Working Paper

Ownership, Control Over the Enterprises and Strategies of Stockholders

Alexander S. Bim

WP-96-050
May 1996

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Foreword

The Economic Transition and Integration (ETI) Project at the International Institute for Applied Systems Analysis (IIASA) started a research activity on the behavior of Russian enterprises under liberalization, privatization and restructuring in 1995–1996. This activity originated upon the initiative of the Ministry of Economy of the Russian Federation. The major reason for focusing on this subject was the fact that the current state and further transformation of Russian medium and large sized enterprises became a challenge for the continuation and success of transition related reforms. Despite certain positive tendencies, numerous enterprises still adjust themselves to ongoing changes without considerable market adaptation and modernization. The emerging ownership structure and financial markets demonstrate limited positive influence on stockholders' incentives, decision-making process and strategies of restructuring.

In the course of these enterprise studies, a workshop on "Russian Enterprises on the Path of Market Adaptation and Restructuring" was organized at IIASA on 1–3 February 1996. Russian and Western experts, extensively working in the area of enterprise performance under transition, focused the discussions on recent empirical findings and analyses concerning the following issues: typical models of enterprise behavior; development of the financial situation at the enterprises and its determinants; impact of emerging markets and competition on enterprises; the consequences of privatization and patterns of restructuring; and enterprise social assets divestiture and conversion. The workshop arrived at both analytical conclusions and recommendations for policy measures stimulating "constructive" enterprise behavior. Possibilities for a joint research project on the motivations and behavior of enterprises in transition economies were also discussed.

The circulation of selected workshop papers as IIASA Working Papers is undertaken in order to provoke broad discussions of presented analytical results. This paper by Dr. Alexander S. Bim examines challenging processes of ownership transformation at Russian privatized enterprises and their impact on investments and other key factors of enterprise restructuring. Analysis is focused on controversial behavioral strategies of managers and other new owners.

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Ownership, Control Over the Enterprises and Strategies of Stockholders

*Alexander S. Bim**

Abstract

This paper examines challenging processes of ownership transformation of Russian privatized enterprises. The major tendency is steady and continuous differentiation of the insider stock on that of managers and that of non-managerial employees. Therefore, wide-spread managerial control is in a process of successful transformation into control of managers-owners.

Managers demonstrate controversial behavioral strategies. The minor part of them utilizes control over enterprises for active market adaptation and restructuring, while the most of directors are much more devoted to intensive income and capital extraction for their own short-term benefits. Advantages and shortcomings of both strategies from macro- and microeconomic standpoints are revealed in the paper.

In order to make the process of ownership concentration more consistent and irreversible, top managers create and strengthen in-enterprise managerial coalitions. It is argued that these coalitions are a peculiar and significant feature of an on-going concentration of enterprise stock; in addition to them, outside managerial coalitions are emerging on the basis of mutual penetration of stock of technologically related companies. The latter pave a path to changes in existing enterprise boundaries.

A portion of outsider investors, who own or control Russian enterprises still remains low, although there was slight growth during 1994–1995. Not only is the relatively modest financial potential an obstacle, but the strong unwillingness of enterprise managers to exchange control and ownership for monetary inflows, which in principle could be provided by interested outsiders, as well.

Actual outsider owners do not demonstrate less problematic incentives and behavior than managers. Hence, the problem of efficient corporate governance does not seem to have synonymous solutions in Russia. Real characteristics of enterprise performance under transition are more dependent on individuals in charge of companies, than on what socio-economic group they represent.

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The paper deals with the desirable functions of the state in the area of privatization and enterpise performance. Given limited leverage of the current statehood on economic developments, it is not clear enough whether suggested functions can be implemented.

1 Introduction

The speed and scale of Russian privatization were quite substantial during 1992–1994. From the beginning of 1992, when nation-wide privatization started, 112 thousand small, medium and large sized enterprises eventually changed the type of ownership, including some 65 thousand during 1993–1994. Instead of former state enterprises joint-stock companies with mixed ownership structure have been created in most cases. (See Frydman, Rapaczynski and Earle, *et al*, (1993) and Bim, Jones and Weisskopf (1994) for a summary on the methods and variants of privatization in Russia).

Privatized enterprises employ about 17 million people, which is 23% of the economically active population. (Sotsial'no-Ekonomicheskoye Pologheniye Rossii, 1993–1994). According to the VCIOM survey, done in early April 1995, a portion of privatized firms within the standard enterprise-size categories appeared to be the following: among the firms with 1,000 and more employees 35% were privatized; among those with 501–1,000 employees — 10%; among those with 201–500 employees — 17%, and among the companies with less than 200 staff members 20% were privatized. (New Russia Barometer IV, 1995).

Naturally, institutional changes of such a global size have drawn a lot of attention towards their actual consequences, i.e., towards the impact of privatization on enterprise economic status, behavior and development. Focusing on the consequences makes a lot of sense: neither numbers of privatized entities nor volumes of circulating vouchers and shares, but qualitative changes in ownership, patterns of control and decision-making, evidence of market adaptation and restructuring of enterprises determine the real significance of the privatization campaign and results.

This paper examines institutional changes within the former state enterprises, following the first phases of Russian privatization. It focuses on the background for new patterns of incentives and behavior, demonstrated by the most important economic agents involved in enterprise performance in the course of privatization. Those patterns have already significantly affected the economic status of privatized companies, restructuring perspectives and further privatization developments, which are also the subject of this paper. More concretely, the following issues are explored:

- Development of the structure of ownership. What are trends of modification, that has occurred to ownership structure, predetermined by initial privatization procedures — in-enterprise subscription for shares, voucher auctions, etc.? What kinds of circulation of enterprise stock are typical and why? What does the current pro-portion between insider and outsider ownership look like? Are there any significant changes within insider and outsider stakes?

- Stereotypes of incentives and behavior of major stockholders. Strategies of insiders and outsiders towards ownership, control and enterprise performance.

- The interrelation between ownership and control. Do transformations of ownership structure lead to new patterns of control? Or, to put it more explicitly, are emerging (modifying) and strengthening patterns of control over the enterprises adequate to ownership structures, by which these patterns are supposed to be stipulated?

- Corporate governance or authoritarian control? What are the prospects for civilized corporate governance in contemporary Russia?

- Relevant policy recommendations.

This paper is based partly on the outcome of enterprise surveys, which were conducted by the author while working with the Russian Privatization Center.[1] For more about the results see: Bim (1994a).[2] Given the limited size of the sample surveyed and the fact that in some respects, changes in enterprise performance were quite dynamic during 1994–1995, the latest empirical results, presented more recently by other researchers and research teams, are broadly discussed in the paper and also involved in the analysis.

Since the author had interviewed enterprise directors, other managers and employees personally, he did not only follow a formal questionnaire, but tried to maintain a dialogue with respondents, to make them talk in order to extract both explicit and implicit information. Thus, not all the statements of this paper, although based on survey results, may be supported by formal, quantitative characteristics. Therefore they could be considered by strict readers more as hypotheses. Some of such statements are strengthened by the fact that they are completely conformable to conclusions, presented in literature. But some statements sound different. Further empirical findings will either confirm those hypotheses or disprove them.

[1] Under the auspices of the Russian Privatization Center, the author conducted in 1993 in-depth interviews with general directors, top and middle-level managers and non-managerial employees of 24 enterprises, located in three regions of Russia — Far East (Primorskii kraj), Vologodskaya oblast and Saratovskaya oblast. The sample reflected quite different sectors of the economy: the wood processing industry, machinery, light industry, food industry, construction, transport, military-industrial complex. All the enterprises had completed the so-called initial privatization procedures (in-enterprise subscription for shares, voucher and first monetary auctions) and were privatized: the state retained not more than 25% of the stock. Observations were then continued in 1994.

[2] Figures with no special quotation in this paper are taken either from Bim (1994a) or from unpublished components of survey results, that are on the author's files.

2 Ownership Structure

The analysis, presented in this section, is focused on some major trends that predetermine the formation of core stockholders and real control over the enterprises. For more general observations of ownership structure dynamics see Boycko, Schleifer and Vishny (1995).

It is quite well known, that most of the enterprises have chosen the so-called second option for privatization (for a description of Russian privatization general framework and options see Frydman, Rapaczynski and Earle, *et al*, (1993) and Bim, Jones and Weisskopf, (1994). In Bim's sample 83.3% of newly created joint-stock companies (transformed state enterprises) had followed this path. The corresponding figure for all industrial enterprises is 78% (Gurkov, 1995).

It was commonly supposed that the second option would lead to significantly prevailing insider ownership with all the inherent characteristics, appreciated by adepts of this type of property relations (of so-called collective ownership) and blamed by its critics (for debate see Bim *et al*, 1994). While not including a theoretical discussion here, it is necessary to mention that insider ownership has, in fact, become quite widespread. According to Blasi and Shleifer (1994) insiders held about 65% of enterprise shares in 1993.

At the same time insider ownership in Russia has manifested itself as a peculiar phenomenon. First, it differs from that advocated by East European and Western enthusiasts as collective ownership. Second, it has started very soon to disperse and, hence, has become substantially differentiated. Third, eventually it became clear that under certain preconditions this type of ownership may be transformed more or less naturally into ownership with considerable and even major outsider stake.

The main distinction between Russian insider ownership and a classical model of collective ownership is the absolutely predominant role of managers in governance and control over the Russian privatized enterprises, that are formally owned by all categories of insiders (this issue will be thoroughly revealed in the subsequent sections of the paper).

As far as dispersion and differentiation of insider ownership are concerned, Bim's surveys showed the following facts. At the end of 1993, non-managerial employees possessed more than 50% of shares only in 16.7% of the surveyed companies. In the prevailing number of joint-stock companies — in 66.7% of them — non-managerial employees acquired 30–50% of the shares with a good portion of the companies quite far from the upper margin of this interval. That meant that this vast group of insiders was actually not a core owner: **without integration (getting in coalitions) with any other group of stockholders, non-managerial employees could not establish even formal control over the stock and, therefore, over the enterprise**. Given serious "positional differences" between managers and other employees it seemed reasonable already in 1993 (see Bim 1994a) to draw attention to the quite peculiar nature of insider ownership in Russia and to argue against simplifications such as common statements of 1993–1994 that privatization in Russia had proceeded *de facto* in favor of workers (employees) or insiders as a homogeneous group.

At the end of 1993 the portion of managers in the structure of enterprise shareholdings appeared to be the following: 3–5% of the shares belonged to managers in 20.8% of the surveyed companies, 5–10% — to managers also in 20.8% of those, 10–20% of the shares were acquired by managers in 12.5% of the companies, and 20–30% of shares belonged to managers in 8.3% of the surveyed companies. Outsiders obtained, on average, 10–15% of enterprise stock. In Blasi's sample (1994), top management (with no indication as to exactly who was covered by the characteristic "top") obtained 8.6% of shares on average. The percentage of outsiders in his sample was higher — it reached 21.5%.

In the course of 1994, according to the author's observations of the same sample, the picture changed. At the end of 1994 and at the beginning of 1995, in more than 70% of the companies non-managerial employees got less than 50% of the stock, and managers obtained in about 60% of the companies 10–30% of the stock. The portion of outsiders on average increased slightly — up to 15–18%, but in several companies outsider stake grew up to 30% of the shares. In the much larger sample of Earle, Estrin and Leshchenko (1995, 439 enterprises), on average across privatized companies, workers held 48% of the shares, managers 21% and outsiders 20%.

The numbers and major outlined tendencies — (i) differentiation of insiders and progressive increase of managers' stake and (ii) slow growth of outsider stake as well as the appearance of a number of outsider owned enterprises — are also obvious from the surveys, that were undertaken by other researchers and research teams (see Earle, Estrin and Leshchenko 1995, for a summary).

Nevertheless, the fact of early and considerable dispersion of insider ownership among different insider groups is surprisingly stressed much rarely. In our view it is quite essential that, basically, workers (employees) ownership (or insider ownership in a classical sense) in many cases appeared to be not the fact at all, and — what is more important for our considerations now — workers themselves are possessing controlling stake rather rarely and, therefore, are unable to control enterprises without unification with other groups of stockholders. This trend also confirms earlier assumptions, that in the course of privatization managers will gradually increase their shareholdings to become majority owners (Peck 1995).

3 Major Characteristics and Strategies of Stockholders

3.1 Managers

The crucial characteristic of the status of managers is that in the course of reforms, top managers not only remained the key figures at the microeconomic level, as they used to be under communism, but have significantly strengthened their positions in almost all respects. There are at least three reasons for that.

First, weakness of the current statehood — certainly not in a sense of giving up centralized planning and distribution, what was natural under market transformation of the economy, but in a sense of inconsistency and discrepancy in reformist economic policy. Classical examples are: unpunished inter-firm arrears; federal and local subsidies, remaining in hidden forms at large; various individual (per enterprise) exemptions; absence of bankruptcies. A badly regulated economic environment gives much room both for normal, productive managerial performance and for perversions in managerial activities.

Second, a deficiency in constructive intentions and mechanisms of enterprise governance which should have been caused by privatization. What seems most important here is the lack of appropriate control over managers.

Third, social immobility and depression of employees unable to somehow defend their interests.

It sounds symptomatically, that none of the interviewed directors had complained about the lack of self-dependence and about pressure either from the upper or lower levels as reasons for the difficulties, which managers have now to overcome. These sorts of complaints used to be quite typical under communism. Gurkov (1995) mentions the same: according to him, top managers are almost completely satisfied by their independence in decision-making — the average estimate of respondents was 4.55 on a 5-point scale.[3]

There are reasons to argue that most directors have been successfully accustomed to transitional reforms of *a lá Rus* type. This was forecasted in 1992 (Bim, 1994b) and has been since then confirmed. It means that despite their often loud public claims, managers at that time already did not rely seriously on the state as a supplier of resources in any direct way and either free or almost free of charge. It appears to be even more important, that directors understood that a transitional situation might promise enormous benefits to themselves; in their explicit or implicit interpretation, negative consequences of reforms would mostly affect enterprises as such and enterprise workers (employees), while benefits flow exclusively to top managers.

This is completely relevant to privatization. Blasi (1994) and others emphasize, that despite the evidence that insiders as a whole (and among them employees) have held a major stake of the shares, control has concentrated around enterprise executives (general directors or CEOs). Initial stages of Russian privatization and post-privatization development clearly have led to **managerialism** (for one of the good definitions see Szelenyi, Eyal and Townsley 1995), typical to other transition economies of Eastern Europe as well. But the scale and significance of this phenomenon is much more challenging in Russia.

[3] One of the major new dependencies (if not to say bondages) of the enterprise directors is certainly their dependence on the *mafia* (criminalized shadow business activities). *Mafia* connections are usually out of more or less exact considerations through conventional economic surveys due to the obvious impossibility of obtaining reliable information. There are claims that the *mafia* is rather persistent in intervening into the Russian industrial sector in the course of privatization.

Surveys made it clear that directors find (or feel) certain interrelations between the constraints of shocking, speedy economic transformation and their possibilities to fulfill individual and corporative interests. 63% expressed no doubts that gradual and "better organized" reforms probably could soften many kinds of constraints, but would definitely decrease individual and corporative opportunities for managers as well. This consideration helps to interpret the unarguable fact that during the whole period of Russian reforms, industrial managers refrained from serious attempts of putting political pressure on the government by heating dissatisfaction and tension among workers.[4] Hence, the hypothesis can be built up, that despite the fact that many industrialists used to be and still are in the prison of old-fashioned communist stereotypes concerning enterprise and national economy organization, they appeared to be much closer to pro-reformist orientation than had been often initially predicted. Nowadays the alliance of enterprise directors with any sorts of marginals looks less and less imaginable: entrepreneural and wealth interests of managers lie far from those of losers in the series of stormy battles for the marketization of Russia.

It is not surprising, therefore, that politically most directors extend support to those parties and/or public movements that do not intend to overrule the achieved results of privatization. At the same time, directors favor politicians, who claim to soften budget constraints, to provide or enlarge tax and duty exemptions, etc., but to the best of our understanding they do not seriously believe that combination of such intentions with irreversibility of privatization results is very likely. So such unrealistic claims do not seem to be of any serious danger.

What might be much more likely and destructive, is state protectionism towards current ownership structure, already practiced by certain federal and regional bodies and declared by some politicians as their future goal and pre-electoral obligation. This is synonymously favorable for most directors and could prevent outside investors (both domestic and foreign) from persistent interventions into the industrial sector.[5]

There is a debate (see, for example, Earle, Estrin and Leshchenko 1995), whether it makes sense to rely on self-reported perceptions of managers concerning their own role in control over the enterprises. Certainly it would be not bad to relate those perceptions to any kind of hard data (reports from the annual meetings of shareholders or meetings of the boards of directors). But, first, this is not always feasible. Second, the reliability of hard data of this particular sort is at least to say not less questionable than the results of in-depth interviews. In our surveys (as well as in Gurkov's) the role of managers has

[4]Well-known strikes and other "protest activities" of the coal miners (Kemerovo and Vorkuta regions mainly) are the exception. These actions often reflect not only the aggressiveness of trade union leaders and workers themselves, but the attempts of directors to gain "support from below" for their claims as well.

[5]One of the most known cases is the willingness of the regional administrative and juridical bodies of the Krasnoyarskii kraj to reverse the results of privatization, occurred at the Krasnoyarskii aluminium plant, in order to help the general director to get rid of outsiders, which had obtained a large stake in this company.

been evaluated as high by non-managerial employees, local officials, actual and potential outsider investors as well. In Bim's sample employees, for instance, reported that enterprises have been under the complete control of managers in 82% of the cases in 1993 and in about 80% in 1994.

Top managers closely identify their individual interests with enterprises. This is not a surprise at all: what other comparable values if not businesses being at their complete disposal, can directors offer in "the market of opportunities" typical to the circumstances of transition? That is why, as it was revealed in the previous section, they do their best to make this advantageous position stronger and irreversible by concentrating enterprise stock directly in their own hands.

Russian evidence does not corroborate the conclusion of Szelenyi, Eyal and Townsley (1995) that conditions of economic uncertainty do produce disincentives for managers to become private owners. This statement is fully applicable to outsiders (although many of them are quite active in privatizing as well), but in the case of managers it seems to be misleading. Directors already practice control over the enterprises and gain a lot from it, so their experience of privatization is quite positive. At the same time, they do not have any alternative sources of doing well nowadays and in future — contrary to banking and trading entrepreneurs. So they have all the incentives to try to keep their controlling position. But they fear outsiders, who are eager to seize control away from managers through further stages of privatization. So they have to be aggressive in privatization in order not to lose control. These are good reasons for directors to be willing to reinforce actual control with genuine ownership.

Blasi (1994) presents the same conclusions. He examined opinions of the senior management of enterprises concerning future optimal ownership of their companies. It would be strange if opinions about this subject did not implicate intentions as well. Senior managers reported, that desirable ownership structure would be the following: all insiders — 72% of the stock, employees (excluding top management) — 32%, top management — 40%, all outsiders — 27%, and the state — 0%.

However, the nature and the manifestations of managers' interests towards enterprises are not homogeneous. 1993–1994 surveys made it possible to argue for two essentially distinctive managerial strategies (Bim, 1994a). The first one could be called **constructive** and means that managers try to do everything possible for the efficient adaptation of enterprises to new circumstances. This involves (either/or) modification and modernization of production mix, substitution of suppliers and consumers by more suitable ones, improvements of inter-firm organization, necessary cuts of personnel, restructuring of fixed assets and so forth. Approximately 26–28% of the interviewed directors were radical enough to be considered as followers of this strategy.

The alternative strategy is naturally suggested to be called **destructive**. It is followed by enterprise executives who realize that, due to quite different reasons, their core businesses cannot be reliable sources of prosperity for a considerably long period of time. Such reasons might have their roots, in particular, in the sectoral allocation of enterprises. Those in the light and food processing industries, for example, are very unlikely to promise under current conditions any wealth to entrepreneurs because of severe competition of imports. So **immediate efforts are made by managers not to adapt enterprises, but first of all to succeed in creative and intensive extraction of incomes and enterprise capital itself for their personal benefits**. These efforts sometimes may be easily defined in terms of barbarism or robbery. No less than 60% of the interviewed directors, while discussing concrete matters of enterprise performance, implicitly confirmed involvement in activities of this sort.

Forms of the above mentioned extraction might be various and depend on both the creativity of managers and enterprise characteristics: profile, boundaries, technological complexity, status of privatization (scale of outside control), etc. There are several common ways. 1993 was outstanding from the point of view of income extraction by managers — their salaries exceeded those of workers and other non-managerial staff 5, 10 and more times. In the surveyed sample, 38% of the top managers reported their salaries to be higher than the enterprise average 5 and more times.[6] These figures probably were not something outrageous in principle (the gap aggravated throughout the years and at the beginning of 1996 reached in some cases 40 times, see Open Media Research Institute Daily Digest No. 34, 1996-02-16), but the given Soviet tradition of equalizing incomes they did mean rather substantial differentiation.

Beginning with the late 80s, enterprise managers practiced largely to offer enterprise premises (sometimes with equipment, sometimes — not) for lease. Dolgopiatova (1994) points out that leasing used to be one of the main "survival oriented" measures in enterprise activities. This kind of business cannot be qualified as perversion as such. It sounds normal in general, and in specific Russian circumstances, large-scale leasing played an extremely positive role in the development of newly created private entities: without renting premises from the state and former state institutions they simply could not start and survive. But the crucial point for our consideration in the current context is, that rent actually is utilized as the one-sided benefits of general directors and their entourage. Few investments of any sort are usually based on leasing-out premises or equipment. In 73% of the surveyed cases, non-managerial employees claimed to have earned nothing from the rather advanced leasing-out activities of the top management. Revenues from leasing-out premises, etc., are normally used for the all-enterprise needs in the cases of emergency only.

Another common path, successfully followed from the late 80s, is the creation of numerous semi-state or semi-private small businesses around the core ones, through which enterprise resources are channelled to physical persons — principals of these small businesses — and then utilized by the latter with no further relation to the deals of the basic

[6]It sounds interesting, that wide-spread wage arrears are in no cases applicable to enterprise managers. While non-managerial employees may be on mandatory unpaid leave, managers continue to be paid even if the production process is terminated, consumers do not pay, banks impose sanctions, etc.

enterprise.[7] In 100% of the cases, those principals are enterprise officials personally or their allies. It certainly appeared to be quite difficult to get obvious answers from the directors on this point, but 73% of those interviewed reported to have small "surrounding" businesses organized under their auspices. All such businesses were evaluated by managers as surviving, 72% of the existing number — as enlarging or gradually being transformed into more vast private entities.

Dolgopiatova (1994) indicates more modest figures: in her sample, referring to 1993, from one-fourth to one-third of the enterprises have practiced the organization of satellite businesses. Szelenyi, Eyal and Townsley (1995) argue that surrounding private firms, owned by managers (these authors call them "subcontracting', which is not exact in all cases), are typical to privatized enterprises in Eastern Europe also.

The next form of enterprise capital extraction is strongly connected with foreign trade transactions and related hard currency outflows (quite well known as "one-way travel of exports").[8] Middle-level officials in 21% of the surveyed companies informally and occasionally (while discussing other issues) reported that top management had obtained property (real estate) abroad on behalf of the enterprises or satellite businesses. Exported and not repatriated capital has certainly been channelled into Western financial markets as well.

The aforegiven statements are conformable to the results of the VCIOM nationwide representative sample survey of 1,998 Russians, covering European and Asiatic Russia and both urban and rural areas (Source: New Russia Barometer IV, Centre for the Study of Public Policy, 1995). With reference to privatized enterprises, 28% of the respondents reported that managers used firms' assets for private benefits, 14% gave negative answers, and 58% reported that it was difficult to say anything exact.

It is reasonable to mention that the described forms of so-called opportunistic behavior are to a certain extent shared by all top enterprise executives, even by those who pursue constructive strategy of management. Key orientations and scale of unfair capital extraction are different, but some inherent characteristics of typical behavioral patterns are similar. These realities characterize the major and most unpleasant feature of vague and uncertain mixture of socio-economic interests and incentives, typical to the current stage of socio-economic transition: **superiority of individual interests over public, corporative and other private interests reached a height, which implies**

[7] Beginning with 1986–1987, numerous cooperatives, joint ventures and — later on — other forms of small businesses, eventually emerged. (See Bim, Jones and Weisskopf 1993) for quantitative characteristics and description). Both logically and historically they appeared to be the predecessors of contemporary satellite businesses, sometimes after the transformation into more modern forms of enterprise organization, more rarely — kept under their initial status.

[8] During recent years, Russian and Western literature have been giving rather different evaluations of the foreign currency outflows. One of the estimations referring to 1992 and 1993 suggests, that during each of those years hard currency outflows reached 15% worth of GDP (The Jamestown Foundation Broadcast, January Prism, Part 2, 1996-01-13). Other sources come up with the cumulative figure of USD45 "Russian billion", kept and circulated outside the country.

complete separation — up to opposition — of individual interests from the interests of institutions (public, private and "mixed" structures), of which bearers of those individual interests are members and even heads. To put it more transparently, it means that incentives and efforts of managers, aimed at individual success and wealth are quite natural. They should be welcomed if they would not contradict dramatically the state of a company. Unfortunately, the Russian transitional phenomenon is completely opposite: the wealth of managers is built up not necessarily on efficient company performance or restructuring, to the contrary — very often it is based on purposeful and semi-legal capital extraction. That is why this phenomenon is called "opportunistic behavior".

Estrin (1994) underlines that in circumstances where owners do not directly control decision-making, mechanisms of governance are required to ensure that managers are motivated to maximize profits. Now it is clear, that it is critical to stress that the talk should be about **enterprise profits**, which ought to be maximized; otherwise there are reasons to evaluate existing mechanisms of company governance in transition countries as quite efficient since they work rather perfectly for maximizing the individual profits of managers with no relevance to the results of companies' performance.

Peck (1995) gave a forecast that if managers become the dominant owners of enterprises, they would focus on profit maximization — exactly what a market system requires. In respect to real market economies this is a truism, but in respect to transition economies it sounds quite a bit like simplification. Russian evidence suggests that for the time being, a minority of directors identify their own profit maximization with that of enterprises. Therefore, it seems difficult to support the confidence that all of the managers, while trying to acquire a controlling stake of shares, are thinking necessarily about companies' progress (profit maximization) and not about better conditions for themselves as potential dominant owners for further profit and capital extraction.

From macroeconomic and institutional standpoints "managerial parasitism" can not be considered simply as a shortcoming (see below). **But the fundamental fact that managers in charge of enterprises, which they in fact own or exercise full control over, are so far delimitating their personal interests and interests of a company as two clear extremes, does not sound very optimistic**. More observations are needed to come up with generalized conclusions on this point. But it seems to be clear that general political and economic uncertainty, as well as peculiar cultural stereotypes, rooting in the past, play a no less important role in the formation of managers' strategies, than privatization as such.

Parasitism of managers, being too painful for a particular enterprise, its employees and stockholders, might have paradoxically better implications on macroeconomic and institutional developments. In fact this is a strategy, the extreme of which leads enterprises to inevitable bankruptcies along a probably much shorter path, than that of other potential bankrupts. This means that, from the standpoint of badly needed general structural adjustment, reallocation of national resources, mobility of the labor force, this strategy could not be so disastrous.

A constructive pattern is beneficial for stockholders if it means attempts of radical restructuring. The positive potential of this strategy, however, may be undermined by a misleading identification of an enterprise as a property object, materialized capital, and an enterprise as a productive entity in its current shape (production mix, boundaries, employment, etc.). Constructivism cannot mean conservation of the latter; it necessarily means restructuring aimed at profit and/or capital maximization.

3.2 Workers (non-managerial employees)

All the interviewed managers and almost all the non-managerial employees reported the lack of any positive influence of privatization on incentives and behavior of workers. The strongest "privatization interest" demonstrated in the course of 1993 was the interest in dividends. Then, given low levels of dividends and their extremely limited availability, employees stopped paying much attention to them.[9]

Another normal interest for stockholders, such as participation in enterprise strategy development and decision-making, according to our observations, is much weaker than is sometimes suggested. In the shareholders' meetings the top leadership dominated completely. Evidence, that some "worker owned firms" (where the major stake remains in the hands of employees) do exist, does not contradict this statement at all. Simply managers in these particular cases either intentionally refrain from further stock acquisition or do not have enough resources for that. At the same time, they are in full control over companies.

If any single fluctuation of workers' activeness occurs, "the activists" are usually unsuccessful in seeking decisions, alternative to those suggested by management. Alliances of non-managerial staff and outsider investors due to the initiative of the first, which could support stockholders-employees in attempts to override managers, are quite rare so far.[10]

Employees are still more often supportive to management in the conflicts "managers vs. outsiders", because they consider even tough managers to be less radical and more tolerant towards employees than "strangers" could potentially turn out. The idea of stock

[9]The level of dividends was initially connected with the prices of shares and therefore low. Moreover, it has been devalued continuously due to inflation. Directors in all cases prefer not to pay dividends, referring to different complications and to a lack of resources. At the same time, they try to pay the so-called "13th salary", explaining to employees that for them it makes no difference in what form — dividends or old-timer payments — employees will receive money. In this way outsiders are certainly discriminated against insiders and the latter, on the contrary, are appeased with the fact of this discrimination as such and with "keeping enterprise profits from unfair distribution among strangers". If the companies are controlled by outsiders, the dividends are certainly paid, but because of modest size still do not play the role of "good incentive" for employees.

[10]Such situations still occur. One of those well announced by the mass media was the dismissal of the old-timer general director of the Vladimirskii tractor plant and the election of a middle-aged Western educated blockholder to this position in 1993. In Bim's sample there were 12.5% of such cases.

concentration in the hands of managers, although not very popular among employees, is still closer to their hearts than that concentration by outsiders. In 72% of the cases in 1993 and in 73% in 1994, responses of interviewed workers showed clearly, that managers had succeeded in creating an "enemy image" with respect to outsider shareholders throughout working collectives.

According to the directors' estimations, from 10–12% (1993) to 15–18% (1994) of non-managerial employees are not interested in their position of shareholders at all. These employees do not see advantages in holding a small part of enterprise stock or, what is more or less the same, do not believe in the reality of any proclaimed advantages. This group of in-house stockholders is most inclined to sell their shares — if not to say get rid of them. They are the main suppliers of shares to both financial markets and to eager managers.

Gurkov and Maital (1995) also indicate some related facts. More than 40% of the workers in their sample reported that their capacity to influence decision-making deteriorated after they became shareholders, and 38% indicated "no change". 46% of workers-shareholders even mentioned that their access to information about the performance of their companies had also become worse after privatization. About 50% of the workers reported playing no role in any kind of distribution including that of dividends.

It does not sound surprising then that privatization, as 100% of the directors do point out, has not yet demonstrated any positive influence on employees' motivations as workers and specialists. Having no role as stockholders, why should they be well motivated as enterprise functionaries? Such factors of higher motivation as the threat of layoffs and wage level do matter, but first, they are not directly connected with privatization, and, second, are in fact beyond any real influence of employees and sometimes even of that of managers. Externalities like level and structure of market demand and arrears of consumers' payments appear to be much more important factors, that determine the economic situation at the enterprises and its impact on employees. The VCIOM survey results offer a pessimistic estimation of current labor activities, based on responses of workers themselves: 60% of them claim that they are "often doing little at work". Characteristically, this figure is the same in reference to state and privatized enterprises. (New Russia Barometer IV, 1995).

3.3 The State as the Enterprise Stockholder

The state bodies in charge of implementing the privatization program were initially assigned 20% of the enterprise shares. In some cases property funds kept up to 30% of the shares — due to the fact, that not all of those envisioned for sale, were successfully realized through primary privatization procedures (close subscription, voucher and monetary auctions).

In principle, the state institutions are supposed to release the enterprise stock in the course of the global process of separation of the state from the economy and depoliticization of enterprises. Nevertheless, there is a resistance towards complete privatization of former state enterprises. On the one hand, such resistance comes from the state apparatus of different levels, that dreams about retaining at least some control over companies. For a lot of remaining *nomenklatura* this is a question of survival.[11] On the other hand, directors, who fail to adjust enterprise performance to the marketization of the economy, prefer to keep links with the state wishing to be supported and protected by authorities. Both sorts of resistance determine different restrictions, which from time to time are put on privatization of the state stake in enterprises of various sectors of industry.

By definition, a process of legal and administrative regulations of privatization rests in the hands of the state. General rules and procedures were more or less set up during 1992–1995. But, as usual in Russia, implementation becomes a problem. Sometimes difficulties arise, when federal, regional or local authorities make controversial decisions on particular points, that are based not on regulations in force, but on one-sided interests of the parties involved in privatization. (See the footnote 5 mentioning the attempts of restitution at the Krasnoyarskii aluminium plant). Such tendencies certainly seem quite dangerous for continuing privatization and its impact on enterprises.

There are two main issues concerning performance of the state institutions as stockholders. The first refers to their participation in the decision-making process at the privatized companies, which is important, given their possession of a large enterprise stake. Strategy of the property funds in this respect seems to have been quite standard: in the general meetings of the shareholders, called in order to elect the directors and executive boards, property funds' representatives used to vote for the candidates who were supported by the majority of other voters. Another variant: if regional authorities, to which the respective property funds are subordinated, had any preferences, representatives of the property funds at the general meetings supported the relevant candidates. In the board meetings enterprise executives have been usually backed by property funds. Both enterprise managers and heads of property funds, confirmed these latter policies in the interviews.

The second issue has been a subject for sharp debate: the continuation of the privatization process in respect to the further destiny of enterprise stock held by the state. Already in 1994, it became more or less clear that financial markets would not absorb much of the enterprise stock, in particular — that which was consolidated in large packages. Demand from outsiders was not large enough. The splitting of packages, currently held by the state, was considered by experts and policy-makers to be undesirable, due to a likely negative impact on the prices of shares and on the creation of potentially efficient stockholders.

[11]Considering the necessity to keep enterprises under control, bureaucracy has not necessarily formal benefits in mind, which it obtains from the state for doing the job. These benefits could hardly be compared with earnings in the private sector and, hence, are not very attractive. But what matters, are the illegal relations between *nomenklatura* and loyal enterprise directors. Through these relationships statesmen [may] get a lot in exchange for different kinds of exemptions and other forms of support.

In early 1995, a consortia of eight large Russian banks came up with an initiative to provide the federal government with long-term loans in exchange for packages of enterprise stock held by the state. Those packages should have been given to the banks-creditors in trust. Such a deal seemed to be quite attractive for the government, since the 1995 state budget had to gain 9.3 trillion rubles as revenues from this so-called "monetary stage" of privatization, but prior to the implementation of loans-for-shares scheme only about 1.3 trillion rubles had been accumulated (Open Media Research Institute Daily Digest I, No. 1, 1996-01-02). So there were no reasons for surprise from the rumors that this "initiative" had been provoked by state officials themselves.

Extensive discussions were focusing on the following issues:

(i) Do banks really have enough resources to fulfill declared obligations concerning the loans? The banking crisis, that occurred in late August 1995, heated suspicion and uncertainty concerning the reliability and solvency of the banks. Later data that refers to the third quarter of 1995, indicates that the net value of bank assets decreased by 11% in comparison with the previous quarter, and growth of those assets occurred by only 2.6%, compared with a 15.5% increase during the second quarter. The number of commercial banks declined by 7.8% in the course of the first 11 months of 1995 (Open Media Research Institute Economic Digest, Vol. 2, 1996-01-04);

(ii) Will the operation planned be really helpful in creating efficient outsider holders of enterprise stock? Or would there not be serious impact on development of fruitful corporate governance?

For the moment these questions remain open. The process started quite recently, in September, 1995. Nevertheless, state packages of shares of selected largest companies were actively realized (given in trust) through competitive biddings (tenders). Among those companies were LUKOIL, YUKOS, Nafta-Moskva (all — oil companies), and Svyazinvest (telecommunication company). Twelve governmentally organized loans-for-shares auctions took place, through which some 4.7 trillion rubles (1.01 billion USD) were generated (Open Media Research Institute Daily Digest I, No. 1, 1996-01-02). This is 78.3% of the total amount, gained by the government from "the monetary stage of privatization" (6 trillion rubles), and 50.5% of planned revenue, fixed in the 1995 state budget.

Three main problems have become obvious in the course of this campaign:

(i) The level of demand and competition, accompanying the auctions, by now is rather low. Typically, not more than 2–3 bidders pretend to acquire share packages being offered. For example, at the auction, where shares of Yukos, the second largest of Russia's oil companies were tendered, only two rival bidders showed up (Open Media Research Institute Daily Digest I, No. 239, 1995-12-11). The same situation occurred at the auction, organized for the release of state-owned shares of LUKOIL, the largest oil producer (Open Media Research Institute Daily Digest I, No. 251, 1995-12-29). The main reasons are the lack of available and "interested" domestic capital, cautiousness of potential foreign investors and, last but not least, results of bidding considered to be predetermined due to obvious preferences, extended by the government to several selected banks (see more below).

(ii) As a consequence, share prices are relatively low as well. Experts claim, that offer prices in federal loans-for-shares auctions on average are more than 30% below the current market value for the shares of companies involved (Open Media Research Institute Economic Digest, No. 6,7 1995-12-13). Bidding itself often appears to be quite symbolic: the consortium of the LUKOIL company and the Imperial Bank won the bid, offering to the government USD35.1 million for a package of LUKOIL shares with the starting price of USD35 million (The Jamestown Foundation Broadcast, 8 December 1995, Monitor).

(iii) The government is dealing with a limited number of banks (about 2% of the total number), which looks as they are enjoying serious advantages. It is amazing, that the winners in the tenders are typically those bidders, who have affiliation with the banks, authorized to organize these very tenders. For example, Menatep bank acquired 78% of the YUKOS shares through an intermediary company Laguna. A 33% stake was purchased at the investment auction for USD150 million, guaranteed by Menatep, and a 45% stake in the loans-for-shares auction. USD159 million credit in the last case was guaranteed jointly by Menatep, Tokobank and Stolichnyi bank. The only rival bidder, admitted to the loans-for-shares auction, was Reagent, another company sponsored by this very bank. Menatep was also the organizer of the auction (on behalf of federal authorities). (Open Media Research Institute Daily Digest I, No. 239, 1995-12-11). Now Menatep has to invest USD350 million only in YUKOS (op. cit.), having a lot of other loan and investment obligations (Open Media Research Institute Daily Digest I, No. 231, 1995-11-29).

The indicated problems cause a lot of concern and, as already mentioned, leave the issue of efficiency of loans-for-shares schemes quite open at the moment.

3.4 Outsider Investors

There are three categories of outsider investors, which have different nature (origins) and demonstrate different intentions and activities from the standpoint of further privatization and impact on the enterprises.

3.4.1 Private companies

These (including sometimes former state enterprises) are most active in financial markets. They intentionally acquire shares in order to obtain either control or at least influence over enterprise deals. So their inclination to intervene in decision-making may be regarded as obvious. The surveys, conducted by the author, did not address this kind of shareholders specifically, but occasional information suggested that often private entities, intending to obtain real influence or control over a particular enterprise or group of enterprises, come up with quite substantial restructuring programs. The problem is, that there are still too few cases where outsiders manage to acquire either a controlling stock or at least a controlling position.

Actually, two kinds of enterprises have to be delimitated. First, companies, in the capital of which outsiders do not obtain controlling or sizable stake. So far, these form the majority of former state enterprises. The participation of private companies in the performance of such enterprises remains on average not significant. It would be strange to accuse them for precautions: what sense does it make to intervene with private money in the deals, that are not under control from the side of investors? Unless the patterns of control would not change due to either the enlargement of outsiders' stake, or to the emergence of any other forms of strengthening outsiders' decision-making and controlling power (let us say, the banks will inevitably put real sanctions against debtors that may bring them to bankruptcy and then eventually in the hands of outsiders), the activity of private investors will stay limited and even shrinking.

Second, enterprises, being owned and therefore controlled by outsiders. These are a minority so far, and owners demonstrate controversial behavior. In Bim's sample, only several companies were owned by outsiders, and in all of the observed cases the new owners implemented substantial restructuring projects based on funding brought in by themselves. Opposite examples are also not a revelation. Therefore, Gurkov's (1995) view on outsiders' characteristics makes a lot of sense. His conclusion is, that private companies are rather active in penetrating into the industrial sector (which probably reflects more 1994–1995 tendencies, than 1993–1994). At the same time, these eagerly expected core owners "act mostly as company raiders", preferring either to dissolve newly-owned enterprises immediately, or to use them as "cash cows" for their own current needs. The lack of strategic agenda in relation to outsiders is seriously stressed by this author, as well as by Earle, Estrin and Leshchenko (1995).

3.4.2 Voucher investment funds ("CHIFs")

These funds were established mainly by banks and other financial structures on the eve of privatization and were supposed to serve as intermediaries in vouchers' ("privatization checks") and shares' circulation. As Estrin (1994) and Frydman and Rapaczynski (1994) point out, such intermediaries were suggested especially in order to confront and overcome the wide diffusion of property rights, materialized in initial privatization certificates (vouchers). Following this logic, these funds had to play the role of major corporate outsider owners. These intentions certainly caused opposition towards intermediary institutions from the side of enterprise managers, and as a reflection legal restrictions were set up, according to which voucher funds were not permitted to possess more than 10% of the stock of a particular enterprise.

As a result "CHIFs" have appeared to be one of the "modest" and inefficient stockholders. In Bim's sample (if referring to 1994), in 21% of the enterprises "CHIFs" were holding 10–12% of the shares (later on the above mentioned restrictions were waived), in 23% of the companies — 5–10% of the shares. Pistor (1994), indicates that the average stake held by a voucher fund in her sample (148 of the total of 516 of these funds in Russia) was about 7.6%. Few exceptions known from the media and other sources only confirm the rule, as usual. Moreover, after gaining huge profits on voucher speculations, voucher funds had tried to extrapolate the same "speculative strategy" on their deals with enterprise shares. So their interests were manifested mainly in the area of financial markets as such with no particular focus on enterprise control, management and/or restructuring. Many of these investors have become insolvent and eventually gone bankrupt; some have been transformed into conventional financial markets' players.

3.4.3 "Physical persons"

There are reasons to subdivide physical persons-outsiders into two groups. The first group is not very large and consists of "free riders", who acquire quite small packages of enterprise shares in order to get dividends and/or to speculate in the markets. This group is not interested in enterprise performance and perspectives at all (i.e., interests are limited by the current sights of getting dividends). The second group is more exciting. It consists of people, who formally have nothing to do with the enterprises in question (in the sense that they are not employees), but at the same time are in close contact with: (i) either top managers or managerial coalitions, which control the enterprise or are seeking complete control; (ii) or private entities interested in the same. In both cases interests and strategies of this type of shareholders are strictly dependent on the strategies of their shadow seniors.

Pistor's (1994) observation, that most of the trading of stocks (88.6%) takes place off the official markets helps to imagine, how such peculiar shareholders appear on the scene (or better, act behind the scene). It also shows that enterprise managers are in fact controlling not only enterprises as such, but outside share circulation (i.e., financial markets) as well.

4 Ownership and Control: Reflection of Late Soviet Stereotypes or Move to Corporate Governance?

The fact that ownership and control cannot coincide to a complete extent had been well known and broadly discussed in Western literature far earlier than privatization in Eastern Europe appeared on the agenda. Therefore, the issue that privatization procedures should have been aimed at the creation of efficient corporate governance system, which would be able to provide more or less appropriate control by owners over managers and assure positive motivations of the latter, was challenged often on the eve of privatization in transition economies. See, for example, Estrin (1994), Frydman and Rapaczynski (1994).

4.1 Control versus Ownership: Russian Peculiarities

This problem has to be considered as particularly important for Russia. The point is, that the former administrative system eventually produced and fixed extremely untransparent and unclear relations of management and decision-making concerning so-called public property. Enterprises and other entities, having been proclaimed as public or even "nation-wide", were never really treated as such by the ruling bureaucracy. Moreover, within bureaucracy, delimitation of rights and functions used to be quite vague and uncertain. Existing hierarchies relied extensively on both formal and informal relations between officials (Joskow and Schmalensee, 1995). Although legal and administrative procedures existed, that were supposed to balance public, regional, local and individual interests, in fact the bulk of power was concentrated in the upper levels of state and communist party hierarchy. Major issues of enterprise performance, such as profile and production mix, main suppliers and customers, rules of income distribution and capitalization, price and wages regulations, etc., were strictly predetermined by the central governmental bodies.

At the same time, the center was seriously dependent on the enterprise administration in the process of working out plans and regulations and in the course of fulfilling plans as well. In the first case, information from below was necessary, in the second, certain efforts were inevitable "beyond the regulations" in order to meet usually not very realistic tasks. Given the scale of the economy and size of the country, the center was doomed to relying on managers from lower levels, first of all — enterprise executives. The latter not only enjoyed a lot of privileges, granted to Soviet *nomenklatura*, but also created a complicated system of levers for the reinforcement of their real (both formal and informal) positions in decision-making. One of the most common levers was multiphasic bargaining for lower plans in return for higher supplies (see for description Bim (1989) and Naishul' (1991).

It is necessary to mention that some pseudo-democratic procedures used to be a part of the Soviet planning. General meetings of "working collectives" for the endorsement of different "counter plans" as well as innovative initiatives (very often — after prior approval of such "initiatives" by the upper levels), local trade unions committees, "recommending" on wages and social benefits, were quite common in this really whimsical system of management and decision-making. So many employees recognized such procedures as meetings of the shareholders as similar kinds of *pro forma* well known from the past.

It makes sense to stress, that in all these artificial mechanisms of management enterprise directors played a key role. In the course of the 70s they became quite qualified in pursuing decisions (or, what was the same, drafts and proposals for decisions of the upper levels), clearly identified with their own interests. Under those circumstances, however, the interests of managers could not be separated too much from those of the enterprises. The further promotion of managers and their material wealth used to be dependent on success (which was actually also a subject for definition! — A.B.) of enterprise performance. The easiest and most common way to achieve higher results was certainly to diminish the goals as well as real production capacities. So both managers' and enterprises' interests were aimed at making life easier — fulfilling lower plans with larger centrally allocated resources.

The challenging feature of "communist management" was the following: depending on the concrete situation, both upper bureaucracy and enterprise employees could be successfully misled by managers. Employees were completely under the influence of enterprise executives.

These facts from the past are mentioned in this far from historical paper in order to arrive at the following: privatization procedures, as they were built up and implemented in Russia, could not rapidly change the psychology, mental outlook and behavioral habits of enterprise insiders. This means that the ruling, superior position of enterprise managers appeared to be *a priori* given obstacle for any sufficient corporate governance at the Russian formerly state enterprises.

Hence, in all cases of the acquisition of the major part of enterprise stock by insiders, the full control over the enterprises certainly belongs to managers, and more concretely, to general directors. That explains a gap between the formal assignment of shares and the real control exercised by the shareholders. Real control is in the hands of managers.

The aforementioned statements are hardly new to experts dealing with economies of the Soviet and post-Soviet type. They are articulated here, because sometimes analysts do not question the adequateness of the real process of control and governance to formal ownership structure. Russian privatized enterprises can be certainly classified according to the structure of shareholdings. But in our view, there is no straight dependence until now between the surface of a picture (structure of shareholdings within insider ownership) and the substance, i.e., shape of real power or control. In-depth interviews clearly show, that even if the majority of enterprise stock is in the hands of non-managerial employees, managers are the only real controlling party. Other insiders simply do not have enough access to working out, considering, formulating, approving and implementing decisions if this is not done through managers. But if it is so, the latter certainly have all the opportunities to pursue those policies, which they themselves evaluate as appropriate, despite "the formalities" of ownership structure.

These statements are completely consistent with some conclusions of Earle, Estrin and Leshchenko (1995); for example with their statement that the balance of advantage between managerially-owned and worker-owned firms in terms of influence on enterprise behavior is unclear. Our explanation is that both types of companies are controlled by managers and, therefore, do not show many differences in performance. The same reason interprets another conclusion of these authors, that the effects of "worker ownership" on behavior and restructuring are not yet as disastrous as predicted.

There are even reasons to argue, that when employees reach the top of their influence on the enterprise deals and change (re-elect) the general directors at the general meetings of shareholders, they do not end up with establishing any real control over newly elected directors. In 18% of the surveyed enterprises late directors did not receive their mandates for the next term during 1993–1994. Both employees and new directors claimed, that the former managers were dismissed due to the lack of competence, mismanagement, etc. But then 92% of the employees emphasized that the new directors did not introduce any radical changes, relevant to the reasons of the dismissal of former leaders, and were not more responsible to workers than the previous ones. 88% of newly elected directors reported that they do not find any sense or possibility to manage the enterprises meeting those demands of the collectives, for ignoring which the former leaders became fired. The situation described certainly may reflect the fact, that some general directors are actually dismissed not due to mismanagement in a common sense, but either because of causes being quite beyond their influence, or because of internal conflicts they did not succeed to ward off or overcome.

The above mentioned statements do not mean that things are more straightforward than they really are. Employees certainly have some influence on management. The variety of precise circumstances force enterprise executives to consider workers' reactions on forthcoming decisions or foreseeable events. Such considerations may be dependent also on the ownership structure, among other factors. Interviews definitely prove that directors prefer to act in order to eliminate or unblock potential or actual conflicts much more than to provoke them. But this kind of indirect influence, which is actually not too strong, differs from that which might be a direct one, predetermined by the active role of holders of a major part of enterprise stock. Such role could be played only in the case of self-identification of employees as proprietors, on the basis of their vested interests, well-targeted strategies and perfect organization. That would mean real impact of privatization on decision-making and management.

4.2 Managerialism in Russia: Key Features and Key Problems

Directors are certainly thinking about making their actual control over enterprises more solid and prolonged. That it is why they are working on the transformation of control, based on traditions and administrative advantages, into control, based on adequate ownership structure. So there are reasons to emphasize, that **the substance of a running process from the side of managers is not gaining control due to the sizable stake of property acquired, but to acquire a sizable property stake in order to keep and strengthen the control already achieved and exercised.** This is a serious difference between the position of managers and that of outsiders. Control serves as a precondition for ownership, not vice versa. And ownership is still not necessarily a precondition for control.

87% of the directors, 73% (1993) and 77% (1994) of other managers reported that they have had definite interest in the further acquisition of enterprise stock. This is not a surprise, given the evidence of the concentration of shares in their hands (see the first section). It might sound interesting, that there are two ways of that concentration: an "open" and a "hidden" — a very typical Russian combination. The "open" way includes the following activities: (i) implementation of differential conditions for closed subscription for shares under the second privatization option, which provided preferential opportunities for managers. This mechanism has been used by 25% of the surveyed enterprises; (ii) intensive buy-out of shares at the first voucher and monetary auctions. Prior mobilization of vouchers and funds was necessary for that; it had been successfully completed by top managers on the basis of their personal benefits, gained from the phases of initial liberalization of the Soviet economy (1988–1991) and well known *spontaneous* or *nomenklatura* privatization (in more or less the same period); (iii) even more intensive buy-out of shares in the secondary market — primarily from the voucher funds, as well as from the employees-shareholders. The latter are commonly forced to sell out shares within the working collective, i.e., to managers, even in cases of open joint stock companies, where such order is not predetermined legally as an exclusive one.

The "hidden" way, used by directors or managers' coalitions, implies : (i) mobilization of existing satellite private structures (see section 2.1.) or creation of new ones, especially for the concentration of shares according to guidelines of enterprise executives; (ii) orientation of private persons formally having no relations with the enterprise, but having those with its leadership, on purchasing shares in the auctions and secondary market.

Not only the "hidden", but also the "open" ways described, were certainly not eagerly revealed by managers in the course of the interviews. It does not seem possible to present any more or less reliable quantities, characterizing scale of these operations. But quite reliable information can be extracted by analyzing the Registers of shareholders. Many curiosities become obvious if one examines those (not to mention that their availability not only for strangers, but also for "ordinary" shareholders themselves is usually in question, and our sample was not an exception in most of the cases). For example, in 67% of the surveyed joint-stock companies, the list of outside stockholders consisted up to 10–22% of legal entities, which were registered at the same mailing addresses as the basic enterprises. Could better proof be found, that those entities were nothing else but satellite structures under the control of enterprise leadership? Moreover, in 58% of the surveyed enterprises among physical persons-outsiders percentage of people, identified in the Registers by the same family names as those of enterprise top executives, varied from 3 to 19%.

There are no reasons to argue that aggressiveness of managers as new owners is in all cases dangerous. There were many claims in professional literature and in the media that managers will necessarily demonstrate old-style stereotypes as lacking competence, conservatism, rent-seeking from the state, excessive care of employees, and so forth. To a certain extent it has obviously appeared to be true. But at the same time, rather many managers have performed in a very flexible and pro-reformist way, and the speed of their adaptation to the new environment has been really amazing. Under such leadership dozens, if not hundreds, of Russian enterprises are already recovering. At some point many directors adapted too rapidly and too radically, given their intentions of clear separation of their individual business interests from those of enterprises for which they were in charge.

We tried "to measure" business qualities of enterprise directors, analyzing their behavior in the spheres of production, marketing, investments and restructuring, financial policy, labor policy, and privatization. It is necessary to stress, that not only facts of enterprise performance were taken into account, but those facts in connection with directors' activities. This way was chosen due to the obvious assumption that success stories and enterprise performance in general are dependent both on subjective factors, such as directors' policies, and (sometimes much more) on objective factors (sectoral allocation, technological level achieved, etc.) and, let us say, external conditions (regional allocation, remoteness from sources of energy and transport).

33% of the directors in 1993 and 38% in 1994 could be considered quite competent and efficient: they managed to maintain a more or less stable financial status of enterprises; sufficient changes in production mix were timely introduced; destructive social conflicts were avoided; and purposeful privatization policy, including admission of outside investors, was pursued.

25% of the directors in 1993 and 27% in 1994 could be evaluated as more or less corresponding to pro-reformist demands: they achieved an acceptable level of current functioning, first of all due to efficient commercial policy, including judicious price formation and flexibility towards suppliers and consumers; restructuring was going on, but without the introduction of all the potentially possible levers and sources; moderate paternalism used to be practiced; privatization was going ahead, but purposefulness and a strategic approach were lacking.

Finally, 42% of the enterprise executives in 1993 and 35% of those in 1994 seemed to be unable to lead their companies to recovery and market adaptation: the financial status was continuously critical; almost no restructuring took place, also in a sense of changes in the output structure; stock was spontaneously diffusing without any evidence of goals from the side of enterprise management.

So from the point of current activities, there are probably not so many reasons to dream about immediate removal of directors–old-timers.

Szelenyi, Eyal and Townsley (1995) consider, that the dominant ideology of **managerialism** is monetarism — "if for the new New Class, what Marxism-Leninism, or scientific socialism was for the old New Class". If it is supposed by the authors that monetarism is a goal or strategy of making money, this is certainly true. Then it is questionable, however, whether scientific socialism was really the practical ideology in the past, because people were concerned about making money under communism as well. But if monetarism should be interpreted in a more classical sense (hard financial constraints, minimal interference of the state in the enterprise performance, managerial behavior meeting these conditions adequately), then our surveys do not confirm this observation, although it may sound very attractive for liberals. It remains a question, if even outside the industrial sector, within the segments of economy, occupied by newly created private entities, this statement is true. Concerning managers of former state and now privatized enterprises, they are rather homogeneous as a whole; despite some differences, they seem to be followers of only one ideology — pragmatism. Identification of their personal interests and thorough following of those interests in practical life form the background of their behavior.

Basically, those directors, who do not meet "the demands of time", eventually go. According to some estimations, that are worth verifying, 20–30% of the general directors achieved their current positions in 1992–1995.[12] What is really crucial, refers more to their status as proprietors. As such they typically demonstrate a strong unwillingness to share their control over enterprises with any outsiders, who are not under their control themselves. This is characteristical to this "social corporation", and **very often the more progressive and efficient particular directors are in current performance, the less they are committed to any losses of control**. It seems a bit too optimistic to suggest, that if enterprise shares are mainly bought by managers, there are no reasons for the latter not to behave in the interests of other outsiders (Sutela, 1995). Such reasons exist and are rooted partly in psychology, partly in the above mentioned possibilities for the directors to benefit more through unfair all-embracing control than through civilized corporate governance.

At least two problems arise here. First, as is well known both from theory and practice of corporate governance, lack of outside control is quite bad by definition. Economic agents are unlikely to work efficiently in the long run, being governed in authoritarian style, i.e., without the influence of concerned and responsible proprietors on administrators. Second and most important: in the contemporary transition economies privatized property and mobile capital are separated and concentrated in different institutional forms. Property — in the industrial sector, mobile (or financial) capital — in the banks and other financial institutions. In order to achieve necessary industrial restructuring of enormous scale, it is inevitable to bring these two components of economic resources together. The challenge is, that this looks completely impossible if financial structures do not channel financial flows into the production sphere, and they will certainly not do it unless the current controllers are ready to exchange control for such inflows.

So more or less normal corporate governance becomes crucial not only because of inherent problems and goals of privatization. It becomes crucial due to the lack (if not to say, absence) of resources at the disposal of enterprises for substantial market adaptation

[12]It is interesting to mention, that new CEOs are typically recruited by those parties, which manage to obtain control over the enterprises and get rid of the former directors, from among the second-third persons of the "relative companies" (with the same profile, similar technology, etc.). "Pure strangers" are put into this position quite rarely. Following this strategy, the new owners, first, demonstrate their care about professional skills of the appointees. Another reason not to recruit general managers from outsiders is the unwillingness of the owners to enlarge the power of only one of themselves; this refers to the situations, in which outsider ownership and control rest in the hands of several proprietors (persons or parties).

and restructuring. That is why specific attention is paid by analysts and policy-makers to the current, monetary stage of privatization and to described loans-for-shares schemes, aimed at obtaining by the banks (through their subsidiaries) a sizable component of the enterprise stock. But in return banks are going to credit government, not enterprises. So direct monetary inflows to the latter, although envisioned in the course of this maneuver, may be regarded as questionable.[13] Time will show also, what this kind of trust (state-owned packages are supposed to be given to the banks in trust) means for both corporate governance and the further destiny of stock — which banks probably would intend to sell further on in order not only to have their money, lend to the government, back, but to end up with a good surplus.

4.3 Coalitions of Managers and Privatization. Erosion of the Former Basic Social Contract

Surveys done by the author, clearly demonstrated evidence of wide-spread in-enterprise managerial coalitions (Bim, 1994a), efficiently created and functioning in order to exercise control over current enterprise activities and benefit from them even if particular enterprises are in deep and continuous financial difficulties. This is the best proof that patterns of control do not necessarily depend either on ownership structure or, what may seem even more surprising, on the financial status of the enterprises. Such in-house managers' coalitions are used very broadly for the successful acquisition of shares and, hence, for privatization of enterprises not only *de facto*, but also *de jure* in favor of general directors and their allies.

Gurkov's (1995) assumption is that coalitions (he calls them "alliances") are usually created by those directors, who lack the financial and organizational means to acquire shares immediately themselves. Our observations are a bit different: coalitions are initiated by directors almost in all cases, irrespective of their possibilities to build up a single-person ownership. There are at least three reasons for that: (i) directors make other managers more interested in proper enterprise performance and more responsible for the results. There are almost no real possibilities to exercise efficient administrative control, for which the formal rights of directors is only one of the necessary preconditions, so the issue of economic incentives sounds quite crucial; (ii) by involving managers into in-house coalitions, directors try to avoid attractiveness for them of other alliances, first of all of alliance with aggressive outsiders; (iii) managerial coalitions make all the managers feel themselves to be "natural partners" of directors in all cases of potential and real confrontations within the working collectives. The importance of the last two points may be confirmed by the fact, that in all the known cases of overthrowing the enterprise directors, the latter somehow lost support from the side of middle-level management.

[13] In most cases, direct monetary inflows are envisioned. In our view, it is still questionable, whether or not they will occur in reality. There are already examples, that investors postpone financing, which used to be a condition under competitive bidding, after obtaining a desirable block of shares.

It seems appropriate to mention here, that managers' coalitions are completely different from the well-known and much less formal **social contracts** between managers and employees, typical to the Soviet era. Peck (1995) supposes, that there are coalitions between managers and the workers' collectives, which the present pattern of enterprise control is still based upon. Not arguing against certain obvious commonalities in interests of all insiders, we defend a completely different approach. Due to the disappearance of all-covering state control (late 80s — early 90s) and privatization (1992–1995) in Russia, differences in the interests of "positionally strong insiders" (managers) and "positionally weak insiders" (workers or other employees) have become much more significant than their commonalities. That is why **contemporary managers' coalitions have nothing to do with the unification of those groups of insiders**. To the contrary, they reflect contradictions in interests and patterns of behavior of former social partners, now almost antagonists. Uvalic (1995), on the basis of analysis of privatization in the countries of Eastern and Central Europe, also points out that it is necessary to distinguish managers and employees as quite different categories of insiders.

One issue has to be especially examined in the context of erosion of the former basic social contract between managers and employees. Dolgopiatova (1994) and many others emphasize, that managers typically feel certain obligations concerning employees, originated in habitual values of the communist past. These obligations refer, first of all, to "safekeeping of the working collective" (refraining from firing employees due to economic necessities) and maintaining a more or less appropriate (socially acceptable) salary level. Dolgopiatova points out, that in her sample among the main goals of enterprises, as seen by general directors, 58% of the latter put in the first place "safekeeping of the working collective".

Bim's sample, however, suggested different observations. Only 33% of the directors reported that they would give priority to the above mentioned goals; 20.8% did not mention social problems by their own initiative at all and, answering precise questions, explicitly underlined that they would not consider these problems, first of all preservation of employment, to be important goals for enterprises in transition.

In-depth interviews demonstrate, that a pragmatic approach in the attitude of managers towards employees is much more prevailing than emotional or ideological ones. Directors would prefer to avoid any more or less large-scale conflicts — that is the criteria they really follow, which has nothing to do with any curtsies towards values, moral obligations, etc. Most of the concrete solutions are made on the basis of a pure pragmatic approach.

With respect to wages, managers try to maintain a certain salary level, compatible with the in-regional standards. First of all, this level follows the inflation and, typically, is almost not connected with particular labor achievements and with economic reasons relevant to the enterprise as a whole. Dolgopiatova (1994) mentions, that wages have been transformed into an "independent component" of production costs. In many cases salary increases eat up a substantial portion of cumulative enterprise earnings. At the same time, a majority of directors channel some current resources for purchasing new equipment, i.e., for a kind of renovation and even restructuring (changing of production mix). In Bim's sample, about 18% of the directors in 1993 and 27% of those in 1994 reported buying equipment for production purposes.

As far as employment is concerned, estimations according to International Labor Organization criteria, show that 6 million Russians — 8.2% of the potentially working population — are unemployed (Open Media Research Institute Economic Digest, No. 8, 1996-01-03). Hidden unemployment (people are kept affiliated with the job, but in reality not working regularly or full time due to the lack of resources, necessary for reproduction) covers much more people. So it is obvious that personnel, in fact, is cut, despite any declarations, but in order to keep people quiet and to save some labor reserve for potential (in many cases — wishable) "production boom", personnel reductions are adjusted and moderate.

The conclusion is, that managers' declarations concerning their "social orientations" should not be taken too seriously. Real facts suggest the pragmatic approach is followed much more often.

Coalitions of the revealed type do not leave any room for non-managerial employees to withstand the dictatorship of managers in governance and their expansion in privatization. There is simply nobody who could organize and lead any resistance. Directors confirmed, that they attentively follow the situation and either expel dissatisfied employees, or involve them in coalitions with all the consequences concerning benefits in general and privatization advantages in particular.

Gurkov (1995) and Gurkov and Maital (1995) underline, that the role of middle-level managers has become, in their own view, considerably less important in the process of decision-making. This shows that these managers actually have accepted a subordinate role in the coalitions offered by top managers. We have monitored quite a few cases, where middle-level managers responded differently, evaluating their influence as much higher than it used to be before. It may easily be so. Inherently predetermined monocentric decision-making (for example, until now everything might have become operational at the enterprises only through written orders, signed by the general directors personally), allows the enlargement of competence of the lower levels. But with one quite necessary precondition: such enlargement can be legally and technically achieved only on the grounds of acceptance by a general director, who is **granting** new functions and rights to the enterprise employees, subordinated to him. So the exceptions that we have observed, sound unarguable in a context of delegation of competence from the top of managerial vertical to its bottom. But it does not mean any aggravation of the self-contained role of middle-level managers in a framework of privatization, corporate governance and enterprise control.

Top management and, first of all general directors (chief executive officers), of enterprises play a dominant role in the coalitions not spontaneously, but quite consciously. The findings of Blasi (1994) confirm, that the design of coalitions themselves is a subject for thorough consideration of the general directors. On his question about desirable distribution of insider ownership in future "optimal" ownership structure, CEOs responded, that within 40% of the stock, they would prefer to be allocated to top management, 31% should be posessed by themselves and 9% — by other top managers. In addition, 17% of the stock should be given to other (lower-ranked) managers.

Besides the aforementioned in-house coalitions, there appear to exist two more of a traditional type and decreasing influence. First, the coalition of managers, dealing with technologically and economically related enterpises of former branches or sub-branches (sectors or sub-sectors) of the economy. Second, the coalition of those managers, who are governing technologically and/or formerly organizationally integrated enerprises within regions. Such coalitions are typically not forming for privatization needs: they embody quite different forms of managerial cooperation, beginning with searching for suppliers and customers and finishing with lobbying in political circles and seeking investors. Our observation is, that most of the directors currently do not need these forms of "mild integration" too much and gradually give up membership in them.

Dolgopiatova (1994) describes in detail existing vertical and horizontal associations ("objedineniya"), which may serve as examples of coalitions of a traditional type. According to her data, in the fall of 1993 43% of the enterprises reported their unwillingness to join associations, 40% of privatized enterprises ceased to be members in any of them. Ickes, Ryterman and Tenev (1995) thoroughly explore the influence of membership in such associations on enterprise restructuring.

Another type of external (or outside) coalition deserves serious further attention. These coalitions are emerging on the basis of mutual exchange and penetration of stocks between technologically and/or economically related companies. This process is organized by interested directors. Surveys produce many examples of directors trying to manage the dissemination of shares not only inside, but also outside the working collectives. In 1993 they were most active with such initiatives, because during that very year outside circulation of shares was broadly launched by voucher and first monetary auctions. Therefore, initial affiliation of large outside blocks could, to a certain extent, determine further development of privatization and control over the enterprises. In Bim's sample, 62.5% of the directors reported implementing purposeful policies in order to attract suitable outsiders by providing the latter with information about envisioned auctions and, what is even more expressive, by propaganda (so to say, very active advertising) of their companies as perfect objects for capital intervention.

In most cases coalitions of this type were organized certainly in order to prevent intervention of unexpected and "dangerous" outsiders. **In other words, "loyal outsiders" were created on the initiative of directors.** There were three typical paths for this process: "loyal outsiders" were selected (i) among more or less stable and reliable suppliers and consumers; (ii) within the economic sector, to which the enterprise-initiator itself belonged; (iii) by mutually advantageous agreements with new private (originally private, not privatized) investment institutions. In the first case, directors considered that they had surrounded themselves with commercial partners, who should be naturally interested in the stable functioning of their company. In the second case, experience and well established connections within former industrial branches or associations of a traditional type were intended to be exploited. The third path promised certain financial support. But the main, usual goal was to prevent stocks from being spontaneously circulated in the financial markets without the control and influence of managers.

Coalitions of this sort (contrary to the above mentioned traditional associations) can be assessed as the product of the privatization process and indicate the emergence of a significant stage of it, theoretically able to break (to change) the existing enterprise structures and boundaries and to lead to the formation of new market entities. But for this purpose the incentives of directors have to change quite a bit: they have to move from safe-guarding, protective aspirations to active entrepreneural motivations, implying interests in stock concentration and expansion of ownership and control not only inside, but primarily outside their basic companies. This was not the case in 1993–1995. So for now coalitions described are used much more not for the development of new market institutions, but to the contrary, for the conservation of old structures, i.e., for the purpose they were originally invented.

4.4 Outsiders as Actual and Potential Core Owners

When discussing the issues of corporate governance, it probably makes sense to mention, that while obtaining a major or controlling stake of the capital, outsiders do not necessarily demonstrate the expected inclinations to invest largely and to improve the enterprise performance immediately. Their practices of control over managers are often quite controversial. We have already cited Gurkov (1995) on this point (section 2.4.); a more milder conclusion of the same sort is suggested by Earle, Estrin and Leshchenko (1995). So a certain contradiction between theory (or expectations) and reality is taking place.

The reasons for the likely inefficiency of outsider ownership in Russia are to a great extent rooted in the nature of rather many outsiders.[14] This time we do not mean CHIFs or individuals, but domestic and even foreign banks, investment companies and whatever. Some of them perform quite normally, some — with serious deviations and perversions. It is beyond our goals to explore this subject now, and the evidence is limited by only a few examples of outsider ownership, but certain considerations and forecasts (if not to say alarms) sound rather urgent.

Many of the domestic investors originated in the Soviet or post-Soviet shadow economy and almost all of them have been functioning during recent years under the influence of hidden "mafiosi" structures. This causes a lot of contamination to behavioral stereo-

[14] Such reasons as political uncertainty and *mafiosnost*, pure economic considerations concerning excessive taxes, lack of legal basis for profit sharing, enormous transportation costs, etc., matter certainly as well.

types and business habits of new and relatively new private structures (even if they are only partly contaminated yet). Foreign investors, who are active in Russia, very often represent not the best Western companies. Along with good names there are a lot of marginal companies, sometimes based on activities of former exiles, sometimes — on partial repatriation of illegally exported or not properly returned domestic capital.

Hypothetical reservations about outsiders (as well as much more obvious facts and statements concerning insiders) should not be taken into account for straightforward revisions of current privatization activities, nor for any forms of illegal and dishonest restitution in cases already done. There are no reasons for attempts to diminish the necessity of corporate governance as a mechanism for establishing and maintaining satisfactory relations between proprietors and managers as well. **The point is, however, that the destiny of the enterprise performance in Russia for the time being is probably not synonymously predetermined by the prevalence of insider or outsider ownership and control. In the short run, most likely it will be dependent on the shape and intentions of concrete actors — insiders and outsiders — dealing with particular enterprises in the course of privatization and post-privatization.** Perotti (1994) seems to be quite realistic, suggesting that the role of individuals, running and controlling enterprises, will continue to be quite high. Current Russian realities require some clarification: the role of individuals will be high regardless of their being either managers or outsiders. That means, *inter alia*, the necessity to take into account a variety of multiple and controversial components, that determine and influence individual behavior and are much beyond schemes and factors of privatization as such.[15]

4.5 Challenging Issues of Corporate Governance in Question

The concrete situation in Russia makes theoretical discussions concerning different variants for efficient corporate governance almost senseless (see, for example, Perotti (1994) for a summary of those variants). Alternatives like financial intermediaries vs. banks or capital markets vs. specially created "holding companies as privatization agencies" (op. cit.) are not precise enough. Assuming that somehow industrial capital will become available for penetration by monetary inflows from the financial sector (what is not obvious at the moment at all), the key very pragmatic issue is, what actual and potential economic actors do have enough interest and resources for essential intervention into the industrial sector? How much are they ready to invest in order to obtain control over the former state capital, a good part of which is so far without a core owner?

[15]The fact, that transition in Russia, CIS and Eastern Europe is of a systemic nature is not completely understood yet, so to say, on the instrumental level. The systemic approach is not realized practically, while concrete economic issues are analyzed. Privatization is one of those issues, that badly need, along with analysis of economic factors, consideration of the psychological, cultural and social aspects of transition.

Not pretending to suggest any immediate scenarios, referring to the evident situation only, it is possible to argue that for the time being only banks, despite the above mentioned complications, appear to be appropriate players in this game. Capital markets as such may sound promising in particular cases, but cannot play an important role in general due to the obvious lack of appropriate financial potential of too many participants. Doubts and uncertainty about financial markets were expressed by Perotti (1994) and Peck (1995). At the same time, as mentioned in section 2.3., it is by far not clear whether an alliance of banks and enterprises is really going to end up with positive economic and institutional changes of a large scale.

Another no less pragmatic challenge for corporate governance is, under what circumstances enterprise managers would be ready to exchange control over companies (or at least part of it) for badly needed financial inflows? In other words, what kind and strength of pressure from the market or from the state do they need to give up "opportunistic behavior" and act rationally from the position of enterprise interests?

5 Policy Implications

There is no question, that problems indicated can be — and, therefore, have to be — solved only on the way of further progress of privatization, on the way of making it more deep and consistent. Any attempts to reverse the results already achieved and turn the process back would worsen the situation, not improve it. Based on this strong belief, suggested policy recommendations are in line with the continuation and strengthening of privatization policy.

A debate still takes place about whether state regulations are important for strengthening the Russian privatization process. Some experts claim, that the market will finalize this job and no interference from the state is necessary. Others are arguing for serious state intervention primarily in order to "correct mistakes" of the previous stages of privatization and then continue to regulate the process further, taking into account "state and public interests". It seems that both extremes, as usual, do not represent a rational, pragmatic approach or a realistic one. The second approach presupposes much more cancellation than continuation of privatization. But the first approach has another sort of limitation: if the state remains indifferent towards the obvious shortcomings, which are typical to privatization and post-privatization nowadays, changes in ownership may easily remain formal and much less productive than they could be in principle. Szelenyi and others (1995) suggest a quite realistic statement that **managerialism** may not at all be a transitory phenomenon. They underline, that key actors of economy and politics have a vested interest to reproduce this phenomenon and there are signs that it begins to enter a growth trajectory.

Vagueness and uncertainty of the current Russian statehood do not promise much efficiency from state policy in this quite complicated area, since it is also the area of strong controversy of interests and lobbying powers. But in our view, at least, the right attempts ought to be made: something is better than nothing.

First, it is necessary to pursue the achievement of more or less efficient corporate governance. Given the fact that the majority of enterprises is under the control of managers, it means the necessity for the state to provide prevailing support for outsiders, despite the aforementioned controversy regarding their behavior. This implies political, legal and practical measures: any possibilities for satisfying managers in their attempts to get rid of outsider investors other than through well motivated court decisions should be legally prohibited and administratively (i.e., really) unattainable; access of outsiders to the enterprise capital has to be continued and enlarged by further selling the state shareholdings; macroeconomic policy should remain anti-inflational in order to, *inter alia*, prevent financial institutions from "making business" on inflation — this may heat their interest in industrial investment and sustain the profitability of the latter.

Second, serious measures have to be undertaken to avoid any possibilities for conservation of the enterprises, that have been in continuous recession and financial losses. Enterprise restructuring, both in macro- and microeconomic aspects, has to be reinforced in order to put an end to the inefficient allocation of resources and to give more room for the implementation of investors' strategies. This could be done through an active policy of bankruptcies. Unfortunately, early beliefs that the great majority of restructuring in Russia would take place without having to revert to bankruptcy, or assumptions that bankruptcies themselves may not be as important for Russia as their threat (for statements see: Enterprise Behavior and Privatization of the Large Enterprises in the Russian Federation, in Economic Transition and Integration Project, 1993), appeared to be unrealistic.

It is possible to say now, that the lack of bankruptcies has been one of the major reasons for the enormous scale of conservation of inefficient enterprises in Russia as well as for relatively low efficiency of privatization. The author would be happy to share the optimism of Joskow and Schmalensee (1995) concerning liquidation and bankruptcy of enterprises as part of industrial restructuring in Russia over the next few years, but there is no current evidence for this sort of forecast.

Until now only a few cases of bankruptcies can be indicated due to badly targeted and not instrumental state policy and the weakness of relevant market infrastructure. The Federal Bankruptcy Department of the Russian Federation admits, that only among the enterprises, partly owned by the state (in which the state posesses more than 25% of the charter capital) 7.75% or 2,314 were insolvent as of December 1, 1995. (Open Media Research Institute Economic Digest, No. 8, 1996-01-03). The introduction of really strong measures for bankruptcy intensification, including the development of efficient market (self-regulative) infrastructure for this process, seems to be critical.

6 Summary and Conclusions

Ownership structure of the Russian privatized enterprises is in the process of development. The major tendency is the steady differentiation of insider stock on the shareholdings of managers and those of non-managerial employees. Managers (first of all — general directors) concentrate more and more shares in their hands, willing to strengthen and enlarge their own *de facto* controlling power, based on historic circumstances and initially widely disseminated enterprise stock, by gradual obtaining major stakes in the enterprise capital. Currently a bulk of companies is under their complete managerial control, which is in the process of successful transformation into ownership control.

A fundamental fact has to be recognized, that so far formal allocation of shares (i.e., ownership structure) in the case of Russia does not coincide at all, on average, with the patterns of real control. If outsiders do not have more or less sizable stakes (the absence of which is still typical), despite formal proportions within the stake of insiders, control rests in the hands of the general directors. Therefore, conclusions concerning enterprise behavior could hardly be made on the basis of characteristics of the ownership structure.

In order to make the process of ownership concentration more consistent and irreversible, top managers create and strengthen in-enterprise managerial coalitions, which prevent spontaneous circulation of shares and undermine possible protests towards "unfairness" from the side of non-managerial employees. Managerial coalitions are a peculiar and significant feature of on-going concentration of enterprise stock in Russia. Besides in-house coalitions, managers have started to design the outside ones by pursuing the mutual penetration of stock of technologically related companies. Thus, preconditions for future changes of contemporary enterprise boundaries are emerging.

Enterprise executives attempt to regulate outside shares' circulation (i.e., financial markets) as well. For that purpose, satellite businesses, surrounding former state enteprises from the late 80s and being owned or controlled by managers, are used at large. This is one of the reasons why registered stock acquisition may be completely misleading from the standpoint of real ownership and control: stock of those satellites, which are formally outsiders, in fact supplements the managerial stock.

Three years of large-scale privatization in Russia permit some conclusions to be made concerning the characteristics of different types of shareholders. Most managers, as mentioned, intend to concentrate controlling stock in their own hands in order to exercise full control over companies. Nevertheless, there are differences in managerial behavior, and the latter refer not only to the speed of such acquisitions, which is certainly discernible. At least two managerial strategies have to be mentioned.

The first strategy is followed by those enterprise top executives, who identify their personal future success and financial wealth with the companies for which they are working. Therefore, privatization in their minds, has strong links with efficient market adaptation and restructuring. They privatize, ideally, in order to recover, continue and enlarge businesses for their own long-term stability and benefits. According to our observations, these managers are in the minority.

The second strategy is followed by managers, who, because of different objective and subjective reasons, do not identify their personal long-term interests and wealth with the company for which they are currently in charge. Hence, privatization is accompanied and followed by various forms of short-termism and even barbarism, aimed at as much acceleration as possible of income and capital extraction from the enterprise in favor of "opportunistic managers".

Both strategies have advantages and shortcomings — depending on from what standpoint it is viewed. The first strategy is advantageous for those who happen to be stockholders of a particular, potentially efficient enterprise and have the willingness, tolerance and skills to keep their stake. The second is probably not bad from macroeconomic and institutional points of view, since it means nothing more than an accelerated move towards inevitable bancruptcies and the following reallocation of resources, i.e., to badly needed structural changes. What seems challenging, is the fact that **a good number of enterprise executives are so far opposing their personal interests and interests of companies for which they are in charge**. This gap between privatization goals and the actual effect of privatization on managerial incentives and behavior (although it is resulting not only from privatization itself) may hamper the potential positive impact of privatization on enterprise performance and the nature of entrepreneurial interests at large.

Another important group of insiders — employees — does not demonstrate any positive impact of privatization on their incentives. The interest in dividends used to be the strongest among the interests referring to privatization, in particular during 1993. Due to the fact, that quite a few companies managed to provide dividends for shareholders and the latter appeared to be of a rather modest size, this interest became less articulated.

The fraction of shares of the Russian industrial enterprises that is owned or controlled by outsiders is still low, although there was a slight growth during 1994–1995. The problem is, that demand from the side of investors for industrial enterprise stock remains not too high — due to both lack of mobile resources within the financial sector, and prospects of Russian privatization and economic growth considered to be not clear enough. Another crucial obstacle is the unwillingness of managers to exchange control and ownership for monetary inflows, which in principle might be provided by interested outsiders.

Actual outsider owners demonstrate no less controversial incentives and behavior, than managers. In both groups there are positive and negative examples of governance, which proved to be typical and therefore may be extrapolated. Hence, the problem of perfect corporate governance does not seem to have synonymous solutions. Not disregarding the basic principle, that corporate governance predetermines control proprietors over managers, it makes sense to argue that **real characteristics and efficiency of enterprise performance under Russian transition are more dependent on personalities (individuals) in charge, than on what social and/or economic group they rep-**

resent. Following this statement, neither managers nor outsiders should be *a priori* praised or disqualified.

The state has to continue playing a role in regulating the institutional changes. Three major functions make a lot of sense and have to be activated. First, the state has to prevent — both legally and administratively — any attempts for restitution of the former state property, assuming that revisions of that sort have nothing to do with efficiency and fairness, but most likely reflect interests of losers in the previous privatization rounds. Second, the state has to pursue a well-targeted and instrumented policy of bankruptcies in order to prevent the conservation of enterprises, that are in continuous and irreversible losses. This might "open" enterprises for further privatization and substantial restructuring. Third, the state has to improve the process of privatization of state packages of the enterprise stock. Ideally, this process has to be transparent, competitive and free of any presupposed solutions. Whether the contemporary Russian state is able to meet these requirements and, therefore, provide positive impulses to further privatization, certainly remains an open issue. But this is definitely a subject for another study.

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