



# **Russian Corporate Governance Roundtable Meeting**

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# Equitable treatment of minority shareholders in SOEs

- Main challenges
  - Preventing abusive behavior by the state
  - Creating incentives for managers

# Preventing abuse of voting power by the state

- Supermajority provisions
- Board composition – more independent directors on board
- Large private shareholder as a counterbalance to state

# Are minority shareholders underrepresented in Russian SOEs' boards?

- Lazareva, Rachinsky and Stepanov (2008). Survey of about 1000 Russian large and mid-size firms.
- Lazareva and Summanen (2008). Survey of about 240 Russian firms
- Conclusion of the two studies: no relationship between state ownership and the presence or share of independent directors on board.

# Are minority shareholders underrepresented in Russian SOEs' boards?

- S&P study (2007) of 75 largest Russian companies reveals a somewhat different picture:

## **% of board members**

	44 private companies	31 government companies
Insiders	64	70
Representatives of minority shareholders	10	19
Unaffiliated directors	26	11

# Are minority shareholders underrepresented in Russian SOEs' boards?

- CEFIR study (2005) on behalf of IFC and IDA of 442 companies:
  - 30% of companies have independent directors
  - Among companies where state is the largest shareholders only 15% have independent directors

# Minority shareholder representation on board. Conclusion

- Overall there is some, albeit not very robust, evidence that minority shareholders are somewhat underrepresented in SOEs' boards as compared with boards of private companies

# Large private shareholder as a counterbalance to state

- Multiple large shareholders can be beneficial for minority shareholders because:
  - Checks and balances
  - Fights for control (need to attract votes or buy shares of minority shareholders)
- Examples: Norilsk Nickel, VimpelCom
- In the S&P 2007 sample in 12 out of 33 companies in which state has > 25%, state control is counterbalanced (to various extents) by a large (>25%) private blockholder
- However, fights for control are *unlikely* to occur in SOEs
- So, the only mechanism is counterbalancing the state voting power at AGM and on board

# Right to obtain information

- Absent relevant information either shareholders or independent board members are likely to be passive
- But the access to information is largely controlled by management
- The problem is especially relevant for SOEs as the goals of the state are often unclear a priori (later on that).

# Transparency and disclosure of information by SOEs

- Computation based on last year S&P T&D study.
- Table here
- Overall, SOEs are not less transparent than companies with a private dominant shareholder
- However, they are worse in disclosing financial and operational information

# Unclear goal of the major shareholder (state)

- Why unclear?
  - Who is actually the shareholder?
- Why is it bad?
  - No clear goal  $\Rightarrow$  no clear objective for management
  - Coupled with lack of market discipline and lack of monitoring by the major shareholder  $\Rightarrow$  no incentives/perverse incentives for management

# Empire building incentives

- Gazprom's management in July 2008: over 7-10 years plan to achieve MCap of \$1 trillion
- Rosneft's management in July 2008: raise MCap by 60% over a few years, get into top 3 oil and gas companies by 2020
- Sberbank's management in April 2008: double MCap and become a top 10 financial institution over 5 years
  
- Maximizing long-term market capitalization is *not equivalent* to maximizing long term *share price*.
- In particular, it means reinvesting all cash or at least keeping it in the firm rather than paying out some to shareholders
- Does it maximize stock price?

# Conclusions

- Some regulatory measures might help (like requiring more independent directors or demanding more transparency)
- However, no matter what regulations you put in place, minority shareholders in Russia will not be treated fairly unless the controlling shareholder wants that himself/herself.
- Potential forces:
  - Need to raise money from the public (esp. abroad)
  - Desire to do acquisitions abroad