financial markets and business decision makers for their ability to provide up-to-date, accurate and often unique monthly indicators of economic trends. To learn more go to www.markit.com/economics.