State-Owned Enterprises in Russia
Presentation at the OECD Roundtable on Corporate Governance of SOEs

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Introduction

State ownership is still important and increasingly so in Russia despite of large-scale privatization

Definition of SOE:
- Enterprises where the state has significant control, through full, majority, or significant minority ownership.
- Direct and indirect ownership at any level of government, at least 10%

Main government objective of state ownership: industrial development, innovation, diversification of the economy

However, holding structures, specific legal constructions, and reduced competition may not be conducive to achieving these goals.
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Corporate governance in Russian SOEs
Conclusion

Outline

- The extent of state ownership in Russia
  - Legal forms of SOEs in Russia
  - State ownership in the aggregate statistics: Extent and sectoral distribution
  - State ownership in the largest Russian enterprises
- Corporate governance in Russian SOEs
  - Trends and objectives of the policy and management of state property in Russia
  - Corporate governance problems
  - The new State Corporations: Examples and specific problems of corporate governance
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Legal forms of SOEs in Russia

- **Joint Stock Companies**: mostly OAO, sometimes ZAO. Examples: Gazprom, Sberbank, Russian Railways, Transneft
- **Unitary Enterprises** at the federal, regional, or municipal level (FGUP, GUP, MUP). Examples: Rosoboronexport, Post of Russia, Rosspirtprom
- **State Corporations**. Examples: Vnesheconombank, Rosnanotekh, Rostekhnologii, Rosatom.
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Extent of state ownership (1)

- Aggregate statistics for firms and organizations – including large and small commercial business firms, non-commercial organizations, and state institutions as long as they are registered as legal entities.
- Fraction of firms with 100% state and mixed (state and private), domestic ownership (2007):
  - among all firms and organizations: 11%
  - in employment 39%
  - in capital investment: 32%
  - in fixed assets (state ownership greater than 50%): 23%
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Extent of state ownership: Capital investment

- State and municipal
- Mixed state and private, domestic
- Private (domestic and foreign, incl. non-profit)

Carsten Sprenger
State-Owned Enterprises in Russia
Sectoral distribution

- Among SOEs, there is a concentration in fuel and energy and the military-industrial complex.
- Among different industries: Output shares in 2006 (fully state-owned and mixed domestic)
  - Manufacturing industry: 19.2%
  - Fuel production: 15.3%
  - Metallurgy: 11.6%
  - Chemical industry: 25.7%
- Banking industry: 45% of total assets held by state-controlled banks (estimation by Vernikov, 2007)
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Overall declining state ownership although the process has slowed down during recent years

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## State Ownership in the largest Russian companies (1)

<table>
<thead>
<tr>
<th>Rank</th>
<th>Company name</th>
<th>Market cap (mln dollars)</th>
<th>State share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Gazprom</td>
<td>236187</td>
<td>50.1</td>
</tr>
<tr>
<td>2</td>
<td>Rosneft</td>
<td>92968</td>
<td>84.6</td>
</tr>
<tr>
<td>4</td>
<td>Sberbank</td>
<td>51058</td>
<td>60.6</td>
</tr>
<tr>
<td>9</td>
<td>Gazprom Neft</td>
<td>22787</td>
<td>73.7</td>
</tr>
<tr>
<td>12</td>
<td>Vneshtorgbank (VTB)</td>
<td>18823</td>
<td>77.5</td>
</tr>
<tr>
<td>15</td>
<td>RusHydro</td>
<td>16738</td>
<td>60.4</td>
</tr>
<tr>
<td>22</td>
<td>Rostelekom</td>
<td>8349</td>
<td>50.7</td>
</tr>
<tr>
<td>23</td>
<td>Unified National Electric Grid (FGC UES)</td>
<td>6377</td>
<td>77.7</td>
</tr>
<tr>
<td>26</td>
<td>Bank of Moscow</td>
<td>5531</td>
<td>44.0</td>
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<tr>
<td>32</td>
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Ranks are from the list of the largest 200 Russian companies by market capitalization, compiled by the Expert Rating Agency.
Federal and regional governments control about 40% of the stock market capitalization in Russia in 2007, compared to only 24% in 2004 (Estimates by Troika Dialog).

Reasons:
- Increase of minority stakes up to a controlling level (e.g. Gazprom)
- Acquisition of formerly private companies (e.g. Yukos, Sibneft, VSMPO-Aвисма)
- Large IPOs (Rosneft, VTB)

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Corporate governance in Russian SOEs
Trends in state property policies

- Increase of control in strategic sectors and enterprises
- Creation of state holdings
- Transformation of unitary enterprises into open JSCs
- Privatization of small and medium-sized SOEs
- Sector reforms: utilities, railways
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Size of the government stake in SOEs at the federal level (JSCs only):

Jan 1, 2002

- Less than 50%
- More than 50%, but less than 100%
- 100%

Jan 1, 2008

- Less than 50%
- More than 50%, but less than 100%
- 100%
Strategic enterprises and sectors

- **Strategic enterprises**: A Presidential Decree with list of more than 1000 SOEs from 2004 (changed several times and reduced since then): Privatization and new share issues require explicit approval of the President.
  - Examples: Transneft, Gazprom, holding company Rosneftegaz, diamant producer Alrosa.

- **Strategic sectors**: Law on foreign investment in companies with strategic impact on the national security of the RF: list of sectors where foreign owners need an explicit government permission to acquire a controlling stake of a company.
  - Examples: military-industrial complex, radioactive materials, subsoil natural resources of federal importance, media.
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- Gazprom: Sibneft became Gazprom Neft (2005)
- Rosneft: former Yukos assets (since 2004)
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Recently created state holdings

- **United Shipbuilding Corporation**: shipyards in the North West, North and Far East of Russia, many of them supplying the Russian navy. Will start to operate on April 1, 2009.

- **United Aircraft Corporation**: unites all major Russian aircraft constructors such as Sukhoi, MIG, Tupolev, Ilyushin, and Irkut (formerly private), two leasing companies and the foreign trade company Aviaexport.

- **Rostekhnologii**
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- **Rostekhnologii**
Objectives of state ownership

- Equity objectives and public goods, e.g. energy security, supply of services in spite of regulated prices, non-commercial media
- Industrial policy objectives: infrastructure investments, enterprise restructuring, vertically integrated structures that can survive international competition, re-integration of research institutions and industrial enterprises

How are these objectives formulated?
- not always clearly defined in the founding laws of SOEs
- holding companies define objectives of subsidiaries autonomously
- no indication how trade-off should be handled
- no system of remuneration for pursuing non-commercial objectives
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- Double agency problem
- Appointment and work of state representatives
- Transparency issues
- External corporate governance mechanisms weak: threat of bankruptcy, threat of takeover, product market competition
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State Corporations (SCs): Examples

- **Bank for Development**: Financing of infrastructure projects, special economic zones, and the support of SMEs in order to enhance innovation, competitiveness and the diversification of the Russian economy.

- **Rosatom**: Civilian and military use of nuclear energy, implementation of the Federal Program on the Development of the Nuclear energy industrial complex.

- **Rostekhnologii** (Russian Technologies): Includes enterprises from the military-industrial complex (e.g. helicopters, radioelectronics, ammunition, foreign trade with armament), and companies in civilian sectors such as mechanical engineering, auto engineering, metallurgy, air transportation.
State Corporations (SCs): Examples

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2. Unclear responsibilities of boards of directors: no criteria for evaluation of the degree of target achievement.
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SCs: Specific corporate governance problems (2)

4. Lack of separation of regulation and state property management
5. Exemption from the bankruptcy law
6. Reduced disclosure requirements
7. No ownership entity
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Conclusion

- Creation of state holdings and ad hoc legal forms may not be conducive to achieve the industrial policy goals
  - Monopolization is not a guarantee for innovation and competitiveness
  - Holdings: small synergy effects, formulation of objectives for subsidiaries is left to the company
  - Corporate governance problems, particularly severe in State Corporations
- Improvement of corporate governance arrangements in the newly created structures needs to be addressed with priority
- More and better data is needed to assess the extent of state ownership and to measure the performance of SOEs relative to their private peers.
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