

# The New Role of State Corporations in the Russian Economy

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# What Is State Capitalism?

- Substantial state ownership of major companies
- Direct government intervention in these corporations
- Basically a capitalist system with market relations and private ownership of most enterprises

# Russian State Capitalism

Two-thirds of stock market capitalization. Mainly four industries:

1. Oil (50%), gas (75%) & electricity (Gazprom, Rosneft & Rushydro)
2. Banks (Sberbank & VTB, VEB, Agroprombank & Gazprombank) (60% state)
3. Defense Industry (Russian Technology, United Shipyards, United Aircraft & Rosatom)
4. Transportation (Russian Railways, Transneft, Rostelecom & Federal Grid)

# Private Sectors

Most industries are almost completely private:

- Retail trade and restaurants
- Consumer Services
- Non-defense manufacturing
- Construction
- Agriculture
- Mining
- Metallurgy
- Mobile phones
- Insurance

# Why Are Companies State-Owned?

- Gazprom: PM Chernomyrdin defended his old clientele
- Rosneft: Yukos confiscation in 2004
- Banks: Gerashchenko's preference for state banks after August 1998
- Transportation: Privatization never went that far

# Why Are Companies State-Owned? (2)

1. Remnants of state socialism – never privatized
2. Strong state managers opted for state ownership (Chernomyrdin, Gerashchenko & Sechin)
3. Putin's policy of state capitalism, 2004-8, aiming at political control and rent extraction
4. Access to cheap state funds and implicit state guarantees
5. Caused by long commodity boom (high oil and gas prices)

# Why Are Companies State-Owned? (3)

## Motives:

1. Political control (Putin)
2. Rent extraction by the state & cronies
3. Strong self-interest of state managers

## Not motives:

1. No socialist ideology. Putin has preached privatization and capitalism
2. No pretense of economic benefit

# Poor Company Valuation

Company	Market Capitalization	Price/Earnings
Gazprom	\$120 bn	2.9
Sberbank	\$65 bn	6.4
Rosneft	\$60 bn	5.2
VTB	\$18 bn	5.0
Transneft	\$10.3 bn	1.8
Rostelecom	\$10.2 bn	9.1
Federal Grid	\$8.6 bn	6.5

Source: Troika Dialog, September 2012



# How Are State Companies Faring?

- Many are secure monopolies and too exposed to efficiency control (Defense industry and transportation)
- State banks have increased their share of banking assets from 40% in 2000 to 60% in 2010 (Vernikov 2012). Cheap capital, implicit state guarantee & large economies of scale
- Rosneft thrives on Yugansk assets

Most state companies lose out on the market but seize or purchase assets with state leverage

# Gazprom: The Weakest Link

Challenge: US shale gas revolution has diverted LNG to Europe and European gas prices have halved.

- Gazprom is completely dependent on piping gas to Europe
- European Commission is pursuing anti-trust case against Gazprom – outcome given
- Gazprom's profit will be wiped out
- But that is the dominant source of rents for the Kremlin

# Sensible Transformation of Gazprom

- Stop all mega projects (South Stream, Nord Stream & new headquarters in St. Petersburg)
- Carve out Gazpromtransgaz as pipeline company
- Sell off utilities, finance and media, etc. (much done)
- Divide production into separate medium-sized companies

But then Kremlin's slush fund would disappear = not likely

# Where Gazprom Goes, Russia Goes

- Gazprom's crisis is the key to the future of state capitalism and Russia
- This crisis can be averted by swift changes of oil and gas prices, but that is not likely
- If Gazprom no longer delivers rents, the Kremlin has little reason to maintain state capitalism, which may dwindle