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The review provides a detailed analysis of main trends in Russia's economy in 2008. The paper contains five big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and credit and financial spheres; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts.

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Property Policy in Russia during the Financial Crisis

5.1.1. The overall process of property redistribution

Even the roughest assessments make it evident, that the financial crisis, started in 2008, leads to a noticeable intensification of several inter-related property processes. First of all, the general property redistribution process in the scope of the Russian economy gets new incentives, just like after the crisis of 1997-1998.

General assessments of the market of mergers and acquisitions in 2008 are very similar with a noted downgrading as compared with 2007, whereas the first ones took place after a long period of steady growth within 2002-2007. Absolute assessments of the reducing market capacity are differed, depending on the methods used: by 36 per cent, from USD 120-122 bln to USD 77.5 bln (with regard to transactions from USD 5 mln, as per M & A Intelligence), or by 9 per cent to USD 120 bln, nearly USD 100 bln of which were addressed to the Russian assets purchase (with regard to all transactions, as per Ernst & Young estimates)¹.

The assessments of the prospects for this market in 2009 are much more controversial. In general, it is expected a further reduction in the market capacity (up to 60 per cent as compared with the level of 2008), but the forecasts on the qualitative trends are rather different (depending on the further market restraints due to the problems with working capital and external funding access, up to the market reviving from mid-2009 at the expense of the purchase of problem assets and companies). In fact, it is clear that, with an overall downgrading in the market of mergers and acquisitions in the situation of the financial crisis, this channel remains «working» particularly for those businesses, which have kept liquidity and were able to take this advantage to purchase the depreciating assets (from May 2008 to February 2009 the capitalization of the Russian stock market has fallen down 4-fold, from USD 1.5 trillion to USD 370 bln).

At the same time, the activity of the insiders is growing (primarily major shareholders and Managers, which is often identical in the Russian model). According to the available information on the dynamics in the 500 largest public companies transactions, in the second half of 2008 the number of transactions on the sale of the shares by the management of the companies has significantly reduced. On the contrary, there is noted an increase in the number of transactions, in which the insiders were acting as the buyers of shares of their company,

¹ Hereinafter the in the analysis of various processes in the corporate sector and measures of public anti-crisis support ther used the information and materials, allocated on the official websites of the leading news agencies and periodicals (of publishing houses) for 2008-2009. (in particular, www.vedomosti.ru, www.kommersant.ru, www.ma-journal.ru etc.).

even in cases, when in earlier periods they had acted as sellers². With some reservations, the same policy, as demonstrated below, was typical in crisis situation and for the state as well.

Although the statistics is not available (primarily due to the restricted access to such information), a significant channel for the assets redistribution (including foreign assets) in 2008 could become the forced sales of bank margin securities (margin calls) of the Russian companies. The problem assets in autumn 2008 there were found shares of Magna (Canada) and Hochtief (Germany), pledged on «Bazela» loan (disposed by creditors), as well as the share of Oleg Deripaska in Strabag, the company of X5 Retail Group, VimpelCom (Depository Receipts have been pledged under the Alfa-Bank loans), Rosneft, Norilsk Nickel (25 per cent pledged under «Rusal» loans), «LUKOIL», Sviazinvest, STS Media (shares were pledged under Alfa Bank loans), AFK «System» (in the mortgage securities of «Sistema-Hals» Company and Bashkiria oil assets were pledged), Wimm-Bill-Dann, Seventh Continent, Novatek and others³. There are also many credit agreements, secured by the minority packages of the largest Russian companies with the state participation, but (due to the state-owned control stake), the transfer of ownership is quite possible (for example, the transfer of ADR and «Gasprom» shares in the amount of 0.77 per cent of Vostok Gas share to Deutsche Bank).

The majority of companies managed, however, to retain their assets. One of the peculiarities of the Russian credit market is the predominance of the Russian banks in the corporate credit portfolio (92.7 per cent in September 2008, while the total credit portfolio of the Russian banks in the non-financial sector was RUR 11.8 trillion), but the practice of margin calls is not typical to them. Sberbank of Russia, being the largest creditor of the non-financial sector (over 1/3 of the total loan portfolio), according to the available data, is not utilizing this opportunity yet. VTB has become one of the few major Russian creditors (about 10 per cent of credit portfolio), which has used this mechanism in practice⁴. Some companies purchased their shares at the open market as early as in summer (for instance, «Norilsk Nickel», MTS), although with the continued decline in the market, this measure could not work to full extent⁵.

According to estimates of Fitch Ratings agency, in the 4-th quarter of 2008 the corporate sector has repaid of USD 36 bln, under external debt, while 55 per cent of external credits has been carried over, including margin calls, burdened with debts. In 2009, about USD 140 bln need to be accumulated for the corporate debts payment.

The transition of assets can be also caused by the started in 2008 defaults in corporate debt obligations. By early November 2008, the aggregate amount of emissions under default has amounted to about RUR 30 bln.

By early 2009, there emerged a practice of debt liabilities settlement through the transfer of assets to the creditor banks (primarily in construction, retail trade, retail mobile communication services, foodstuffs production, etc.). In January 2009, there was also the case of transfer of oil and gas fields as for the debt settlement (Urals Energy to cover the to Sber-

² However, it is not surprising in the face of crisis, especially for problem companies, when capitalization, for example, of «RBC Information Systems» for the year has fallen down 21 times in the RTS. Ref: Forced Acquisitions. - Dengy, № 3, 26 Jan, 2009.

³ Ref.: Corporate secret, № 46, November 24, 2008.

⁴ Ref: Merges and acquisitions, 2008, № 12, pp.10–16.

⁵ Undoubted interest was attracted autumn of 2008 by the receipt by «Don-construction», specializing in «elite real estate», credit lines in VTB in the amount of USD 0.5 billion. Herewith, the government support (at the federal and Moscow levels) was expressly promised only to the economy class developers.

bank). Among the recipients of assets we can also mention the VTB, Alfa-Bank, Yunikredit-bank, Trust Bank and others. A subsequent exposure of the assets on sale is most likely (due to the inconsistency of the acquisitions to the basic banking activities, the lack of relevant experts, etc.), what urges intensification of the corporate control in the market.

5.1.2. External corporate debt and a new phase of state expansion

A specific feature of the present crisis (as opposed to the crisis of 1997-1998) is the *active participation of public* and state-controlled businesses in the process of property redistribution. Moreover, the current situation becomes in fact a mirror reflection of the well-remembered shares-for-loans auctions (arranged in November-December 1995), when the government, receiving the funds from private companies to supplement the budget, has placed in pledge shares of 12 major (strategic) Russian enterprises to fulfill public liabilities. Among them, in particular, there were packages of shares of «YUKOS», «LUKOIL», «Surgutneftegas», «Sibneft», «Norilsk Nickel», «Novolipetsk Metallurgical Works» and others, but there were no cases, when such quasi-credit was repaid, which according to the vast majority of evaluations, actually meant privatization of those blocks of shares by manifold reduced prices.

In autumn 2008, the roles have been drastically changed: on the publicly declared announced grounds of «economic security», the Government expressed willingness to refinance those external credits of public and private companies, incompliance of which could result in the loss of national control over the Strategic Asset (by the state or by national capital). This means, in particular, that the objects of *actual nationalization* can be not only the shares of the public sector in the direct meaning of the word (those, where participation of the state capital exceeds 50 per cent), but also strategic businesses (though the definition of that term in the Russian legal framework is rather vague) of the private sector.

Back in 2006, it was noted in the IET works⁶, that further development of the companies with the state participation, which have become the «core targets» of the state expansion, will be defined, among other things, *by their ability to redeem credits* in view of global prices for energy sources. The most pessimistic estimates were based on the expressed downfall in prices for energy sources, greatly affecting the largest state-owned companies-borrowers business. It was noted that along with the downfall in oil prices, an access to financial resources in the external markets for the debts refinancing will be decreased, whereas the price for credit services will be increased. In this situation, short-term outflow of foreign capital, downfall of the stock market and severe problems in the banking system, based on reduced liquidity were expected.

In 2000-2005 external debt of the Russian state-owned companies has increased many times: USD 570 mln in 2000, USD 12 bln in 2002, USD 28 bln in 2005, that is, according to the estimates, it amounts from 30 to 40 per cent of the total external corporate debt of Russia. Thus, in 2005, the external loans of Sberbank, Vneshtorgbank, Vnesheconombank and Rosselkhozbank amounted to nearly USD 6.45 bln (about 36 per cent of the funds raised by Russian banking sector). «Gazprom», «Rosneft», «Sovkomflot», OJSC «Russian Railways», «Transneft» and «Alrosa» total external debt reached USD 28.2 bln. The tear of 2006 has

⁶ Ref.: Russian economy in 2005 . Trends and prospects. Moscow, IET, 2006 and: Interview with Ye. Gaydar // Expert. 2006. N3. P. 6.

been characterized by a new wave of the debt growth: the external debt of non-financial companies and commercial banks amounted to USD 135.4 bln and USD 78.5 bln accordingly (whereas the share of public companies is estimated at over 50 per cent of the total external corporate debt of Russia).

By July 1, 2008, according to the Bank of Russia, the total external debt of Russian companies, banks and government administration authorities reached USD 527.1 bln (an increase only within the second quarter of 2008 totaled nearly to USD 50 bln). Herewith, the share of external debt of financial institutions amounted to USD 191.3 bln (the debt growth has exceeded USD 21 bln per quarter). The debt of non-financial companies, regardless debt liabilities to the direct investors, amounted to USD 263 bln (nearly USD 25 bln growth per quarter).

As of July 1, 2008, external public debt of Russia amounted to approximately USD 41 bln. It is estimated, that the debts of state-owned companies and banks currently make around 50-60 per cent of external corporate debt of Russia (for example, «Gazprom» - around USD 60 bln, «Rosneft» - about USD 26 bln, VTB – USD 11.4 bln, subject to redemption before the end of 2009)⁷.

According to common formal indicators (the ratio of the company debt against operating income), the largest Russian borrowers have not reached the critical «threshold». Nevertheless, various control measures (restrictions) of public companies external debt have been extensively discussed since 2005. From the standpoint of the Ministry of Finance, the State should take some responsibility for the activities of such companies through the development of common approaches to external and domestic debts of the state-owned companies. External debts should not be banned, but they should be limited in scope and, where possible, be replaced by credits in the domestic financial market⁸. There were some expectations from the state representatives in the Boards of Directors. Since the borrowing issue is closely related to the companies' net profit allocation (dividends to shareholders, including the State), documents were being developed for establishment of a unified system of borrowing and dividend policy. *Overall, by mid-2008, no regulations or standards of these processes have been implemented.* Moreover, the administrative restriction of state companies' access to external fi-

⁷ Investment company ATON estimates: as of Oct. 5, 2007, Russian external debt grows due to state-owned companies www.svobodanews.ru. Nevertheless, it should be noted, there are difficulties in assessing the debt of the state-owned companies: first, because of the lack of consolidated corporate registers (at least disclosed ones). Secondly, there are methodological inconsistencies. Relevant statistics of the Central Bank on external debt (detailed analytical report for 2008, ref.: www.cbr.ru/statistics) takes account of external debt for public and private sectors separately, and in the public sector includes only those banks and non-financial companies «in which the government or monetary and credit authorities direct or indirect participation makes 50 or more percent in the form of shares ownership or in any other way of control over the capital». All other public companies (combined patterns of ownership), apparently, belong to the private sector. Assuming that all the major «debtors» with the state participation over 50 % are related in the Central Bank records to the public sector, the total amount of the external corporate and bank debt is notably less than the general expert estimates (USD 141.9 billion, or 34, 7 % of the total external debt of banks and public and private companies as of April 1, 2008). It should be noted, that even the debts of «Gazprom» and «Rosneft», the companies, that can be undoubtedly related to «non-financial companies» as per the definition of the Central Bank (whose debt amounts to about USD 86 billion) has already exceeded the total amount of debt of non-financial companies of «public sector» (USD 74.5 billion). And thirdly, there is in fact «double counting», because according to the estimates, some assets, recorded by the Central Bank as external debt, are in fact, the domestic credits, provided within the groups of companies (holdings), which have no relation to external debt in economic terms.

⁸ RIA «Novosty». December 8.

nancing sources can be hardly regarded as an effective inflation curbing mechanism. The issue of external borrowing for the state holdings should be resolved from a different point, namely by definition of their priority in government issues, ensuring the transparency of financial flows and effective management of targeted assets.

It is known, that a substantial share of the leading state companies' debt has been associated with operations in the market of corporate control in 2005-2007. In other words, a large share of borrowed funds was addressed not to the existing business development, but to the process of the new property redistribution, i.e., the purchase of assets, changes in the equity capital, etc. Unlike the forceful redistribution of preceding years (for example, «YUKOS case»), the new phase, when the leaders are the state companies and number of companies, enjoying political support from the government, is the market-power by nature. Assets are sold not entirely voluntarily, but at a close to the market price (it is enough to mention the history of 50 per cent share acquisition in the project «Sakhalin-2»). As a result, the transition to the state-capitalist economic model contributes to the market growth and investments attraction. In conditions of high liquidity and favorable macroeconomic situation the state companies actively attract credit resources for the purchase of new assets, which leads to their market capitalization growth⁹.

Although the State is not responsible for the debts of the mixed-type companies, in fact, their debts are estimated as sovereign ones. Moreover, for investors, investing in such businesses becomes a source of virtually guaranteed profit, as the government demonstrates willingness to support those companies in both, political and state regulation terms (the program for gas prices upgrading for domestic consumers). This predetermines the extreme popularity of Russian shares in the offshore hedge funds, for which the *deterioration of the institutional environment (especially «double standard» policy) in Russia is favorable in terms of profits*. At the same time, foreign banks are willingly provide credits under low interest for the purchase of new assets by the state companies (note the expressed marked increase in the debt of non-state borrowers in the second quarter of 2008, i.e., during the global financial crisis).

It is obvious, *that this model of market growth is largely speculative one, as there is no significant capital investment in production¹⁰ and the model is applicable only in the background capital inflow to emerging markets, as well as companies' revenues growth due to increasing prices for their products and the redistribution of assets in their favor*. Furthermore, such a speculative market growth conceals the real economic problems and distortions, provoked by deterioration of the institutional environment (while the state participation in the economic sphere is being expanded). It should be reminded, that in mid-2008, ten most capitalized companies provided 66 per cent of the total market capitalization, while 50 per cent of capitalization was derived from oil and gas extraction and refining¹¹. The huge inflow of funds is ensured by the small number of the leading companies, that are getting political sup-

⁹ Ref: A. Abramov, Radygin, Rogov Model Development: The Trap of the State Capitalism // Vedomosty. 2007. April 9, p. A 4.

¹⁰ According to A.E. Abramov estimates (based on stock exchanges and Russian Statistical Service), only within the period from 2005 to the first half of 2008, the share of investment from the corporate bonds issues, invested in the fixed assets, ranged from 0.4 to 2,2 %. Only slightly better was the use of funds by companies and banks involved in the IPO. In 2007, the most successful year in terms of IPO only 3.6 billion dollars, or 10.9 per cent, were implemented for the growth of real capital, out of 33 billion dollars, derived from primary and secondary placements of shares.

¹¹ The Russian stock market. The first half of 2008. NAUFOR, SKOLKOVO Moscow Management School, 2008.

port, while in general, the allocation of investments in the economy is restrained by institutional environment failures.

This model is clearly projected on the situation and the *financial crisis of 2008-2009*, when emergency measures of the Russian companies and banks support are being discussed.

5.1.3. Anti-Crisis measures in the context of increasing public sector

There are several trends, that should be highlighted in the package of anti-crisis measures, taken by the Russian government authorities in September-October 2008, in respect to the problems of expanding of the public sector.

1. *Public credits for foreign loans service* of the Russian companies and banks (initially – USD 50 bln in 2008).

According to available data¹², in the IV quarter of 2008, the amount of payments of Russian companies on external debts was estimated at USD 47.5 bln, and at USD 115.7 bln in 2009 with regard to extensions of redemption share USD 115.7 bln. Deposits (in the amount of USD 50 bln), allocated by Central Bank in «Vnesheconombank Bank Development», were enough finance companies for payments in 2008.

Herewith, it is justified, that credit terms are estimated as extremely tough (including such terms as «temporary nationalization»): securities pledge, a pledge of export earnings, undisputable and acceptance-free write-off of funds from any account of the borrower to recover credit, the inclusion the representatives of the Bank in the administration of the borrowing company, agreement with the bank to attract other loans and transactions on sale of more than 10 per cent of the company value, credit securities similar to foreign credits, etc. However, the VTB retains an unprecedented right for decision-making with regard to any increase in the pledge, as well as the opportunity to choose between debt redemption or the «set off» by the pledge.

By mid-October, 2008, applications were submitted for refinancing of «Rosneft», VTB, «Gaspromneft», TNK-BP, «Lukoil», UC Rusal, the AFC «System», Severstal, Michel and other companies. The minimum standard amount of the refinancing at the level of USD 100 mln (according to the Memorandum of the Bank financial policy), relates only to the largest companies and banks. OAO «Gazprom», having initially declared that there was no problem with payments, apparently can turn into an applicant for public funds, though, due to the exclusive status in view the Russian authorities, the refinancing terms and schedule can be different from common ones.

2. *Direct («anti-crisis») public intervention* in the stock market (RUR 175 bln in 2008 and 2009.)

In mid-October 2008, it was also decided to allocate assets from the National Welfare Fund for the purchase of the Russian companies shares (for RUR 350 bln in 2008-2009). Currently there is no official information on the interventions, the exact amount of investments and purchased shares, as well as the beneficiaries thereof. It would be at least reasonable to ask a question about the *expediency of the monopolization of virtually all transactions* in «Vnesheconombank-Bank of Development», on the procedures for the selection of Control-

¹² For more information, including detailed diagrams and charts of government anti-crisis «injections», it is enough to refer to the official web sites of the major news agencies and periodicals for October 2008 (in particular, www.vedomosti.ru, www.kommersant.ru, www.expert.ru, etc.).

lers (professional agents) for the transactions, which have been executed or will be executed in future, including the commission terms.

One of the very reasonable questions, that arise in relation to this kind of VEB activity, is on the source of the funds, allocated for the intervention. As you know, one of the key optimal objectives of the National Welfare Fund establishment was pension reform financing. It would be quite reasonable in the crisis situation to place the blocks of shares, acquired by the Fund in the open market, namely in the Pension Fund (or its equivalent) to ensure pension payments in future (at the stage of market capitalization growth). It is still unknown, where and to whom, in the existing nontransparent situation, the blocks of shares, purchased by VEB in 2008 and possibly in 2009-2010 will be transferred.

The issue of *transparency criteria for the expediency of these transactions and their public control* is no less important. According to the Decree of the RF Government dated of October 15, 2008, the Ministry of Finance has the right to invest in stocks and bonds up to 80 per cent of the National Welfare Fund assets, including up to 50 per cent¹³ in the securities, listed in MICEX and RTS, or included in the MSCI World Index and FTSE All-World Index, and in the funds, that carry out relevant investments.

Judging only by indirect information, such injections began only from Oct.17, 2008 in the shares of «Gazprom», «Rosneft» and Sberbank, and, according to the available data, in the shares of «Lukoil». Leaving aside general theoretical considerations of the near-to-zero efficiency of budgetary funds investments in stabilization of the stock market during the crisis¹⁴, according to the available expert estimates, no overall strategy of intervention, no proved anti-crisis measures with regard to divergent market trends are implemented even in relation to the narrow range of the leading companies-emitters.

Apparently, there were three possible trends: random counteraction against *margin calls*, acquisition of certain problematic assets and the attempts to market adjustments in favor of individual emitters, selected by the government. The problem of insider trading and, in the broad sense, a general policy against any kind of financial abuses (theft of funds) becomes particularly acute in this context.

According to the VEB, by the end of November, 2008 the Treasury of the Bank has received RUR 115 bln (from the National Welfare Fund). RUR 85 bln was spent to the «support the financial market». The funds were addressed to «the acquisition of shares and corporate bonds of the top Russian emitters», and the actions under those operations «were approved by the Ministry of Finance»¹⁵. Although there is no more recent data on this type of interventions, in February 2009, the issue of VTB participation in this scheme, was also under consideration.

3. In October 2008, as one of the extreme measures of support, an option was considered of the *acquisition of preferred shares and convertible bonds* (new emissions) of the emitters, supported by the government. This tool is common and has been used in a number of countries (UK, Switzerland) to support the problematic banking groups. Moreover, its appli-

¹³ In the scope of USD 45–50 bln at the Fund amount as of October 2008.

¹⁴ It is estimated that during the week of October 17-24, 2008 there was spent at least USD 1 billion, but the downfall in securities equities of the supported issuers, was continued (from 15 to 33 %). This means at least direct government funds losses, although in the short-term prospect the rates downgrading would be more significant in the absence of government interventions.

¹⁵ Kommersant, December 12, 2008.

cation does not make it necessary for the country to interfere in the operational management or directly participation in the stock equity.

By the end of February 2009 no information was available on the allocated for that purpose financial resources and the target of their allocation. Nevertheless, such proposals were submitted, for example, in late January, 2009 in regard to OC «Rusal» (conversion in preferred shares of the company debt to public banks in the amount of USD 6 bln. The pledge included 25 per cent of GMK «Norilsk nickel» shares, owned by «RUSAL»).

Apparently, in early 2009, *the policy of support has undergone significant changes* at the background of an overall shift of accent from the statements, made in autumn 2008, that «there is enough money for everybody» to the more sober strategy of reserves preservation till 2010-2011, selective support of the largest banks, rather than the global support to the companies.

First, through the above-mentioned program of foreign loans refinancing in the corporate sector, about 100 applications were submitted to VEB, totaling to USD 75 bln. However, the program was closed, when its expenditures reached USD 11 bln. Among the recipients were: Rosneft (USD 800 mln), UC Rusal (USD 4.5 bln), VimpelCom, Euras and some others. On the one hand, the program has been recognized inexpedient, as the majority of the participants have accumulated sufficient foreign currency reserves and were able to solve their problems with creditors independently (about USD 85 bln by February, 2009, which is, according to Government estimates, enough to settle credit payments in 2009)¹⁶. On the other hand, the terms of such credits, apparently, seemed too strict to the applicants (which is however, points to the undisclosed internal resources of companies to solve their financial problems without tighter government control).

Nevertheless, it should be noted, that even on the allocated credits, transparent public information on the selection criteria of the participants of the public support program is virtually not available. It is also not clear, how VEB intends to dispose the blocks of shares, obtained as a pledge, after the established one-year term (maximum credit maturity).

Secondly, in October 2008 it was envisaged to allocate RUR 450 bln from the National Welfare Fund for allocation with the «Vnesheconombank Bank Development», followed by RUR 225 bln. Allocation in the banking system for co-financing of the capital increase (by February 2009, private banks have selected RUR 17 bln.). Nevertheless, the policy of extensive infusions of funds into the banking system (by mid-February, 2009 it amounted to nearly RUR 3.4 trillion, including RUR 1.9 trillion of the debt of the banks to the Bank of Russia under unsecured credits¹⁷) did not result in the renewal of the mass bank investments in industrial sector. On the contrary, it is estimated, that the total credit, requested by the Russian enterprises from the government, was about RUR 3.5 trillion, while in December 2008, the relevant estimates of the Russian budget for 2009 imposed only RUR 325 bln for the crisis measures, and RUR 300 bln (including RUR 100 bln for defense enterprises) for the government guarantees¹⁸.

This has served, in particular, as a motivation to search for the new ways to support enterprises of the real sector by the government.

¹⁶ Money, № 6, February 16, 2009.

¹⁷ Power, № 6, February 16, 2009.

¹⁸ Merges and Acquisitions, 2009. № 1-2, P. 4.

The program for recapitalization of the banking system for lending to the enterprises of the real sector (in fact, that means the increase the state participation in capital), claimed in 2009, could cost about USD 40 bln (that is, actually equivalent to the «balance» of the suspended 2008 program of credit refinancing). The number of banks, which can participate in this program, is not defined yet, but there notably different official estimates, depending on the scope and models of public support and on participation (according to Vladimir Putin there should be 81 banks, according to I.Shuvalov - up to 50 in the case of subordinated credit co-financing, from 4 to a maximum of 30 banks in the case of additional emissions redemption). By early February, 2009 the model of support, when a direct state participation in the capital is foreseen only in 3 banks (VTB, VEB, Gasprombank) looked mostly realistic. Herewith, Sberbank, VEB, VTB and Gasprombank are instructed to extend credit portfolios by at least 2 per cent per month¹⁹. It is envisaged to provide subordinated credits to private banks in the (total) amount of RUR 100 bln. In particular, that means the government unwillingness to take the risks of operational management as a shareholder.

Back in 2008, a discussion has started of alternative (financial) approaches to the support of the Russian enterprises, operating in «important sectors of economy». By the end of December 2008 the absolute number of potential recipients of the state assistance within a short term has decreased 5-fold (1500 on the initiative of Vladimir Putin, 500 – proposed by Igor Shuvalov, 295 – by Elvira Nabiullina). Among the formal requirements for companies' enrollment in the anti-crisis program are such terms as: at least 5000 employees, RUR 15 bln of revenues, or the company is the principal local employer and mainstay. VEB should become the government agent in this trend of the state support. Companies will be able to invest up to 50 per cent of the government guarantees (enterprises of military-industrial complex - up to 70 per cent) as credit security. Herewith, the maximum amount of public guarantee to each applicant is limited to RUR 10 bln.

For 293 enterprises from 25 industries, which eventually have been included in the list of the RF Ministry of Economic Development and Trade, the credit support instruments are provided, but the range of possible solutions is much wider: the government guarantees (which are widely used as an anti-crisis measures in developed countries in the amount of nearly USD 10 trillion and require only a conditional reservation of funds), interest rates support funding, restructuring of the tax arrears, public contracts, customs and tariff policy. Some measures on mitigation the “negative social and economic impact of the businesses closure” are foreseen, apparently, in the event of bankruptcy²⁰.

By mid-February 2009, the information was disclosed on the applications of the largest Russian manufacturers for government guarantees under credits (from AvtoVAZ, GAZ, Kamaz and Sollers, totaling to RUR 29.5 bln). Among other methods of public support to the Russian automobile industry, the redemption of bonds up to RUR 60 bln and public procurement contracts for the amount of RUR 12.5 bln are envisaged. In the military-industrial complex there were taken decisions on state guarantees provision to 3 enterprises, on subsidies for 19 enterprises, balance of capitalization of RSK «MiG», amounting to RUR 15 bln. The state corporation «Rostehnologies» (which has received 20 of the local economic mainstays and

¹⁹ Vedomosty. February 3, 2009.

²⁰ Ref.: Public feeder for three hundred hamsters.– www.gazeta.ru, 26.12.2008.

278 of strategic enterprises) has requested the state guarantees in the amount of RUR 110.8 bln (in addition to RUR 151.32 bln of material contribution)²¹.

Though from a technical point of view, the range of anti-crisis measures of support is doubtless, there are at least two issues in terms of quality. First, the privileged list puts at an obvious risk the basis of the market (microeconomic) incentives to overcome crisis challenges on their own, namely in «the major» industries. Though the list is declared as an open one, an open tender procedure for applications for some kind of support (in case of anti-crisis programs availability) from any Russian enterprise would be more fair (if the traditional corruption component is ignored). Second, one can easily assume, that many of the problems of the enterprises are associated not only with the crisis as such, but with the management quality and credit policy, carried out in 2005-2007. It would be reasonable, if one of mandatory requirements to provide any kind of public support was the replacement of the existing operational management, perhaps, similar to the anti-crisis management (if the threat of corporate raiding and team replacement for the operation of remaining benefices are neglected).

Bankruptcy can also be regarded as a way of anti-crisis public interference. Herewith, the issue is not in the company liquidation or disintegration, rather than in the owner replacement or in the introduction of supervision by the authorized government body.

In any case, it is too early to give any more detailed assessments to the current developments, at least due to the lack of a critical mass of actually performed transactions, as well as insufficient open information, at least in regard to the scope and criteria for the State interventions. *There are grounds for the most pessimistic estimates at least in regard to the basis of the overall assessment of the institutional environment, which problems, in our view, have become one of the typical «Russian» indicators of the current financial crisis in the Russian economy*²².

Nevertheless, the conclusions to the beginning of a new phase in the state property expansion (even with regard to the objectively needed anti-crisis component) is indisputable. If capitalization of the Russian market would be sustained at the level of mid-October 2008, then, according to a simple calculation, one could predict the increase of the public share in the corporate sector within 2009-2010, or from 3-4 per cent (lower threshold) up to 9-10 per cent only due to the funds, allocated for intervention in the stock market. The scope of further expansion of the state sector is impressive, though there is no certainty about the Government plans yet:

- retention of public property the blocks of shares, pledged in VEB in the framework of the refinancing program in 2008 (USD 11 bln), performance term is late 2009;
- retention of public property the shares, acquired in the open stock market (USD 350 bln at the 2009-2010), decision-making deadline is in 2013-2014;
- further expansion of the state companies in the strict sense (despite partial withdrawal of the allocated financial resources);

²¹ It is remarkable, that it is planned to address RUR 34 billion to finance the purchase of shares in OAO «VSMPO-Avisma» by public corporation. Ref: Vedomosti, February 9-10, 2009, Kommersant, February 6, 2009.

²² Ref: A.D. Radygin. Stability or stagnation? Long-term institutional issues of development of the Russian Economy // Economic policy. 2007. N 1 (5). P. 23-47.

- acquisition by public banks assets of commercial companies, provided under the security of issued credits and through the direct acquisitions, formation of new state holdings²³;
- the increase of the state share in the bank capital in the framework of recapitalization program in the banking system (USD 40 bln). According to the Bank of Russia, the aggregate capital of Russian banks in early 2009 made RUR 2.5 trillion. With the level of the recapitalization scope, declared for 2009, it means that the state can claim for 32 per cent more of bank capital at the background of the overall growth of the state share up to 75-80 per cent²⁴.

At the same time, (other things being equal, including political and rent-corruption issues), a qualitative threshold of such expansion is obvious: the larger the public sector, the more limited are the opportunities for effective management and control. This is confirmed, in particular, by the experience of the introduction (the attempts of introduction) of any new instruments of management and control over the unitary enterprises and joint-stock companies with the state share at the late 1990-2000-ies. By analogy, with the evolution of Russian private business groups in the second half of the 1990's - early 2000-ies²⁵, in the medium term, one should expect some reorganization procedures, aimed at optimization of the structure of the acquired assets and organizational and management aspects of the public companies (groups) restructuring. In view of the financial crisis of 2008-2009, this process can be accelerated due to the need of companies (both, public and private ones) to attract financial resources through the disposal of a number of assets, not directly connected with their basic activity.

Moreover, the quantitative growth of direct government participation in the economy or a large permanent share of the latter are not extraordinary in the current global situation, especially during the crisis. According to the available estimates, by the end of 2008, in the framework of anti-crisis support, various countries have spent about USD 1.4 trillion for the companies' capitalization and about USD 880 bln for the new assets acquisition. Nevertheless, among the leading global countries, taking anti-crisis actions, large direct purchases of private assets in 2008 were performed only by the USA (USD 663 bln) and Norway (USD 51 bln), while the Great Britain, France, Italy, Germany, Netherlands and Japan carried out capitalization without the direct purchase of assets²⁶.

In fact, the financial crisis of 2008-2009 has resulted in the contradiction, or at least in the ambivalent situation.

On the one hand, the crisis events have urged a sound understanding of public sector scope expansion. The issues of the extended public sector management (in all its aspects, such as operational management, management expediency, ethical risks, «principal - agent» relations, corruption, rent, etc.) seem to be understood by the government. This is, apparently, confirmed by the gradual withdrawal of the government (during the crisis) from the direct methods of support by direct public participation in the capital of problematic private compa-

²³ In mid-February 2009, for example, the scheme of the key communications companies consolidation was discussed through the VEB, which has already received 90 % of shares «Svyaz-Bank» in autumn 2008 (purchase of 40 % of «Rostelecom» shares from «CIT Finance», 90 % of which belong to OAO «RZD» and ALROSA since autumn of 2008, as well as 25 % +1 share purchase in «Svyazinvest» holding from AFC «System»).

²⁴ *Commerzant*, February 4, 2009; *Money*, N 5, February 9, 2009 .

²⁵ See, for example, A. Radygin. The evolution of integration and management models: the major Russian companies and groups experience//*Russian Journal of Management*. 2004. V.2. N 4. October-December. P. 35-58

²⁶ *State Capitalism (Special issue)*. – *Smart Money*, N 143, February, 16, 2009.

nies and banks. Moreover, the ability of launching a new «program of global privatization», rather than the investment economic growth is becoming one of the options, discussed once again in the crisis. On the other hand, there is no reason to speak about withdrawal from the direct control principles, since the suspension of direct «anti-crisis» expansion, which is currently replaced by the stronger indirect control through a small number of banks, supported by the government, the formation of preference lists of «significant» enterprises, and through the continued activity of state corporations and state holdings (the few market subjects, having an opportunity for the new merges), the inevitable (though not as extensive as expected) and the nationalization of problem assets in its «hard» or «soft» options.

In view of the above, the most acute issues in the scope of the qualitative assessments, primarily the precise strategy, the objectives (incentives) and long-term results (costs) of the process are the most acute ones.

5.1.4. Privatization

By the end of 2008, it was evident, that privatization process was expressly slowed down, if not completely terminated. Large-scale transactions in this area were rare within the preceding years (although the reasons were different), but poor financial standing of potential buyers, as well as the reasonable reluctance of the government to dispose any assets for a trifling sum, in the face of crisis urged the slowdown in privatization of medium and small objects as well. In autumn 2008, in particular, such methods of privatization that could beat down the price of the objects enjoying minimum demand, were suspended. Apparently, a similar situation takes place in regard to the renewable revenues from public property (the suspension of dividend payments by companies with a state share of capital, land repurchase, etc.).

According to the official data of the Russian Property Agency, in mid-January of 2009, there were 1293788 objects of movable and real property in the Register of Federal Property (including more than 1.1 million of registration objects, owned the holders of relevant legal property right, and about 107,000 of the state treasury objects). The Register comprises also 3600 blocks of shares and nearly 67000 land areas, owned by Russian Federation. About 5700 Public Unitary Enterprises still remain in the property of the Russian Federation as well.

The plan for 2008 envisages the sale of share packages or public shares in 404 joint-stock companies and privatization (incorporation) of 440 Public Unitary Enterprises. The plan for 2009 (as of September, 2008) envisages the sale of securities or public shares in 291 joint-stock companies and the incorporation of 235 Public Unitary Enterprises. Herewith, the annual federal budget revenues from privatization of federal property in 2008 - 2010 were estimated at RUR 12 bln.

Initially, there were no large objects in 2008-2009 privatization plans, but this is based not only on the «suspension» of public sector in the background of state capitalism policy, routine conflict of interests and resistance of official authorities. Among other reasonable grounds, the rejection to use privatization techniques to replenish the budget and some technical problems should be mentioned. First of all, there is a one-year deficit (versus the official plan of privatization) in regard to such transactions even for a number of small and medium-sized enterprises. However, in accordance with the effective legislation, the transactions, failed to be executed before December 31 of the planned year, will be automatically shifted to the plan of the next year or dismissed from the scope of privatization process.

By some estimates, a number of innovations in the sphere of state management, that have been discussed or have already started to be implemented in 2008, could have served as a prelude to a new phase of «global privatization». First of all, this is an appointment of independent Directors to the large joint companies, starting from summer of 2008 (i.e., the image incentive to improve the quality of corporate management preceding public offerings), an opportunity for the privatization plan extension from 1 to 3 years (what allows to take time before passing through the entire cycle of preparations for the sale of a block of shares), tentative incorporation (in the true sense of the word), of the state corporations, established in 2007-2008.

Even at the level of official comments, plans for the new large sales are cautiously related to the year of 2010. Rather reasonable estimates of the crisis duration in the Russian economy for at least 2009-2010 leave the issue unresolved for a longer period (even only with regard to economic factors, i.e., beyond the policy of state expansion). Nevertheless, two extreme scenarios are already quite evident.

The first scenario is clearly based on the forced return to the privatization instruments implementation for the growing budget deficit financing (as in the 90-s.), despite the low cost of the disposed assets. In the macroeconomic context, this scenario has enough chances to be realized at the peak of the crisis, when oil prices are low, financial (gold) reserves are being exhausted and the budget deficit is growing. In fact, we are speaking about the sale of a part of public assets at dumping prices, though the internal motivation might be different - from the short-term (due to non-restorable source) assurance of the previous social commitments, up to the «non-transparent» allocation of assets, privatized for trifling sums among a narrow range of subjects. The combination of these two options is quite realistic, though in the first case one can speak about a wrong economic policy, and in the second case - about future suspension of «privatization of profits, nationalization of losses» model.

The second option, much more optimistic one, is based on the «soft» exit out of the crisis after 2010, gradual restoration of the stock market capitalization (assets value) regain and the beginning of single sales at the new wave of economic recovery. Thereby, the «large-scale privatization» should not be targeted at fiscal problems, but rather, like in 2000-2007, it should solve the problem of quantitative optimization of public sector and the government rejection of inappropriate functions of business entities management.

An alternative option of those two scenarios still remains in force, i.e., further quantitative expansion of public sector (direct and indirect) in the framework of anti-crisis measures of direct control, followed-up unlimited term of state ownership of the obtained objects. With regard to the anti-crisis measures of early 2009, mentioned above, it is nevertheless possible to imply, that the indirect measures are predominant, what implies both scenarios of privatization.