

## ТЕОРЕТИЧЕСКИЕ И ЭМПИРИЧЕСКИЕ ИССЛЕДОВАНИЯ

# RUSSIAN LISTED COMPANIES: CONTROLLING SHAREHOLDERS AND THEIR CONDUCT

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The high concentration of ownership has remained the key feature of Russian companies, including publicly traded companies. Even at the peak of the romance with Western portfolio investors, the controlling shareholders of Russian listed companies put the full control at the top of their priorities. In the 2000s, the Russian listed companies' controlling shareholders sought gradual accommodation with minority shareholders and a gradual acceptance of Western corporate governance practices and thus espoused market capitalization as an important strategic goal. This was reversed in the 2010s as the rapidly tightening grip of the state on private business and mounting restrictions on Western investment in the Russian economy took hold. It has also reduced a market demand for Western best corporate governance practices on the part of Russian controlling shareholders. After 2014, most controlling shareholders of Russian listed companies have switched to the strategy of acting as junior partners of the state. This switch has largely diminished their market orientation and the demand for Western-style corporate governance. The future of the large Russian listed companies fully depends on the relations of their majority owners with the Russian state and thus remains uncertain.

*Keywords:* listed companies, ownership structure, state, controlling shareholders, IPO, monetization of property rights, corporate governance.

*JEL:* D02, D03, D021, F31, F59, G18, G30, G32, G34, G38.

## INTRODUCTION

This article analyzes the ownership policy, ownership structure and key decisions of

controlling shareholders of Russian non-state listed companies. This analysis is made in the context of the evolving role and interests of the Russian state and its impact

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on the controlling shareholders' conduct. The high concentration of ownership, as experts point out, is the most important singular point for understanding the post-privatization behavior of Russian companies from the beginning up to end of 2010s [Sprengrer, 2002; Guriev, Rachinsky, 2004; Corporate Governance in Russia..., 2004; Entov et al., 2009]. It is stressed that the risk of expropriation of minority shareholders by controlling shareholders represents the main risk for the newly-emerged Russian public companies. Improvement of legal regulation and law enforcement by the state were seen as a key to solving this problem. In mid 2000s, few experts pointed to the threat of the expropriation of controlling shareholders of both private and listed companies by the Russian state as a key problem [Lazareva, Rachinsky, Stepanov, 2007]. Yet, since late 2000s, the ownership structure strategy pursued by controlling shareholders of Russian listed companies, the evolution of the Russian state's policy towards big private business and outside investors, both domestic and foreign, as well as the drivers behind this policy have dropped from the focus of Russian scholarly and business analysis. Those few scholars who recently referred to the ownership structure of the Russian listed companies simply suggested that it poses threats to minority shareholders and diminishes their attractiveness for investors [Zainullin et al., 2018].

The bulk of literature on Russian listed companies as corporate entities has been focused on mapping formal aspects of their corporate governance practices (board and board committees' composition, number and criteria of independent directors, board evaluation, etc.) from the point of their consistency or inconsistency with the Western corporate governance best practices and the Corporate Governance Code by the Bank of Russia [National Report on Corporate Governance, 2014; 2015; 2017; 2018; Filatov, Dzhuraev, 2014; Assessment of Corporate Governance..., 2017; Russian Code of

Corporate Governance, 2014; Shevchuk, 2013; Modern Corporate Governance..., 2017]. This mainstream approach was set by the state regulator (the Bank of Russia) and is clearly reflected in its surveys of corporate governance practices [Bank of Russia, 2017a; 2017b; 2018]. This approach is based on the implicit assumption that the fundamental interest of controlling shareholders is to move toward the model of Western corporation (i.e. dispersed ownership) and the goal of higher market capitalization should be their key business priority. This implies that the domestic business environment in Russia, despite its serious defects, has been evolving towards the one in which Western companies operate, and that the Russian state has been interested in large number of foreign portfolio investors to come making ownership of Russian companies much more dispersed.

However this approach dismisses evidence of the reverse trend in the Russian politics and economy in the 2010s. In face of the expanding role of the state in the Russian economy in 2010s, experts refocused from analyzing companies' private ownership and the related corporate governance issues to analyzing the expansion of the state ownership in terms of the post-privatization "failures of the market" and the ways of improving governance practices in state-owned companies [Radygin, Simachev, Entov, 2015; Abramov, Radygin, Chernova, 2016; Abramov et al., 2017]. Despite being extremely important, the relations between Russia and the West and the fate of non-state listed companies in the new economic landscape have not been addressed in the prior studies. In previous works we have addressed the ownership structure policy pursued by controlling shareholders of Russian listed companies and their basic business orientation in the context of the evolving role and interests of the Russian state and its vision of the global politics and economy [Belikov, 2019a; 2019b]. In this paper we intend to continue this approach.

This paper seeks to:

- understand the ownership structure of Russian listed companies and thus their nature;
- analyze the conduct of their controlling shareholders;
- include the role of the state and its impact on the conduct of the controlling shareholders into the analysis;
- understand the evolution of the state policy towards the private business since 2000s;
- understand the evolving approach towards corporate governance by controlling shareholders of Russian listed companies.

Specifically, in this research we analyze the ownership structure of Russian listed companies as well as the conduct of their controlling shareholders in the context of the expanding role of the state and its evolving vision of the global politics, which shape the domestic environment for Russian business. Although the analysis is focused entirely on Russian companies, it is also relevant to many other companies from emerging market countries. The conclusions of our paper are useful for investors in stocks of Russian companies.

## OVERVIEW OF OWNERSHIP STRUCTURE

In 2012–2018, the total number of Russian companies listed at domestic and foreign stock exchanges varied from 135 to 85, exhibiting a definite downward trend<sup>1</sup>. The Deloitte survey of ownership structures and corporate governance practices of listed Russian companies in 2012 numbered 135 companies [Corporate Governance Structures..., 2012] and the survey of 2015 numbered 120 companies [Corporate Governance Structures..., 2015].

<sup>1</sup> This figure includes companies listed at Moscow stock exchange as well as at foreign stock exchanges (with exception of AIM).

While 73% of companies, included into the Deloitte survey of 2015, had majority shareholder owning more than 50% of voting shares<sup>2</sup>, 95% of companies in the sample had at least one block holding with 25% of shares. Only four companies in the sample reportedly had two or more block holders, owning between 25 and 50%. The average free float in the sample, according to official data, was 25%. Experts pointed out that, as compared with the survey of 2012, concentration of ownership grew up. According to the survey by S&P of 2006, the ownership structure of 70 largest Russian listed companies looked like the following: 53/59 companies had majority shareholder owning more than 50% of shares, 10/16 companies had had at least one block holding with 25% of shares and the rest declared to have dispersed ownership structure [Entov et al., 2009]. So, in 2000s—2010s, the ownership structure of Russian listed companies remained steadily highly concentrated.

There is a small number of Russian listed companies in which the major shareholder, who exercises operative control, reportedly owns less than 50% of shares. For instance, according to official data of 2018, the largest shareholder of Phosagro owned 43.5%. The largest shareholder of OVK listed company, Otrkytie pension fund, according to official data of 2018, owned 19.8% in the company. LUKOIL has provided a unique for the Russian context history of more than 25 years of close business partnership between “senior” shareholder (V. Alekperov — 27% of shares) and “junior” shareholder (L. Fedun — 10%). Yet, while analyzing ownership structure of Russian companies, both listed and non-listed, one should keep in mind the following factors.

- The official data on ownership structure do not always provide a completely true story of real beneficial ownership. Beneficial controlling shareholder, while

<sup>2</sup> Here and further on, number of shares will mean voting shares.

reporting to own less than 50%, can have higher actual level of control through control of legal entity which owns a significant stake in the listed company, but officially is not affiliated with this major shareholder. Another tool used to disguise actual beneficial control is a private, publicly undisclosed, agreement of the major shareholder of a Russian listed company with an owner of a significant stake in this listed company on taking concerted decisions on all major management and governance issues. The owner of that significant stake, in most cases, has been in long business relationship with the major shareholder, usually as his junior partner.

- The lasting partnership between significant shareholders of a similar or different weight category is a very rare phenomenon in Russia.
- Most widespread practice in Russian companies, both listed and non-listed, is a strong desire of major shareholder to have full control (i. e. over 50% of shares).

OECD experts provided the following explanation for the Russian corporate landscape: “The ability of large businesses to protect their property rights against both the private sector and government intervention resided precisely in their size, giving them an advantage that smaller competitors did not have. Likewise, the size of these conglomerates allowed them to finance themselves more easily and redistribute the cash flows intragroup in the face of an underdeveloped external capital market. Internal mobility of the workforce was also a substitute for an inefficient labor market” [Kostyleva, Lehuedé, 2012, p. 18].

The key factors, which have contributed to cementing high concentration of ownership of Russian companies, both listed and non-listed, over the period after 2012, in our view, are high risks of assets expropriation by raiders with connections in law enforcement bodies and judicial system, weak judicial protection of property rights, authoritarian social and business culture

and a low level of trust in relations among business partners. As a result, real free float of Russian listed companies, with very few exceptions, has not exceeded 25% and for most of them it has been much beyond that level.

The history of IPOs and SPOs of Russian companies is spectacular in terms of understanding the business credo of Russian controlling shareholders. In 2006–2007 which was the peak of Russian firms’ romance with Western investors, stock price multipliers at IPOs of Russian companies reached 16–17 or even 18. Yet, even at that fabulous time controlling shareholders of Russian companies never allowed amounts of stocks, meaningful in terms of governance, to slip from their hands. Russian controlling shareholders used the following ways to retain control at IPOs and SPOs:

- to buy large amounts of newly-issued stocks (up to 50% or even more) on their behalf;
- to buy large amounts of newly-issued stocks through entities controlled by the controlling shareholders which were declared to be unaffiliated with the latter;
- to arrange purchases of significant amounts of newly-issued stocks by close business partners of controlling shareholders with the former taking publicly undisclosed commitments to act on governance issues in concert with controlling shareholders.

Various sources provide somewhat different figures on Russian IPOs. Yet, the figures below, in our view, provide a reasonably reliable aggregate picture of capital attraction by Russian companies through public share offerings (Table 1).

The global financial crisis of 2008 marked a serious drop in the number of Russian IPOs and SPOs. Although, this started to recover in 2010, the year 2014 became the really dramatic turning point. It is not that the total number of public offerings dropped in 2014 dramatically far beyond the level of 2008. It tolled the beginning of the exodus of many large Russian companies from

Western stock exchanges through voluntary delisting. Among them were such flagships of Russian industries as Uralkali, Megafon, NordGold, Polyus, Cherkizovo Group, PIK, Chelyabinsk Zinc Plant. That exodus was a sharp contrast to the growth of global IPO market in 2014–2017 which covered companies from leading emerging markets (see [Baker & MacKenzie, 2017]). It is remarkable that since 2014 Russia has been out of the radar of the Global IPO trends quarterly issued by EY, a very influential analytical source on IPOs.

A number of Russian companies which delisted their stocks from the major foreign stock exchanges, listed their stocks at the Moscow exchange (MOEX). Since 2014, Russian companies have refocused their activity in public offerings on the MOEX, with few exceptions. Yet, the total number of Russian public companies has continued to decline after 2012. According to the overview by the Bank of Russia, the number of domestically listed companies was 84 in 2015 [Bank of Russia, 2017] and 65 in 2018 [Bank of Russia, 2019].

Our analysis of policies pursued by the Russian companies at MOEX has revealed that very often these are much different from a “classic” business strategy pursued by Western corporations and by issuers from emerging markets, which is aimed at raising stock market capitalization through increasing a share in its ownership structure owned by leading global institutional investors and increasing a free float of their stocks. To prove that we provide two following examples from the history of Russian IPOs and SPOs at MOEX after 2014.

- In November 2016, RussNeft company made an IPO of 20% of its stocks. According to the official report on the results of the placement, the share of the controlling shareholder, M. Gutseriev, dropped down to 47%, the demand for shares exceeded the offer by 30%, the major buyers were “physical persons” and 10% of shares were bought by “banks, investment funds, hedge funds and for-

*Table 1*  
IPOs и SPOs of Russian companies  
at Russian and foreign exchanges  
(main markets) (2001–2018)

Year	Russian exchanges	Foreign exchanges	Total
2018	0	0	0
2017	8	5	13
2016	5	2	7
2015	6	2	8
2014	0	2	2
2013	9	7	16
2012	2	8	10
2011	12	8	20
2010	14	4	18
2009	8	5	13
2008	8	6	14
2007	17	17	34
2006	6	12	18
2005	3	6	9
2004	4	1	5
2003	0	1	1
2002	1	2	3
2001	0	0	0

Source: An overview of Russian IPOs. URL: <http://www.preqveca.ru/placements/> (accessed: 15.12.2019).

eign investors”. According to the company, all buyers were not affiliated with the it or with the controlling shareholder [Dzyadko, 2016]. However, no details on buyers were disclosed for the market. Vedomosti, the leading Russian business daily, gave the following comment on this IPO: “It is unknown which buyers ensured the reported high demand and the over-subscription”. Representatives of large investment funds called by the daily denied they took part in the IPO. “We did not see benefits in this placements and our customers did not express interest in it”, said one of them. Prior to the IPO, a senior investment fund manager admitted that this IPO would be a “backstage” one and a part of securities offered would be bought by pension funds which make

part of Samafar financial group controlled by M. Gutseriev's family. Yet, Samafar denied it had taken part in IPO [Starinskaya, Mesroelyan, 2016]. Market analysts cast doubts on the announced placement price. A. Kalachev, analyst of Finam financial company, pointed out that Russneft market capitalization/*EBITDA* ratio after the IPO was as high as 6.5, while for other listed Russian oil companies, well-entrenched in the industry, which had proven their financial stability and ensured good dividend flow, it was between 4.5 and 5.5 at that time. The net debt/*EBITDA* ratio for these oil companies in 2015 was much lower (TATNEFT — 0.04; RossNeft — 1.36) than for Russneft (4.5). So, if buyers bought RussNeft stocks at the officially announced price at the IPO, they got no discount for the newcomer status of the company but paid a significant premium [Easy Money..., 2016]. It could have been that all buyers overpaid for RussNeft stocks due to miscalculations. But in our view, there is an explanation for this which looks more sound: high price was paid by buyers who were affiliated with RussNeft's controlling shareholder. This explanation makes the real ownership structure of RussNeft after the IPO look quite different from what was officially announced.

- In December 2015, Evroplan, financial leasing company, announced to have made a very successful IPO selling 25% of its stocks. According to the company, the demand exceeded the offer by 40% and the securities were sold at the top of the offering price level. The company announced that as the result of the IPO the share of the controlling shareholder, M. Shyshkhanov, dropped from 100 to 75%. However, this triumphant reporting was a sharp contrast with massive negative comments by business media and experts. *Vedomosti* described this IPO as “yet another deal when the owner of pension funds financed with their money his

other business. M. Shyshkhanov sold 25% of Evroplan, owned by him to the pension funds of Bin group controlled by him”. Analysts of Sberbank CIF investment bank were equally critical of the IPO: “The placement was made with a minimal public disclosure... The buyers have remained unknown... Such investment does not fit into customers' interests and is an example of a conflict of interest of customers and owners of pension funds”. They also pointed out that institutional investors did not include Evroplan stocks in their portfolios and did not show interest in them [Petrova, Biyanova, 2016]. In January 2016, Evroplan reported that the stake owned by M. Shyshkhanov dropped down to 51.1% as the result of the sale of 25% to the same buyers.

At large, the history of IPOs and SPOs by Russian companies shows that the overriding priority of their controlling shareholders has been to retain their full control over these companies. In our view, this is fundamental for understanding the Russian IPOs and SPOs in the foreseeable future.

Major Russian companies, which made voluntary delisting from both, Western and Russian stock exchanges, explain these moves by their plans to make successful comebacks in a near future which would ensure quick increase of their market capitalization. But stagnant Russian economy, sustained political tension between Russia and the West and controversial history of many Russian IPOs make these declarations very questionable, to put it mildly. Analysts do not take these declarations at face value but consider them as a veil for a new corporate strategy of these companies for the foreseeable future.

From our point of view, this is a strategy which does not provide for the reducing stakes of controlling shareholders, does not diminish their grip on these companies and does not include the prospect of a transit of these shareholders from their present status to the status of financial investors. Under this strategy, market capitalization

is not viewed as a key economic objective. At the core of this strategy is a close cooperation with the Russian state as its junior partner and obtaining advantages from it, such as large state contracts, loans from state banks at beyond-market rates, legal restrictions on activities of foreign competitors on Russian market, support by the state in export, etc. This strategy also includes utmost priority to close cooperation with large state-owned companies, state-owned banks, private companies with strong connections at the top political level and some Western companies which obtained a most favored status from the Russian political leadership<sup>3</sup>.

<sup>3</sup> There are some examples. In spring 2019, media reported that A. Mordashov, a major Russian tycoon owning the controlling stakes in two large listed companies, Severstal and Lenta, obtained a significant stake in Rostelecom, large state-owned listed company. He did that in alliance with VTB, one of the two largest state-owned banks, and Rossiya Bank, which is reputed to have very strong personal connections at the very top of the Russian state hierarchy. These three new shareholders paid their stakes in Rostelecom by shares of Tele 2, the fourth largest mobile telecom company, jointly owned by them [Korzhova, Kodachigov, 2019]. In February 2019, the CEO of Megafon (recently delisted from the LSE) said that the new strategy of the company, after delisting, provides for becoming the main partner of the state in transforming Russian cities into “smart ones” and in “digitalization” of Russian regions, including management of urban infrastructure (procurement and technical installation of “smart” equipment, urban lighting, road traffic regulation, communal services management, security, tele-health services, etc.). After the adoption of the Yarovaya law, in 2016, which mandated all Russian telecom companies to install audio surveillance equipment (the total costs are estimated at 100–120 bln rub.), by 2019, Tsytdel company, affiliated with A. Usmanov, the controlling shareholder of Megafon, took up to 80% of the surveillance equipment market [Kolomychenko, 2019]. Both Russian listed largest Internet companies, Mail.ru (LSE) and Yandex (NASDAQ), have signed strategic cooperation agreements with Sberbank, a top-2 largest bank, owned by the state. Cooperation provides for a gradual integration of many key assets owned by the bank and these com-

## CONDITIONAL OWNERSHIP

The important factor which determines business conduct of controlling shareholders of major Russian listed companies is restrictions imposed by the Russian state on their right to sell large stakes, let alone control stakes, to foreign investors. The Russian state considers these companies as national strategic assets over which it has ultimate control for national security reasons. To regulate sales of stakes in companies (both listed and non-listed) which are considered strategic entities the Government Commission on Foreign Investment was set up in 2008. Under the new regulation, all transactions by foreign investors who gain direct or indirect control over more than 25% of the total voting shares of any “business entities of strategic importance for national defense and state security” or acquire the right to directly or indirectly control more than 5% of the total voting shares of the “business entities of strategic importance for national defense and state security” involved in exploration and development and production of natural resources in the subsurface areas, must be preliminary approved by the government commission. Our analysis of the commission’s proceedings has revealed a very broad definition of a “strategic company” used by the Commission. It acted on applications by foreign investors to acquire stakes not only in strategic major companies but in companies of mass media, fishing, pharmaceuticals and with annual sales in the range from 200 mln rub. (about \$3.3 mln) to 4–5 bln rub. (about \$63–80 mln).

According to the Federal Antimonopoly Service (FAS), in 2008–2018, the Commission received 516 stock acquisition applications from foreign investors. It reviewed 229 applications and rejected 13 of them (less than 5% of applications considered).

Russian media regularly reports, that Sberbank is assigned by the state with gradually taking over control over both companies.

No explanation has ever been provided on why the other 287 applications have not been reviewed. In all likelihood, these applications have been tacitly withdrawn by applicants who saw very little chance to succeed. Reportedly, an unknown number of prospective applicants decided not to submit their applications at all for fear of being rejected. The example below clearly reveals problems faced by controlling shareholders of Russian companies seeking to sell controlling stakes to foreign investors.

In 2015, major shareholders of Eurasia Drilling Company (EDC)<sup>4</sup>, which then controlled 20–22% of the Russian oil drilling market, reached an agreement with Schlumberger on stage-by stage selling (within 3 years) to it of 100% of EDC stocks. Following the agreement, EDC got its shares delisted from the LSE. For this transaction the EDC major shareholders raised loans from banks. Yet, after the transaction entered into effect and the shares were bought out by major shareholders after delisting, the latter were unofficially informed about negative reaction of the Russian government to the transaction. The reason was that Schlumberger is “a US company” and will have to bind to economic sanctions which have been already taken or can be taken by US government against Russia. Years of negotiations between the EDC owners and the Russian government on the destiny of the deal have followed. Initially, the Russian government insisted on gaining for free the golden share in the company [Melnikov, Khvostik, 2015]. In further negotiations, the Russian government insisted that Schlumberger must take obligation that only a Russian citizen can be appointed the CEO of EDC and to sell all EDC shares to a Russian company designated by the Russian government in case new Western economic sanctions are taken against Russia. Later, this was added by the demand to split the controlling stake in EDC between Schlum-

berger and the consortium led by the state-owned Russian Fund for Direct Investment (RFDI) including state-owned investment funds from China and the UAE. Subsequently RFDI changed its stand several times and in June 2019 it asked the FAS to cancel its application for a permit to acquire 30% of EDC by the consortium led by it. This has made the fate of the transaction completely uncertain.

The fundamental fact to take into account is that after 1917 Russia has lost tradition to bequeath large industrial assets through inheritance and there are no signs of preparation for such handover as a massive business phenomenon in modern Russia.

S. Sviridov, head of analytical department of A1 investment company<sup>5</sup>, predicts a sharp escalation of conflicts over corporate assets control in Russia. In his view, among the drivers of this escalation will be the forthcoming withdrawal of founders of companies due to their advanced age. Many heirs, in his view, will not be as tough as their fathers who founded the corporations and this will provoke raiders’ attacks on them to wrest corporate control out of their hands [Sviridov, 2018]. Experts point out that almost all founders of major Russian companies view their companies’ sales as the best strategy [Succession in Russian Business..., 2014].

It is very likely that the Russian state will not allow the controlling shareholders of major Russian companies to sell control to foreign investors. It is good reason to expect that it will impose conditions of such transactions which most foreign investors will find unacceptable.

Then, what are prospects for controlling stakes of major Russian companies to be sold at a fair market price at the domestic market and who would be able to buy them?

According to the assessment made by Moody’s Investors Service in October 2018,

<sup>5</sup> A1 is a Russian company known for its very tough treatment of business partners. Its services have been often used as an “ultima ratio” by parties involved in corporate conflicts.

<sup>4</sup> The company was registered at BVI but had all its assets in Russia.

the Russian banking system is the weakest in the BRICS group of countries in terms of asset quality, liquidity and profitability [Among BRICS nations..., 2018]. So, it is very unlikely that Russian banks will be able to finance buyouts of controlling stakes of major Russian companies at more or less fair market prices. Even largest Russian state-owned banks, VTB and Sberbank, are very unlikely to finance buyouts of controlling stakes of 15–25 major Russian companies at a fair market price within 3–4 year period by buyers who will obtain political blessing from the Kremlin. With the share of the state in the Russian banking system reached 70% in 2018 and the forecast to reach 85% in the next 3–5 years [Falyakhov, 2018], non-state Russian banks are very unlikely to play any significant role in this process<sup>6</sup>. So, it is more likely that the controlling stakes of these companies will be sold at very large discounts to designated buyers, similarly to the privatization of the 1990s.

Lasting political tension between Russia and the West undercuts prospects for Russian banks to borrow much funding from the West and makes unacceptable for Russian political leadership the schemes in which major stakes of leading Russian companies are used as collateral to Western banks.

Despite high-pitched political rhetoric of Russo-Chinese friendship, Chinese banks have been very cautious in their activities in Russia. Providing large-scale financing by them will raise similar national security concerns in the Russian political establishment as in the case of Western banks<sup>7</sup>. Therefore, the controlling shareholders of

major Russian companies face the prospect of having no choice but to sell their control stakes at a very discounted price to new owners designated by the Kremlin, or to state-owned banks or companies. Domestic political and economic situation in Russia, the steady expansion of the state's control over all areas, coupled with a sustained political tension in relations between Russia and the West, make the future of major Russian non-state companies very uncertain. In our view, this is the key to understand the conduct of controlling shareholders of these companies.

## THE ROADS THEY TAKE

In terms of their conduct, Russian owners of large industrial and financial assets (including controlling shareholders of major listed companies) can be divided in two groups.

The first group has opted for emigration from Russia. According to Knight Frank, in 2000–2013, 14 000 of individuals with personal fortunes counted in millions and billions of dollars (high net wealth individuals and ultra-high net wealth individuals — HNWI and UHNWI) left Russia [Second Citizenship..., 2015]. A part of them has stopped doing business in Russia. But another, more significant part, by estimates, has continued doing business in Russia, despite no longer being Russian tax residents. In 2014–2016, according to Knight Frank, more than 6000 of Russian HNWI and UHNWI left the country. It is not clear how many among them are controlling shareholders of Russian listed companies. Mass media has referred to 10–15 names with periodical confirmations and denials.

The second group is the overwhelming majority of public companies' controlling shareholders who have stayed in Russia and do their business in accordance with rules

<sup>6</sup> In our view, it is very revealing that the acquisition of the relatively limited stake (11.8%) of Magnit, a major Russian retailer, by Marathon Group, investment company with reportedly very strong political connections, was funded by VTB and structured as a repo transaction [Demidova, Parfentjeva, 2018].

<sup>7</sup> It is remarkable that a failed attempt to sell a large stake (about 15%) of RossNeft, in 2017–

2018, to CEFC, a large Chinese energy trader, was financed by VTB and not by Chinese banks.

set by the Kremlin. For many of them the period of 2016–2018 was extremely successful.

The number of Russian billionaires grew by 29 in 2016–2018, as Russian Forbes reported in its list of richest Russians in 2018 [200 richest businessmen, 2018]. According to The Knight Frank Wealth Report, in 2017 the number of owners of \$500 mln fortunes grew in Russia by 22% [The Wealth Report..., 2017]. According to Credit Suisse, the number of Russians with \$50 mln-plus fortunes in 2017 grew up by 26% to have reached 2620. This trend continued in 2018 [Global Wealth Report, 2018]. In 2018, the total number of Russian billionaires reached 106 and this put Russia third in the global rating of billionaires, after US and China.

According to the BCG findings [BCG, 2019], in 2010s, Russia enjoyed very high level of the personal financial wealth growth pace and its total amount reached \$1.3 trl 46% of the Russian private capital is owned by ultra-high net wealth individuals (with assets of more than \$100 mln), while for Eastern Europe this indicator is 28% and the global average is 12%.

The period of 2016–2018 was the one of a very lackluster performance of the Russian economy<sup>8</sup>, with very few IPOs and SPOs, many of which were “technical” exercises. So, it is a good reason to believe that the above success stories were based on close cooperation of big Russian business with the state on selective favorable terms. The success in this cooperation requires from the Russian businessmen a strategy which is quite different from a “classic” market one.

The other side of the coin is that the Russian state has cemented its belief that it can order, at its full discretion, big Rus-

sian business to make additional financial contributions, besides taxes already paid, to projects which the state considers as having strategic importance.

For instance, in August 2018, A. Belousov, assistant for economy to President Putin, publicly voiced the idea to make 14 largest Russian companies, mostly listed ones (Acron, ALROSA, Evraz, NLMK, Norilsk Nickel, Mechel, Magnitogorsk metallurgy plant, Polyus Gold, Severstal, Sibur, SUEK, Phosagro, Uralkali, Uralchim) pay 500 bln rub. of “excessive profits” — either as an ad hoc quasi-tax, or as their “voluntary investment” — into projects selected by the state<sup>9</sup>.

Speaking to the Eastern economic forum, in September 2018, President Putin designated infrastructure of the Russian Far East as the objects the Russian companies, which use it, to invest in.

Experts, close to the Kremlin, periodically assert that expropriation of “super-profits” of large non-state companies is a “tax on privatization” to legitimize the right of their controlling shareholders to keep on their assets, obtained in the dubious privatization of the 1990s. Yet, some experts admit: “It is not possible to put the end to debates on legitimacy of ownership (large private companies. — *I. B., A. D.*) once and for ever, especially due uncertainty related to the post-Putin transit of power” [Simonov, 2018].

## THE IMPLICATIONS

The decreasing attractiveness of Russian listed companies for major Western institutional investors and a lasting effect of factors behind this trend, the tightening grip of the state over these companies and uncertainty of the fate of these companies,

<sup>8</sup> The GDP growth rate, as calculated by The Russian Government Analytical Center, based on the Russian State Statistics Agency (Rosstat), famous for providing too optimistic data: 2016 — 0.6%, 2017 — 1.6%, 2018 — 2.3%.

<sup>9</sup> This news has resulted in the downfall of market capitalization of 9 listed companies from the above list by 392 bln rub. at LSE, NYSE and MOEX.

lead the majority of Russian controlling shareholders to no longer consider market capitalization of their companies as the primary strategic goal. Our analysis has driven us to the conclusion that since 2013 the controlling shareholders of major Russian listed companies have refocused their interest on dividend payments at the most appropriate way to monetize their property rights and have embarked on the policy of maximizing dividend payments.

Since 2013, the Russian listed companies have been increasing a share of their net profits paid out as dividends. They have been changing the rules of dividend payment calculations so as to make the performance indicators with higher values the calculation basis. The frequency of dividend payments has been growing: more companies have started to pay not only annual dividends but interim dividends, as well as special dividends. This trend has expanded to all industries of Russian economy. There are large listed companies which have fixed the minimal levels for their dividend payments at 50 or 75% of their net cash flow and some — at 100% of net profits or net cash flow.

Analyzing the dividend payments for 2013, Expert weekly reported: “There is a growing number of equities on the Russian market with dividend yields exceeding 7–8% and even 15%... According to calculations by GHP Group, the average dividend yield on the Russian market... reached 4.41% which is among the highest ones in the world” [Kontsevich, Obukhova, 2014].

As Vedomosti reported, “despite the economic recession, which started last year (2013. — *I. B., A. D.*) and the decrease in the total profits of Russian companies in 2014 (by 9.8%, according to Rosstat as compared with 2013), many Russian listed companies have preserved and even increased their dividend payments for the year 2014” [Koval, 2015]. Among the leaders in the amounts of dividend payments were such listed companies as ALROSA, M-Video, Magnit, NorNickel, Severstal, FGC UES, Phos-Agro and some others.

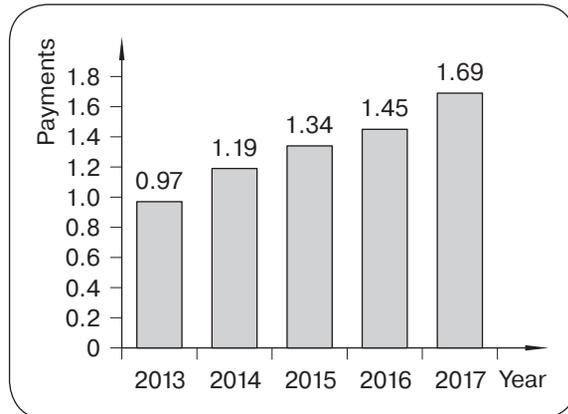


Fig. 1. Dividend payments by Russian non-financial companies (in trl rub.)

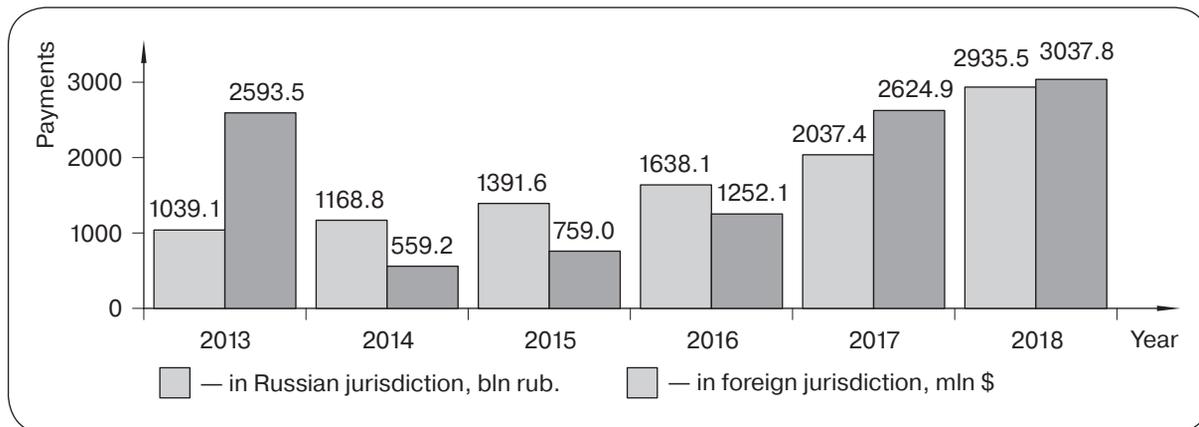
Source: ACRA rating agency [Burmistrova, 2018].

According to ACRA<sup>10</sup>, dividend payments by Russian non-financial companies for 2016, grew up by 9% as compared with 2015 and reached 1.5 trl rub (Fig. 1). The dividend payments by large Russian companies for 2017 grew up by 16% as compared with 2016<sup>11</sup>. According to Bloomberg, the dividend yield for 2017 of Russian companies in RTS index was 6.3%, while for Turkish companies this indicator was 4.8% and for Brazilian companies — 4.2%. The average dividend yield for MSCI Emerging Markets was 2.8%. ACRA experts pointed out that as the result of high dividends for 2017, the aggregate free cash flow of large Russian companies became negative with less funds used for investment [Burmistrova, 2018].

There was a dramatic increase in dividend payments by Russian companies for 2018 — up by 50%: for the first time in Russian corporate history their total amount reached 3 trl rub (Fig. 2). According to calculations by National Rating Agency (NRA) expert K. Koukoushkin, the average dividend payments growth pace in 2013–2018 was 23%. According to Bloomberg, in March 2019,

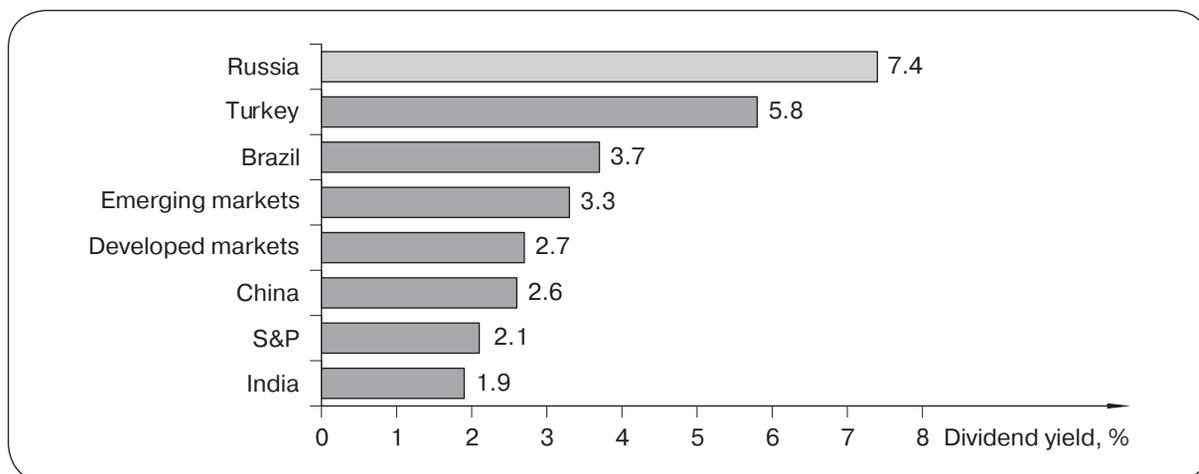
<sup>10</sup> ACRA (Analytical Credit Rating Agency) is the leading Russian rating agency, accredited by the Bank of Russia.

<sup>11</sup> This calculation by ACRA was based on the analysis of dividend payments by 227 largest non-financial Russian companies.



*Fig. 2.* Dividend payments by Russian companies

Source: National Rating Agency (NRA) [Burmistrova, 2018].



*Fig. 3.* Dividend yield of Russian companies as compared with other markets, 2019

Source: Bloomberg, Aton investment company [Burmistrova, 2018].

the dividend yield of Russian equities reached 5.7%, while for MSCI Emerging markets this indicator was 3%, for the leading European indices — 2.5–4%, for US indices — 1–2.2% and for Asian indices — 2–3.5% (Fig. 3). Experts specially noted “an extremely high” growth of dividend payments by state-owned Russian companies.

Despite some differences in amounts of dividend payments, all the above data clearly display that after 2013, dividend payments have been growing steadily and they have become the main means of monetization for the controlling shareholders of Russian listed companies.

In 2012, the OECD experts assessed the impact of high ownership concentration of Russian listed companies on their corporate governance practices in the following way: “This high concentration of ownership in the hands of a few powerful shareholders presents challenges similar to those described from Indonesia and Korea in the OECD peer review, rather than those faced by countries like the U.S. or the Netherlands. This is somehow reflected in strong de jure duties assigned to the board combined with a de facto situation in which they often do not play a decisive role in the governance of the company” [Kostyleva, Lehuede, 2012, p. 20].

Since that time the problem has become more acute.

Deeply entrenched ownership concentration of Russian listed companies with strong stimuli to keep this level and diminishing stimuli to decrease it strengthen the belief of Russian controlling shareholders that from the point of beneficial ownership structure the right of the real governance power fully belongs to them and not to boards of directors. In face of persistent and even growing non-economic risks, the controlling shareholders of Russian listed companies consider endowing the boards with real powers, even to a limited extent, as an unacceptable move.

In late 1990s — late 2000s, a growing number of listed Russian companies espoused some elements of the Western best corporate governance practices, primarily those related to composition of boards (election of a limited number of formally independent members) and their work procedures (board committees, regular meetings, setting up of internal audit functions, etc.). This process was driven by the then high attractiveness of emerging markets for Western investors at large and of the Russian market in particular, due to high pace of economic growth and high level of oil prices (Russia's main export commodity). At that time, the controlling shareholders of the growing number of Russian companies seemed to believe that such steps really helped to attract major Western portfolio investors and to drive up market capitalization of their companies.

Yet, by the end of 2010s, big Russian business, including most of controlling shareholders of Russian listed companies, apparently lost the above belief because of mounting political tension between Russia and the West and tightening restrictions by the state upon sale of large stakes, let alone controlling ones, to Western investors. As the result, since 2015, corporate governance practices of many Russian listed companies in their important components (number of independent directors, board procedures, transparency and disclosure, etc.) have stagnated or have

turned into box ticking exercises. For the controlling shareholders, dividend maximization has replaced market capitalization as the main way of property right monetization.

The focus on close partnership with the state as the core of the new strategies of many Russian listed companies and the mounting restrictions by the state on Western investment in the Russian economy have dramatically reduced a market demand for Western best corporate governance practices on the part of Russian controlling shareholders.

The “turn to the East”, declared by the Russian political leadership after 2014, includes the substitution of Western investors with the state and state-affiliated large investors from China and Arab countries (Saudi Arabia, Qatar, UAE). Some of these new investors acquired significant stakes (10–15%) in some Russian listed companies. Yet, our analysis shows that in taking decisions on such acquisitions these investors are much more motivated by political relations of these countries with Russia than by purely economic interests. As shareholders of Russian companies, these investors rely primarily on interaction of their governments with the Russian government and political guarantees from the latter as the way to protect their interests, rather than on corporate governance practices of the target Russian companies. As the result, these investors usually make very little, if any, contribution to improvement of corporate governance practices in Russian companies.

## CONCLUSION

High concentration of ownership has become the DNA of Russian companies, both listed and private. This situation is very unlikely to change in the foreseeable future. The major risk which cements this stand of controlling shareholders of these companies is expropriation by groups with strong connections in the law enforcement bodies and at the top levels of the political hierarchy

or by the state. The controlling stake does not provide full guarantee against this risk but the stake below it makes this risk too high. Authoritarian social and business culture and a low level of trust in relations among business partners have contributed to high ownership concentration of Russian companies. There has been no indication of improvement on this front.

The Russian state considers big private business as its order-taking partner and this makes the state very much interested in preserving high concentration of ownership of major Russian companies. It is much easier for the state to deal with a limited number of controlling shareholders rather than with large number of portfolio investors, especially with politically influential Western institutional investors. This is the key to the real practices of the government regulation and especially enforcement of relationship between majority and minority shareholders in major Russian companies.

Till the late 2000s, most controlling shareholders of Russian listed companies sought

to combine high ownership control with gradual accommodation with minority shareholders and acceptance of some Western corporate governance practices. Increasing market capitalization of these companies at that period due to their growing attractiveness for Western portfolio investors was a very important driver in this policy.

After 2014, in face of the policy of mounting restrictions on Western investment in the Russian economy pursued by the government, most controlling shareholders of Russian listed companies have switched to the strategy of acting as junior partners of the state. This switch has largely diminished their market orientation and the demand for Western-style corporate governance.

It is quite likely that in the first half of the 2020s many of the existing large non-state Russian listed companies will come under direct control of the state or will be taken over by new controlling shareholders who are closely affiliated with the top echelon of ruling political establishment.

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## **Российские публичные компании: контролирующие акционеры и их стратегия**

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Высокая концентрация акционерной собственности выступает основной характеристикой российских компаний, включая публичные. Сохранение контроля — приоритетная цель контролирующих акционеров этих компаний. В 2000-е гг. они стремились к привлечению западных портфельных инвесторов, внедряли элементы западной практики корпоративного управления и рассматривали рост капитализации как важную часть своей стратегии. В 2010-е гг. этот процесс остановился в связи с резким ростом контроля государства над экономикой и

ограничений с его стороны на западные инвестиции. После 2014 г. большинство контролирующих акционеров этих компаний сделали выбор в пользу стратегии превращения в младшего партнера государства, что резко сократило их рыночную ориентацию и спрос на западную практику корпоративного управления. Будущее крупных публичных компаний в России полностью зависит от отношений их контролирующих акционеров с государством, в связи с чем является весьма неопределенным.

*Ключевые слова:* публичные компании, структура собственности, государство, контролирующие акционеры, IPO, монетизация прав собственности, корпоративное управление.

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