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# RUSSIAN INVESTMENTS IN LITHUANIA – POLITICS, BUSINESS, CORPORATE CULTURE

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## Contents

## Executive Summary

As in the 1990s relations between Lithuania and Russia had their ups and downs Lithuania tried hard to minimize its economic dependence on Russia. Ironically the closer Lithuania got to its foreign policy objectives of becoming NATO and EU member, the easier for Russian companies became to enter and operate in the Lithuanian market.

Being only the 7th biggest investor in the Lithuanian economy in 2004 quantitatively Russia's investment record is perhaps not impressive. However, as the Yukos controls the biggest GDP contributor and taxpayer in Lithuania, MDM Group owns the 4th biggest Lithuanian bank as well as the 5th biggest (in terms of sales volume) industrial producer, Lukoil has approximately 25% of the Lithuanian retail fuel market while Gazprom has stakes in the biggest gas distribution company, qualitatively Russia has increasingly significant role. These investments and investors are in the focus of the report.

Briefly reviewing the major sets of factors forming the contemporary Russian business culture one may conclude that serious problems of business ethics plague and continue to plague the way business is conducted in Russia. Consequently the internationalisation of Russian companies puts forward the question what exactly business cultural influence they spread when they internationalise? The report elaborates on three main areas of concern, namely, (1)the unbroken link/dependence of Russian companies on state, (2)the non-negative attitude towards bribing and corruption, and finally (3) the somehow neglected in Russia issues of raising efficiency and productivity.

In the report the mentioned above biggest Russian investments in Lithuania are checked against these main concerns and certain conclusions are made. While there is no evidence to slink Russian ownership with deteriorating efficiency and productivity in Russian controlled companies, the unbroken dependence of the Russian corporations from the Russian state and the readiness to use bribing, whenever an opportunity exists need certainly bigger attention. Based on its findings the report also makes some policy recommendations.

## Introduction

Immediately after the Baltic States gained their independence in 1991 they took the road of economic and political transition. A strong unifying factor driving the Baltic States politics and economics was the urge and the perception to drift away from their colossus neighbour Russia and to get closer to the West.

Such policies were not always balanced and certainly did not to help find the most optimal and practical relations with Russia but in the long run paid off in the form of full integration of the Baltic States to the West. Only 13 years later the three countries are members of both the North Atlantic Treaty Organisation /NATO/ and the European Union /EU/.

Russia also did not choose the best pattern of foreign policies. For quite some time it was trying to assert political and economic pressure that to a large extent misfired. First, such pressure served the Baltic States as a confirmation that their only course of action is to pursue even more vigorously for continuing integration with the West. Second, it was not only the Baltic States who suffered economically from the spoilt political relations as quite some time Russian investors were almost banned from freely operating and participating in the Baltic economies.

Lithuania is perhaps the country whose relations with Russia could be characterised as quite normal compared to those of Latvia or Estonia. Lithuania did not have a large Russian-speaking minority as in Latvia or Estonia. Still, the Lithuanians were quite cautious in building their new relations with Russia and constantly tried to prevent the active participation of Russian companies on the Lithuanian market.

Ironically enough the closer the Baltic States were getting to NATO and the EU, the easier it became for Russian companies to enter and operate in their markets. The more EU legislation and business practices were adopted by Lithuanian decision - makers in both political and economic matters the more Russian investors were enabled to participate in key areas of the Lithuanian economy.

Russian investments abroad are gaining momentum and the question of what exactly business ethics Russian corporations spread during their increased internationalisation is becoming more actual than ever. The Baltic States are natural area of Russian investment interest as they were part of the Russian empire and later the Soviet Union. During these eras intensive economic links were created and enhanced. Therefore the Baltic States represent an interesting environment for monitoring and observing what corporate culture Russian companies bring along when they invest and operate abroad.

In the focus of this report are the Russian investments in Lithuania and the corporate culture Russian companies radiate when they operate in this (new) EU market – business ethics, corporate governance, productivity, and efficiency. The study is divided in three parts. Part 1 provides a short background of the political and economic relations between Lithuania and Russia since Lithuania gained its independence. Part 2 focuses on the issue of foreign direct investments /FDI/ in Lithuania and analyses the Russian share of this process in both qualitative and quantitative aspects. The final part briefly states the main factors formulating the contemporary business culture and derives some important concerns that should be observed from a point of view of the country hosting Russian investments. At the end the four most prominent Russian investments in Lithuania are reviewed against the underlined concerns and conclusions are made.

# 1. Political and economic cooperation between Lithuania and Russia 1991 - 2004

## 1.1. Political relations between Russia and Lithuania

*Independence and initial Russian pressure*

As the Mikhail Gorbachev's "perestroika" decreased the oppression stemming from the Soviet totalitarian regime in 1988 in Lithuania nationalism drove the movement for independence and the beginning of the state building process. A national movement (Sajudis) was formed, which gained wide public support for its program of restoring an independent Lithuanian state and won the first democratic parliamentary elections in Lithuania.

Predictably Moscow inserted considerable political pressure on Lithuania that was accompanied by corresponding economic sanctions. When the Lithuanian Supreme Council refused to abide by the Soviet constitution, the President's decrees and resolutions of the Congress of People's Deputies, Moscow began an economic blockade against Lithuania (on April 18, 1990) by suspending deliveries of energy resources and raw materials to Lithuania. The shortage of raw materials led to the closing of some factories and there was an acute shortage of petroleum and other types of fuel and oil. In short, the Lithuanian economy began to falter (*Vitkus, 1996*). That was perhaps the strongest signal to the Lithuanian authorities that Lithuania must aim at gaining maximum economic independence from Russia *with an emphasis on independent energy supplies and policies*.

The victory of the Russian democrats after the unsuccessful coup of August 19-21, 1991 meant that the real political power moved in the hands of the Russian Government, which had already committed itself to respect Lithuania's independence. Starting at the end of 1991 Lithuanian-Russian relations began developing on a wholly new legal basis. Lithuania became an independent state *de facto* and *de jure* (*Bildt, 1994*).

At the end of 1991 in Lithuania and the other Baltic States there were still military troops. Under Russia's command; the economy of the new states was fully and completely integrated into the economic space of the former Soviet Union; in the Baltic States there were many people of Russian nationality (28,1% in Estonia (*CIA, 1998*), 29,6% in Latvia (*CIA, 2002*) and 8,7% in Lithuania (*CIA, 2001*)), who upon the dissolution of the Soviet Union suddenly found themselves living abroad.

Thus, the withdrawal of the Russian armed forces and the regulation of economic relations on a new basis became the main problems in Lithuanian-Russian relations. In Lithuania, alongside the growing political confrontation and re-grouping of political forces, an economic crisis was developing. Certainly, just like the 1990 economic blockade was not Prunskiene's fault, the blame for the deterioration of the Lithuanian economy in the summer of 1992 fell not only on Vagnorius government (*Vitkus, 1996*).

The end of the summer of 1993 and the withdrawal of the Russian troops marked the beginning of a new stage in Lithuanian-Russian relations. Both states were no longer burdened by the complicated problems of the troop withdrawal, the solution of which had required tireless efforts, so the tension about and fear of the breach of the withdrawal timetable receded.

*Russia's fears of NATO membership and the links to Kaliningrad*

The Lithuanian NATO membership was another issue that for some time looked to seriously overshadow the relations between Lithuania and Russia and which again put the economic pragmatism aside. While NATO became less of problem after the USA granted Russia increased non-member role in NATO, later the problem crystallized in the question how citizens, military personnel and equipment would travel between Russia and Kaliningrad. As the Baltic exclave of Kaliningrad is entirely surrounded by Lithuanian and Polish territory no visas were necessary for residents of the exclave who wished to travel to Russia proper. But the EU membership required on some form of visa regulation, saying that such measures are needed to control what could be a large flow of illegal immigrants into the EU territory.

Russian and European Union leaders finally agreed on travel rules for Russia's exclave of Kaliningrad, thus defusing a dispute that had been straining relations. The new travel rules are designed to make it easy for Russians in Kaliningrad to reach the rest of their country through the territory of future EU members Lithuania and Poland. But Lithuania has doubts. The agreement came into force in July 2004. It was a compromise deal under which Kaliningraders will be able to transit with so-called "facilitated travel documents" that will be easier and cheaper to obtain than regular visas (*EU Business, 2002*).

It must be mentioned that the most serious issue in the political dialogue (or dispute) between Russia and the Baltic countries was the treatment of Russian minorities in the Baltic States. However, Lithuania was in much better position to avoid such tensions, as the ethnical Russian minority in Lithuania is approximately 9% of the total population.

The intensity of the Lithuanian national movement, however, did not pose a serious threat to Lithuania's national minorities or to inter-ethnic relations, because the republic has already adopted significant guarantees of minority rights (*Resler, 1997*). Regarding its relations with Russia that put Lithuania in a favourite position related to the situation in Estonia and Latvia where huge amounts of Russians settled after the World War II.

### 1.2. Economic links between Lithuania and Russia

The economies of Lithuania and the other states that emerged in place of the Soviet Union were fully and completely integrated into the common economic space of the former Soviet Union. However, the huge Russian market, which in theory was able to absorb an enormous quantity of imports, in fact became inaccessible to Lithuanian producers. This could be accounted for not only by the newly created borders and other political problems, but also by the fact that Lithuania's economy was not reformed and it was unprepared to function on a new basis.

A major problem was the decay of the Soviet financial system: payments between economic subjects were disrupted; mutual indebtedness between suppliers and clients was colossal. Regardless of the general economic crisis, Russia was in a position to exert great influence on Lithuania's politics through economic means. The Lithuanian Government could not ignore the reality; it had to realise that it remained fully economically dependent on the supplies of key raw materials and energy resources from the former Soviet Union, and particularly from Russia. In July 1992, the Bank of Russia suspended payments to Lithuania because of the debts of the latter and reviewed conditions of bilateral economic co-operation (*Vitkus, 1996*).

This amounted to the abolishment of the status of most-favoured nation and meant that from now on Lithuania was to pay for Russia's goods in hard currency at world prices. In Lithuania, economic relations were becoming increasingly complicated and degenerating at a fast pace. This led to the disruption of the whole economic reform process and allowed the level of inflation to rise unrestrictedly (by the summer of 1992 it exceeded 2000%); the standard of living was dropping at a disastrous rate. As a result of such a critical situation and the abovementioned re-grouping of political forces within the Supreme Council, on July 14, 1992 a no-confidence vote was held concerning Vagnorius government (*Ibid.*).

On the background of the tensions around the timeframe of the troop withdrawal the autumn and winter of 1992 were an especially difficult period for Lithuania's economy, which was deteriorating even further. Russia was exerting indirect economic pressure by breaching agreements on supplies of energy resources and by closing its market. This inflicted big losses on Lithuania's economy and deeply affected the living conditions of the Lithuanian population. It was the Russian way to demonstrate that Lithuania should acknowledge its economic dependence on Russia.

Russia's refusal to grant Lithuania most-favoured-nation status further exacerbated the mistrust of Lithuanian politicians for the Russian attitude towards Lithuania. Ironically for Russia, the refusal actually helped Lithuanian companies to readjust themselves and find new markets in the West. According to the then Lithuanian ambassador in Moscow, Kozyrovicius, "the length of abnormal trade relations with Russia (double tariffs), which discriminated against Lithuanian goods, was even beneficial for some of our firms. It forced them to find a favourable market in the West. Almost 80% of all our foreign trade was with Russia, but during 1991-1993 when the trade agreement was inactive the level of trade fell to 29%. This would have been even lower if not for the necessity of importing raw energy materials (fuel, natural gas). The reorientation of Lithuanian business is well illustrated by the example of commerce. In 1993 78% of light commercial production was exported to the CIS. One year later this figure was reversed: 80% of light commercial goods were exported from Lithuania to the West (*Kozyrovicius, 1995*).

The concrete agreements on bilateral trade were signed in November 1993 and came into force in 1995. They gave Lithuania the status of the most favourite trading nation with Russia – a status that is still valid (*Miskinis, 2000*).

In 1997 the trade turnover between Lithuania and Russia amounted to almost 25 % of the total Lithuanian foreign trade turnover. In the second half of 1998, however, with the start of the crisis in Russia the bilateral trade turnover decreased to 19 % (*Ibid*.).

The rapid development of the Russian economy after mid 1999 favourably affected also the volume of Lithuanian exports and imports. Recovered export to the Russian markets was the main factor which conditioned a considerable increase in the total volume of Lithuanian exports during the first half of 2000 – by 26 %, compared to the same period in 1999, the imports increased by 10 % (*Ibid.*). In 2003 Lithuania's exports to current EU countries declined sharply from 48% to 42%. The most important trading partners were Switzerland (12%), Russia (19%) and Germany (10%). In imports, the EU's share grew slightly, up to 45%. Russia's (22%) and Germany's (16%) share is still dominant in Lithuania's imports (*BRE, 2004*).

Particular attention is paid to the issues of the economic, commercial and cultural cooperation with the neighbouring Russian region – the Kaliningrad Oblast. Poland, Germany and Lithuania have been the most important trading partners of the Kaliningrad region for many years and retained their positions as such in 2003 (*EMK, 2004*). As of the beginning of 2000 there were 304 joint enterprises with Lithuanian capital registered in the Kaliningrad Oblast. According to the number of joint enterprises in the Kaliningrad district, Lithuania ranks second after Poland (*Miskinis, 2000*).

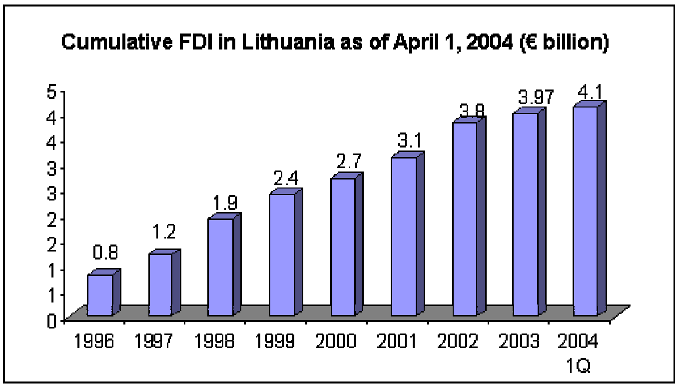
## 2. FDI in Lithuania and the Russian share

### 2.1. Foreign direct investments and investors in Lithuania

During the 1990s Lithuania was not the most popular FDI destination in Eastern and Central Europe. Still, by the end of 2003 as could be seen in Table 1 Lithuania has received some €4 billion of foreign direct investments /FDI/. The 1991-2003 cumulative FDI on per capita basis was $1169 that is almost 3,5 times less than in the Czech republic but it is still considerably higher than in countries such as Bulgaria, Romania or Russia (*IMF, 2004*). Among the main reasons why foreign companies decide to invest in Lithuania are inexpensive and skilled work force, potentially growing market, geographic location and economic and political stability.

Manufacturing, and wholesale and retail trade sectors have received the biggest FDI inflows in Lithuania throughout the 1990s, although their share is gradually decreasing giving place to telecommunications. By January 2004, manufacturing had received more than a quarter of all FDI (*LDA, 2004*).

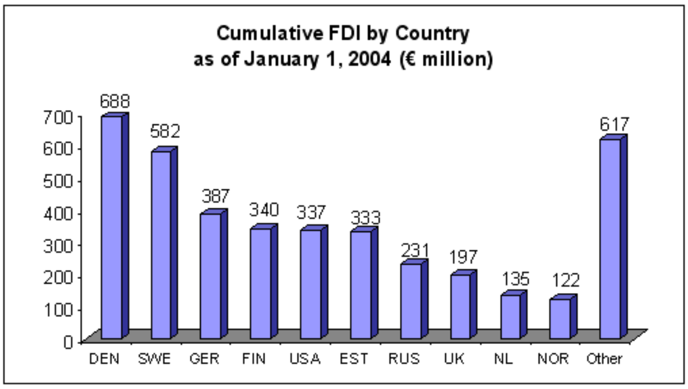
**Table 1.**



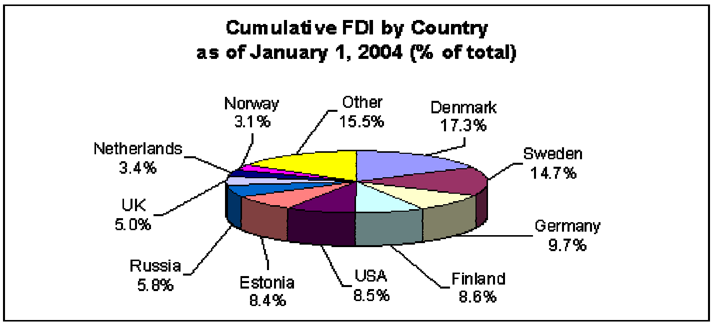

Source: Lithuanian Development Agency

As of January 2004, Denmark has accounted for the biggest share of cumulative FDI (17%), followed by Sweden (15%), Germany (10%), Finland (9%), the United States (9%), and Estonia (9%) (*Table 2*). Currently, the European Union accounts for about two-thirds of all FDI, and its role is expected to increase since Lithuania joined the EU in May 2004.

**Table 2.**




Source: Lithuanian Development Agency




Source: Lithuanian Development Agency

There are only two Russian companies among the top 36 foreign investors in Lithuania. Yukos ranked 4th with €150 million purchase of Mazeikiu Nafta and Lukoil is ranked 23rd with the €29 million investment in gas stations (*LDA, 2004*). However there is reason to believe that the situation is slightly different. It is quite difficult to monitor accurately the Russian investments as Russian companies often use off shores for their investment purposes or just companies registered outside Russia. For instance in December 2000, there were 1073 enterprises registered in Lithuania with the participation of capital from Russia, among them – 839 joint enterprises and 234 enterprises fully owned by Russian capital (*Miskinis, 2002*). As of June 2003 the Cypriot investments in Lithuania amounted for $75 million (*Vahtra&Liuhto, 2004*). The significant amount of Cypriot investments is generally considered to be of the countries recipients domestic or of Russian origin.

According to the amount of capital investments, Russia ranks 7th (Table 2) among the 112 countries, which have invested their capital into the economy of Lithuania. There are two ways to review this figure. One is to note that Russia is one place after even Estonia whose economy with 1,36 million inhabitants is hardly compatible as size and strength. However it should be accounted that the political hostilities and the weakened economic situation in Russia did not contribute toward much of an outward Russian economic expansion before 1999. It was then when Russian companies enabled by a reviving Russian economy and high oil prices got the will and the means to expand internationally. The second is to put the accent on the qualitative dimension of Russian investments.

In Lithuania it is not the amount of Russian investments, which causes concern among Lithuanian politicians and decision makers. It is their clear orientation toward strategic sectors of the economy - energy supply and distribution.

### 2.2. Russian investments in Lithuania – to fear or not to fear?

The two main reasons for trying to rebuff Russian investments were perhaps the fear of loosing control over vital aspects of the economy and secondly the usually unclear source of investments. Along these lines for a long time in Lithuania it was commonly accepted that keeping the Russian investments away is in the interests of national security.

Thus Lithuanian politicians observed potential investments not only in terms of their economic value and essence but also for their political impact. In the light of Lithuanian candidacy for NATO and EU membership it was considered that priority should be given to investments from Western Europe and the USA. In this respect it is interesting to observe that Russian analysts do see only the political motivation in such prioritisation but fail to acknowledge that besides capital Western investment lead also to transfer of management culture, know-how and technology that are as a rule superior to anything Russian companies may offer.

The first tangible Russian effort was the 1994 offer of Lukoil to participate in the construction of Butinge terminal in exchange for shares in it (*Skripov, 2004*). However for political reasons the proposal was categorically rejected. The rejection was also interesting indicator as it was made by the left wing government (Shleziavichus) and left wing president (Brazauskas) with a parliamentary majority also from the left. When opening the construction the Prime Minister Shlezavichus called the project “political investment” that will free Lithuania from the dependency on Russian oil. Thus the claim that the left wing political forces in Lithuania are pro-Russian do not really hold true (*Ibid.*)

Another good example was the privatisation of Mazeikiu Nafta in 1997-1999. It was the conservatives who ruled the country at the time and the minister of the economy Vincas Babilus summarised the policy of the Lithuanian Government with the slogan “Don’t let Ivan to the pipe!” The Lithuanian government assessed the economic and political pros and cons and the pipe together with the oil refinery and the terminal was given to the American company Williams International.

The three companies (the Butinge terminal, the Naftotiekis oil pipeline company, and the Mazeikiu Nafta refinery) were combined into one, and 33% of the combined company's shares were allocated to Williams International /WI/. The total investment by WI in their 33% share in the new combined Mazeikiu Nafta company was about $150 million. WI has also committed another $650 million investment to modernization. As part of the deal, the Lithuanian government agreed to cover a previous $350 million deficit the pipeline company had incurred. The deal gave the WI management control of the company and the right to buy a majority of the shares within five years, and also included the right to transfer 10% to financial institutions like the EBRD and 10% to oil suppliers (*US DoE, 2004*).

However, there were objections to the deal from some Lithuanian citizens and from the Russian oil company Lukoil. The former caused delays in completing the deal while the latter caused continuing oil supply shortages. Repeated attempts by WI to reach a lasting supply agreement were unsuccessful, and some crude supplies were arranged from North Sea and Kazakh suppliers.

As the political benefits (better relations with the USA) were marginal and the economic benefits were somewhat dubious the overall calculation proved to be wrong. The economic losses were tremendous as it became apparent that Russian oil suppliers deliberately or not can not secure a steady supply of oil for the refinery. Different evaluations show that for the approximately 3 years WI owned the company it generated losses of approximately $500 million (*Skripov, 2004*).

Over time the Lithuanian government realised that the Western origin of investors alone is not enough to guarantee that the investment is fruitful and productive in the long run. To the not really successful sale of Mazeikiu Nafta to WI could be added also the near destruction of the leading Lithuanian textile manufacturer in Alituse by the Singapore company Tolaram Group.

Still to Lithuanian politicians is uneasy to accept that about the only sphere of the Lithuanian economy where Russians have particular interest is in the strategically important energy resources supply and distribution. For them it is not easy to accept that the investment decisions of Russian companies are taken exclusively on economic but not on political principles. Along this lines it may also be explained perhaps why Lithuania was particularly worried about the activities of Russian state owned (or state controlled) companies such as Gazprom, Rosneft, TNK, RAO UES.

After the year 2000, Russian companies again intensified their investment interest toward Lithuania and this time their efforts reached certain degree of success. According to the data of the Department of Statistics in July 2002 there were 119 investors of Russian Federation with $172,3 million or 5% of all direct foreign investments in Lithuania. Among the largest enterprises, which have Russian investments, besides Mazeikiu Nafta, could be mentioned enterprises such as:

- Kuro aparatura (fuel injection equipment for diesel engines, bought for $3 million by the Russian OOO Kris (*Baltkurs, 2002*)
- Polasta is 49,18% owned by Surgutgazprom and produces plastic products and chemistry (*Gazprom, 2003*)
- Atrama (boilers and heaters)
- Silmega (plastics)
- Gargzdu mida (polymeric bitumen roofing)
- Alytaus pieninė (dairy products)
- Nilma (forestry products)
- Baltic Garantas (insurance and pension fund)
- Korelita (fabrics and fibers)
- Stella Vitae (natural gas supply)
- Atomkomplekt (nuclear power engineering)

(*Lithuania Presents, 2002*)

By 2004 the figure went to cumulative investments of €231 million that represented 6% of all direct foreign investments in Lithuania (*LDA, 2004*).

In the focus of this article are four of what could be considered to be the major Russian investments in Lithuania. These are:

- the purchase of Mazeikiu Nafta refinery by Yukos
- the Gazprom investments in the Kaunas power plant and Lietuvos Dujos
- the purchase of Lifosa by the Russian Eurokhim Holding / MDM Group
- the purchase of Snoras Bank by the Russian Konversbank / MDM Group

### *2.2.1. Yukos in Lithuania*

In June 2001, Williams International reached a 10-year oil supply agreement with Yukos, Russia's largest oil company. Under the deal, Yukos guaranteed almost 100,000 b/d to the Mazeikiu Nafta refinery and 80,000 b/d for exports through the Butinge terminal. As part of the deal, Yukos got the right to buy 27% of Mazeikiu Nafta, and WI's stake was reduced to 27%. This gave WI and Yukos equal ownership, but Williams International retained management control of the company. As part of the deal, the Lithuanian government's share was reduced to 41%. The deal was ratified by the Lithuanian parliament in August 2001. That was the basically the competitive advantage of Yukos over Lukoil – Yukos preferred to use "one step at a time" approach instead of the much more confrontational strategy of Lukoil. In September 2002, Yukos bought out WI share of Mazeikiu Nafta for $85 million and thus took control of the company. Right after the buyout, Yukos increased the crude oil supply for Mazeikiu Nafta to about 145,000 b/d (*US DoE, 2004*).

The financial results for the first six months of 2004 according to the company's auditor PricewaterhouseCoopers reviewed net profit of $82.4 million compared to $23 million US dollars net profit during the same period in 2003. Company's revenues reached $1.1 billion during the first six months of 2004 or $391.9 million more than in the same period of 2003. According to P. Nelson English, General Director of Mazeikiu Nafta that was the most profitable six months in company's history due to high refining margin, record throughputs and the hard work and dedication of Mazeikiu Nafta employees (*MN, 2004*). Mazeikiu Nafta refined over 3.9 million metric tons of crude and other feedstock during the first six months of 2004, more than 1 million metric tons more than in the same period last year (Ibid.). The refinery reached a record monthly throughput in June by processing 754 thousand metric tons of crude oil and continues to run at record daily rates. The Butinge Terminal loaded 4.62 million metric tons of crude during the first six months of 2004, compared to 5.87 million metric tons in the same period of 2003. Sales of gasoline, diesel and other products within six months of 2004 amounted to 672 thousand metric tons in Lithuania, 249 thousand metric tons in Latvia, 167 thousand metric tons in Estonia and 167 thousand metric tons in Poland. Sales in strategic markets for same period a year ago were 633 thousand metric tons in Lithuania, 194 thousand metric tons in Latvia, 129 thousand metric tons in Estonia and 116 thousand metric tons in Poland. Almost 2.23 million metric tons of products were transported via the Klaipeda seaport to Western Europe, the US, Canada and other parts of the world during the six months of 2004, up from 1.39 million metric tons within the six months of 2003 (*Ibid.*).

However such good results did not spare Mazeikiu Nafta from the problems related to the Russia’s government assault against Yukos. At the beginning of the Yukos crisis the Lithuanian stock market reacted quite. However as of August 2004 the situation got upside down and in one single week Mazeikiu Nafta share rate dropped by 22.48%. Market participants worry about the stability of the company activity, which after events in Russian can be disturb this situation. Also recently gossips started that Russian oil company Lukoil (favoured by Kremlin) aims to Mazeikiu Nafta and can discuss its purchase plans (*Byla, 2004*).

### *2.2.2. Gazprom in Lithuania*

It must be noticed that Gazprom is much more important to Lithuania than Lithuania is to Gazprom. The Lithuanian share of Gazprom total exports for 2002 was less than 1,4% (*Gazprom, 2003*). The Kaunas power plant produces about 80% of the heating consumed in Kaunas, Lithuania's second largest city (*Pravda, 2003*). In September 2002 the winner of the tender was announced as a consortium consisting of Gazprom, Dujotekana and Clement Power Venture. The Kauno Termofikatsios Elektrine (KTE) international consortium and Lithuanian company Kauno Energia have signed an agreement on the sale of the Kaunas power plant. According to Gazprom's press office, *KTE* paid around $35 million for the plant as well as pledged financing for a $42-million investment programme up to 2006 (*Ibid.*).

The JSC Lietuvos Dujos is a Lithuanian gas company dealing with gas procurement, transmission and distribution in Lithuania. The company operates 1630 km of high-pressure gas pipelines and employs 2200 people. Lietuvos Dujos is one of the largest state companies in the country and owns a compressor station, a gas measurement station and 58 gas distribution stations. Gazprom acquired a 34% stake with $37 million and guaranteed natural gas supplies for a decade. The stakes were sold from the government's 58% holding. The German company Ruhrgas also owns 36% of Lietuvos Dujos. Gazprom is expected - in conjunction with the German company -- to upgrade the local gas sector, extend the grid, and pave the way to connect the grid with the EU network. In March 2004 Gazprom finalised the deal to acquire Lietuvos Dujos' 34% stake and signed the Shareholders' Agreement adopted between the State Property Fund of the Lithuanian Republic, Gazprom (as the Gas Supplier), and Ruhrgas Energie Beteiligung AG (as the Strategic Investor) (*Ibid.*).

Stella Vitae is another major player in the natural gas market where Gazprom is reported to hold 30% stake in the company (*Pravda, 2001*). Another company where Gazprom (through its affiliate company Surgutgazprom) holds 49,18% is Polasta that is owned by and produces plastic products and chemistry (*Gazprom, 2003*)

### *2.2.3. Lukoil Baltija in Lithuania*

Lukoil was established as a closed stock company, a joint venture between Lithuania, Russia and Luxembourg, in November 1992. Initially, it served to co-ordinate the supply of crude oil for the Mazeikiu Nafta oil refinery and the export of oil products to Russia.

Since the conclusion of the WI deal, Mazeikiu Nafta has encountered problems obtaining crude oil supplies from Russia. It was the Lukoil way to demonstrate its disappointment with the privatisation strategy the Lithuanian government applied for the oil refinery. As a result, Mazeikiu Nafta suffered close to $40 million in losses in 1999 and posted $10 million dollars in losses for the first half of 2000. In May 2000, after months of negotiations, WI and Lukoil announced that they had signed a protocol of intent to create joint supply and marketing enterprises in the Baltic region.
Under the deal, a jointly owned supply company will deliver 6 million tons of crude a year (120,000 bbl/d) from Lukoil and other Russian companies to the Mazeikiu

refinery. The Lithuanian refiner will process the crude and sell resulting oil products through a series of marketing enterprises jointly owned by Mazeikiu Nafta and Lukoil. However Lukoil continued to insert pressure to become shareholder in the company insisting that oil should be supplied at world prices that at the time were about $10 higher than the prices at which Mazeikiu Nafta was purchasing the Russian oil. WI offered Lukoil 33% of the shares, two places in the board of directors of Mazeikiu Nafta and the position of associated deputy director of the refinery (*Bernstein, 2001*). Lukoil was reluctant to accept such an offer, as the operational management in this case would have remained in the hands of WI. The discussion between WI and Lukoil was becoming increasingly ugly as Lukoil was accusing WI management in incompetence while WI was insisting that the situation is deteriorating due to an intentional uncooperativeness of Lukoil.

Later, following economic changes, Lukoil Baltija began buying crude oil and refining it. Profits have been invested in building petrol stations and enlarging the infrastructure of the enterprise. In 2003 Ivan Paleichik, Lukoil Baltija chairman, said the company is expected to expand its existing chain from 100 to 120 petrol stations by the end of the year. In 2003 the company controlled nearly 25% of Lithuania's fuel retail market (*Baltic Business Monitor, 2003*).

#### *2.2.4. MDM Group in Lithuania / Lifosa and Snoras*

Both Eurokhim holding and Konversbank belong to MDM Group of Russia that is owned by an Austrian parent company, MDM Holding GmbH (*MDM, 2004*). In 2003, Antilles Comercio Internacional S.A. (Portugal), a company controlled by Mr. Melnichenko, sold a 50% stake in MDM Holding GmbH to Metano-Servicos E Marketing S.A. (Portugal), a company controlled by Sergey Popov, Mr. Melnichenko's long-standing partner in MDM Industrial Group (*Ibid.*).

In August 2002, Eurokhim acquired 70% of Lifosa shares for €4,5 million (*NSE, 2002*). Lifosa is one of the biggest in Europe producers of phosphate fertilisers and the 5$^{th}$ biggest (in terms of sales volume) Lithuanian manufacturer. Eurokhim is a vertically integrated holding including companies in mining, chemical processing and trading where management planning, budgeting and investment processes were centralised in the holding. Thus it has a full control over the assets, industrial and investment activities, and cash flows of all the participating enterprises (*Gromova, 2003*). In the production of phosphate products the holding is the second biggest in Europe and sixth worldwide with annual turnover of $900 million (*MHK, 2004*).

In 2003 the board of Lithuania's Central Bank has granted permission to the Russian Konversbank and its subsidiary, Luxembourg-based Incorion Investment Holding Company, to raise its ownership stake in the commercial bank Snoras, assuming management control as well. After the stock purchase Konversbank holds a combined 58% stake in the Lithuanian commercial bank (*RFE, 2003*). Snoras bank is the forth bank in Lithuania by size and possesses one of the most advanced and extensive banking service networks in the country. Snoras bank has over half a million customers or almost every sixth Lithuanian resident uses its services and is a member of Konvers Group, an international Banking group[1] with (*Snoras bank, 2004*). The new owners sold the belonging to Snoras bank non-life insurance company Snoro Garantas to the Russian insurance company Reso-Garantia (*BBM, 2003*). For the first half of 2004 Snoras bank had 15% growth of profits that amounted to LTL 10.6 million - the highest growth among all Lithuanian banks (*BBM, 2004*).

It seems that even if Russia is only the 7$^{th}$ biggest investor in Lithuania, its investments are in key areas with strategic importance. Russian companies control the 4$^{th}$ biggest Lithuanian bank, approximately 25% of the retail fuel market, the Kaunas power plant, and stakes in the biggest gas distribution company. Russian companies own Mazeikiu Nafta (as of 2001 some 30% of Lithuania's GDP were associated with the refinery (*Roe et al., 2001*) as well as the 5$^{th}$ biggest (in terms of sales volume) industrial producer.

Therefore the importance of the topic what corporate culture and business ethics Russian companies spread when they internationalise for Lithuania could be more than an academic elaboration.

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[1] Starting in 2003 Konversbank started forming Konvers Group that included Konversbank, Academchem Bank and Snoras bank. Among others the group is supposed to be the financial branch of the Russian Academy of Science and Ministry of Nuclear Power.

## 3. Patterns of corporate culture among Russian companies operating in Lithuania

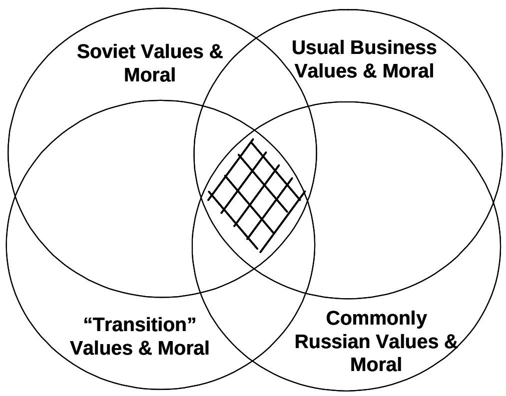
An important influence of the contemporary Russian business culture seems to be often unnoticed – the one Russian companies could spread in their foreign operations. The growing international expansion of Russian companies (*Liuhto 2001; Liuhto&Jumpponen, 2001, 2003; Vahtra&Liuhto, 2004)* results in some "export" of the underlying recent business values and attitudes of Russian corporations. That has certain impact on the involved foreign players and environments be it businessmen, officials, companies, bureaucracies, international organizations etc.

In parallel with their international business expansions Russian companies certainly do bring their own corporate culture with them and use it in full or partially. This chapter attempts to outline the factors shaping the contemporary Russian business culture and elaborate on the possible negative influence they may have in the foreign activities of Russian companies.

### 3.1. Contemporary Russian corporate culture.

The contemporary Russian corporate culture could be presented as the cross-section of four different sets of factors and their consequent impact on collective and individual culture and mentality as shown in Figure 1.

**Figure 1.** Four sets of factors forming the contemporary Russian business culture.




The first set is formed by the traditional Russian values and norms that distinct Russians as compared to other national cultures. The second set could be defined as those norms and values that were added / enforced to the Russian mentality during the time of the Soviet Union. The third set represents those new developments and modifications in mentality and culture that the last 12 years of transition process required from every social group and/or individual in Russia. Finally, the fourth set of factors is assembled by the influence of Western business culture whose impact constantly increases due to the growing business interaction.

A more detailed critical survey of the four sets is provided below with accent on the influence they have had and the features they have brought to contemporary Russian corporate culture.

### *3.1.1. Commonly Russian values and moral*

As one of the most striking factors influencing the commonly Russian business values and moral could be underlined the near total lack of competition in the Russian social and economical life – an argument that was pointed out by many authors (see e.g. Prohorov, 2002). Thus among the three main features of the Moscow state were:

- *militaristic nature* as the state had to fight external enemies and expand further geographically
- *society based on force rather than law* with clearly determined division of social groups. These groups differ by their duties rather than by their rights
- *supreme power of the state / tsar* with not clarified and unlimited authority space

All these features were slowly suffocating the very concept of free competition in the allocation of any type of resources – human, financial, natural etc. As a result a highly centralized system was built where the state in the face of the Russian emperor had unlimited and not clarified powers. The latter were transmitted to the rest through an ever growing, slow and inefficient apparatus of state bureaucracy. It is not by a surprise that in such conditions the competitiveness was directed mainly on attracting the attention of the supreme power through gifts, bribes and network of important acquaintances.

Such system will also partially explain that all prominent international Russian business projects – be there in railways, investments or simple exports were in most cases directly or indirectly sanctioned and/or financed by the state.

### *3.1.2. Soviet values and moral*

The system did not change much in the soviet times – the state succeeded into implementing total control on all activities that could be characterized as deeper and broader if compared to the centralized administration during tsar's times.

Again the state had the not clarified and unlimited authority to allocate resources of all types. Furthermore the state imposed an ideological embargo that additionally stalled the system. The Soviet rule also imposed concepts such as the "uravnilovka" that eliminated the link between work and pay, "planning" versus market that geared further the bureaucracy and made cheating an inbuilt part of the economic system, "repression" that became a state concept and thus eliminated initiative, decision making and freedom of choice.

Again, surviving and economic (and physical) prospering in the system was dependent on one's links to the state power in its various forms: communist party, state administration, and military, KGB etc. Again the competition was levelled down to none as most factories obtained a monopolist status and were given predetermined figures on input and output and workers did not have initiative due to the "uravnilovka".

The Soviet system also did not succeed to eliminate the corruption and bribing that plagued the Russian state machine in the times of the tsar. Quite the opposite, in the presence of an almost total deficit for goods and services corruption became the normal way of life. The basic lesson Soviet managers learned was that being obedient to the system through keeping a low profile was the best strategy to follow. Maximizing the requested from the planning committee input and minimizing the expected output was a common strategy.

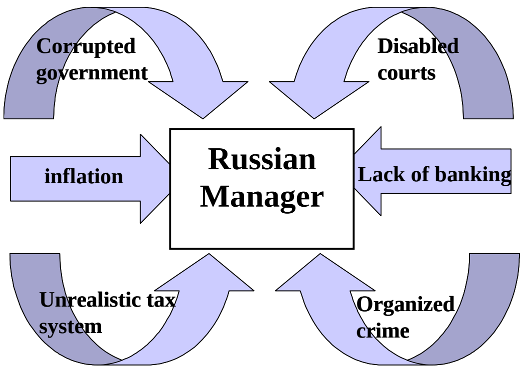
The foreign operations of Soviet companies were an absolute state monopoly controlled by the party, the state and KGB. Officially only the Foreign Trade Organizations were authorized to link Soviet factories with their overseas markets, suppliers, partners etc. Any investment decision, be it a power plant in Cuba, factory in Sudan or military equipment to Egypt was part of a conscious centrally planned and controlled foreign policy rather than a money wise business rational based decision.

### *3.1.3. Transition values and moral*

Perhaps the most interesting and intriguing period that has a considerable influence on the Russian business culture is the economic and political transition that Russia is experiencing for the last 14 years.

A dramatic (by the Russian standards) change has appeared in the form of a massive (initial) retreat of the state. Dodgy or not, fair or not, the privatisation in Russia created in few years a new social group of owners – investors, capitalists, industrialists etc. Still, it must be noticed that it was not their entrepreneurial spirit that was the main factor for their success. It was rather a well build network of contacts with the government at all different levels in combination with a total disrespect for the "transitional" semi-Soviet, semi-market legal system.

**Figure 2. Sources of pressure on company management**




The state retreat in the 1990s and its inability to perform vital functions generated huge vacuum in the economic and social situation in Russia. Russian managers at the time were imposed to number of stressful forces as shown in Figure 2.

One of them was the high inflation that was making business itself a difficult task and almost impossible to make any mid- or long-term business decisions and planning. Such a high degree of unpredictability was one of the main reasons for Russian managers to be focused mainly on short-term incomes, profits etc. Another reason for that was the absence of normal corporate banking (that still continues) and of bank credits to businesses. That meant that alternative sources of financing are needed. Such are provided typically very risky conditions and from very risky places.

Another serious obstacle was the growing organized crime that was constantly trying (and to a large degree succeeded) to be deeply involved in business. Drugs, prostitution and racketeering were only the initial operations that soon went into much more sophisticated schemes such as tax dodging, money laundering, banking and privatisation. In the presence of next to none existing legal system and dysfunctional courts business disputes and debt collection became a domain of activities for the organized crime.

Not succeeding into building a stable macroeconomic environment, launching a failed bank reform, not effectively combating organized crime were perhaps not the biggest shortcomings of the Russian state in the early 1990s. The worst three pressures that the state offered to businesses and managers were extremely weak and corrupted institutional / bureaucratic machine, practically disabled courts and an unrealistic tax system that made most members of the business community outlaws by definition.

Surprisingly the state stopped performing vital duties of control and regulation but still remained the prior arbiter with the known from history not clarified and unlimited rights to interfere into everybody's business and daily life.

### 3.2. What corporate culture Russian companies spread in Lithuania

From the presented above evidence one may jump to the conclusion that Russian companies are some sort of puppets in the hands of the Russian state machine, that they bribe themselves out of any situation, rely mainly on informal networking, have over manned and inefficient labour and managerial practices and generally in their survival mechanism there is little respect for law. To some extent this description may fit many Russian companies operating in Russia.

Hence, if serious problems of business ethics plague and continue to plague the way business is conducted within Russia, the internationalisation of Russian companies puts forward the question what exactly business cultural influence they spread when they internationalise? Standardization or localization - do Russian companies and executives use a standardized approach of utilizing Russian business culture or they try to adapt to the local environment? Is the statement that Russians see no problem with favouritism, price fixing, ignoring senseless laws and regulations and manipulating data (*Puffer, 1996*) valid and do they bring such type of thinking in their foreign operations? Is it correct to conclude that Russian companies prefer Russian managers in their offices abroad? Are the features in Russian business ethics perceived as negative, influencing other business cultures when the Russian corporations go abroad and if yes then to what extent? When it comes to their overseas operations the situation is a bit more complicated than that.

The Russian companies are also acknowledged to be among the most active bribers when doing business abroad (*Transparency International, 2002*)

The discussed above assumptions provide enough reason to assume that as most worrying features of Russian corporate culture could be considered:

- an unbroken link/dependence of Russian companies on state and stemming from it consequences over political versus economic motivation when making corporate decisions
- non-negative attitude towards bribing and corruption
- the somehow neglected in Russia issues of raising efficiency and productivity

### *3.2.1. The unbroken dependence on the state*

Are the biggest Russian investors in Lithuania emitters of official Russian state policies? To what extent their relations with the Russian state made them dependent on it?

The current ownership of OAO Gazprom shows that the company belongs 38,37% to the Russian state, 36,28% to Russian legal subjects, 13,85% to private persons, 11,5% to foreign investors (*Gazprom, 2004*). Even though that information is not sufficient to understand who actually controls and runs Gazprom (it does not answer who are the legal subjects themselves – private or state owned) it is widely accepted that Gazprom is a state owned company that has natural monopoly over exploration, production and distribution of natural gas.

As such the company's CEO would naturally be the selected and appointed by Kremlin and personally the president. It is not by surprise then that the current Gazprom CEO Alexei Miller is a personal appointment of President Vladimir Putin.

Miller is the President's former colleague and, according to experts, his mission at Gazprom is more political, to transmit Kremlin policies, than economic management of Gazprom. It is obvious then that most overseas investment decisions of Gazprom must first have a Kremlin clearance. Such as the decisions to buy the Kaunas power plant and to take stake in Lietuvos Dujos.

That is exactly what worries Lithuanian politicians. The former chairman of the Lithuanian parliament, Vytautas Landsbergis argues "We should avoid such Russian expansion in the energy sector, which is pre-planned, calculated, and which is also part of a political expansion seeking to increase Russian influence in Lithuania. In the past Vladimir Putin has said Russia's policy aims could be achieved by using so-called "energy diplomacy" (*Mite, 2004*)

On the contrary, a member of the Lithuanian parliamentary committee of economics, Birute Vesaite, says it would be silly to build stumbling blocks for Russian capital just because it is coming from Russia. "We have no other way out," Vesaite says. "Who are the main oil and gas suppliers for Lithuania?" Lithuania may have no alternative. That's the view of Nicolas Redman, a Russia analyst at the London-based Economist Intelligence Unit. He says the country cannot afford to buy gas from the West when the Russian product is cheaper and closer (*Ibid.*).

Still, Vytautas Radzvilas, an analyst at the Lithuanian Institute of International Affairs in Vilnius says "there is no doubt" that Russia is seeking to maximize its influence through economic means. However, he says that the presence of the German company will make it difficult for the Russians to abuse their position.

Yukos is also an interesting example as it shows the opposite case when a completely private company is subjected to such pressure by the Russian government that it turned Yukos from the wealthiest in Russia to the verge of bankruptcy in less than one year. Yukos was internationally recognized as one of the most efficient, market driven and transparent Russian companies. However, Mr. Khodorkovski did something wrong in the eyes of Kremlin and the state demonstrated that it is intent to almost ruin the Russian most successful oil company for the sake of politics.

Lithuanians are monitoring the development quite closely. The situation of the Lithuanian oil refinery Mazeikiu Nafta would worsen only in case the stable supply of raw material from Russia was disturbed. It was believed that the fallen ratings of the Russian shareholder Yukos and ceaseless attacks of the Russian authorities against this oil giant could not influence the output of Mazeikiu Nafta and its financial operations. However the latest strategy applied by Russian authorities is exactly to cut short the oil supply to Yukos (*Reuters, 2004*).

Lukoil is perhaps the opposite story of Yukos. It is an oil company that is approved by Kremlin where its CEO Vagit Alekperov is in good standing with president Vladimir Putin. Only in July 2004 Russian president Vladimir Putin, ConocoPhilips CEO James Mulva and Lukoil president Vagit Alekperov discussed oil and gas projects during a meeting in the Krasnodar territory (*Interfax, 24.07.2004*).

Still only few years ago the Russian tax police have simultaneously opened criminal charges against Lukoil and its director, Vagit Alekperov for concealing revenues in “especially large amounts.” (*GPF, 2000*) The 1995 big scandal surrounding Lukoil and its practice of mixing different gasoline types that brought them additional profit 4,6 billion roubles can easily be brought back (*Rstaki, 1999*). Bureaucrats are who covered it back then and bureaucrats are who can easily bring it on again. Just as the Yukos case. Is it then possible to foresee if Lukoil will always stay as a favourite to the Russian government? And if not is it possible to claim that Lukoil is a competitive, stable, predictable international player?

While Eurokhim holding bought Lifosa, Snoras bank is property of Konvers bank. In fact both Konvers bank and Eurokhim belong to the Russian MDM group that belongs to Andrei Melnichenko and Sergei Popov. Their interests are various and the two of them sit in the RAO UES board of directors. Their positions seem to be stable. At the moment! For how long they and their business empire will be approved by Kremlin is an open question.

### *3.2.2. Corruption and bribing*

Official corruption in Russia is endemic, a system-wide state of affairs with deep historical roots. A shocking number of both foreign and Russian private businesses regularly pay bribes to government officials. Most justify the practice on the basis that in a highly regulated market where officials of every level are poorly paid, bribery is a harmless means to facilitate government approvals and avoid penalties. In a system fuelled by bribery, the free market forces of competition, efficiency and quality are displaced. Economic decisions are taken by government officials on the basis of ulterior motives. For example, when a bribe helps secure a government contract, public funding is not being allocated for the best service at the lowest cost.

As artificially high project costs use up limited Russian budgetary resources, bribery diminishes the funds available for government spending on basic infrastructure. Bribery is also a brake on competition in Russia, which is desperately needed as a catalyst for economic growth. For example, bribes are sometimes paid in order to keep a competitor out of the market, by preventing it from receiving a license or winning a bid (*Murray, 1998*)

The Russian companies are also acknowledged to be among the most active bribers when doing business abroad (*Transparency International, 2002*) In May 2003, a leading Iraqi politician -- Iyad Allawi of the Iraqi National Accord (who has been appointed as interim Iraqi Prime Minister) -- accused former Russian Prime Minister Yevgeny Primakov of accepting money in return for defending Saddam (*Stanley, 2003*).

The ability to bribe and corrupt is to a large extent dependable on the legal and social framework of the country hosting Russian investments. In the 2003 corruption perception index Lithuania is ranked 41$^{st}$ while Russia shares 86$^{th}$ place together with (*TI, 2003*). That is why we may discover more corruption scandals involving Russian companies in, say, Lithuania than in Finland. A general assumption might be that wherever an opportunity to bribe arises, a Russian company would most probably not hesitate to use it. That is inbuilt feature of the Russian business culture that was always part of it – no matter if historically it was during tsars times, communism or transition, no matter if it was during the oppressive Ivan the Terrible or Stalin’s regimes or in the more relaxed times of Catherine the Great or Brezhnev. The economic transition of the 1990s during which MDM Group, Yukos and Lukoil were created and Gazprom transformed also does not give reason to believe that Russian companies should not actively use bribing whenever the opportunity exists. Hypothetically bribing would be comparatively more available option when the company is fully owned by a Russian parent company as it is with Snoras bank, Lukoil Baltija or Lifosa. The opportunities to do it in the case of Lietuvos Dujos are limited as the participation of the German partner (Germany is ranked 16th in the TI corruption perception index) Ruhr gas certainly provides with checks and balances.

### *3.2.3. Productivity and efficiency*

Even Karl Marx understood that productivity is the crux of capitalism. It's hourly output per worker, and for years before and after the collapse of the Soviet Union, Russia's workers were at the bottom of the league tables. According to the completed by McKinsey Global Institute a yearlong study of the Russian economy in 1999 productivity in Russia was less than 20% of the U.S. level and stagnating (*Lewis, 1999*). However, the same survey concluded that approximately 75% of the Russian industrial capacity, if well managed and improved with modest investments, could rapidly reach 60% to 70% of U.S. productivity (*Lewis, 1999*).

The standard of living is determined by the productivity of a country's economy, which is measured by the value of goods and services produced per unit of national resources (human, capital and physical). Productivity then defines competitiveness (*Porter, 1998*). As recognised by the Moscow bureau of the International Labour Organisation a considerable part of the labour force is concentrated in unprofitable enterprises. Labour time is not efficiently used. Productivity is low and not monitored.

Another case study from 70 firms in 8 of Russia's regions in the summer of 2000 collected interviews of general directors and other senior management and revealed that some job destruction has occurred, but many firms are still over-employed *(Broadman, Recanatini, 2001)*. "Labour productivity and efficiency levels have been Russia's biggest problems since the Soviet era," says Ruben Vardanyan, CEO of Troika Group, a Moscow financial services firm (*Belton, 2002*). Some experts go as far as to claim that in reality most Russian companies lost their competitiveness in the 1990s and by 2002 just under 15% of the remaining fixed capital in Russian industry is able to produce competitive goods (*Beloussov, 2002*).

Is there basis for concern in the case of Yukos, Lukoil, Gazprom and MDM Group? Of course, the conventional assumption here will be that the state owned companies would be less efficiently managed than the other privately owned companies. Indeed, the biggest productivity gains have been made at privatised companies. Not as burdened as some other Russian oil companies by excessive national pride – the belief that Western executives can't really teach the Russians anything – at the end of 1990s Mr. Khodorkovski settled into a stable working relationship with Schlumberger, the giant oil-services provider, and the two set out to improve the productivity of Yukos' vast number of wells in western Siberia (*Powell, 2002*). As a result Yukos has cut costs per barrel from $7 in 1998 to less than a third of that as productivity has doubled since 1998, thanks to a $1.3 billion investment in new fields and technology. In a comparison it costs state-run oil company Tatneft $4.5 to produce a barrel of oil, double what it costs Yukos (*Belton, 2002*). In respect of productivity and efficiency state-controlled enterprises such as Gazprom and RAO Unified Energy System /RAO UES/ have been slow to make changes.

Such statement could be confirmed by the latest study by a key minority shareholder in Gazprom, Hermitage Capital Management (*Belton, 2004*) According to the report Gazprom appears to have haemorrhaged more than $2 billion last year via a massive increase in miscellaneous expenses and staff costs, as well as from lost sales to key European export markets granted to a middleman with a murky background, according to a new study.

Gazprom CEO Alexei Miller has pledged to put an end to the egregious mismanagement at the company under his predecessor, Rem Vyakhirev, when up to $3 billion per year was squirreled away into crony companies, investors alleged. But despite successes in returning some lost assets and in keeping down costs, Miller oversaw a "significant deterioration" last year, Hermitage says. "The situation looked like it was getting better in the early post-Vyakhirev years," said William Browder, CEO of Hermitage Capital Management, which manages some $1.5 billion in assets on the Russian stock market. "Now, however, it seems to be quickly deteriorating."
Other analysts said that overall, Gazprom's corporate governance performance has much improved and in general Gazprom appears to be operating more honestly than it ever was. Still a comparison of the 2002-2003 productivity levels between the 10

most productive industries in Russia (output volume measured in rubbles per employee) and Finnish companies (turnover per employee) from the same industrial field reveals that at the average Russian companies are 20,2 times less productive (*Zashev, 2004*) In Russia it is the Oil & Gas industry considered to be the productivity champion. The Russian productivity (turnover per employee) in Oil & Gas is 22 times lower than the joint average for Fortum, Finland and TotalFina, France (*Ibid.*).

In the case of MDM Group with Lifosa and Snoras again the factor that the Russian parent company is private could be seen as overwhelming. The results of both Lifosa and Snoras after they became part of the MDM Group demonstrate that the companies are efficiently managed. Still, their major restructuring was done before the purchases. Lifosa has reorganized and became leaner, signed a distributorship contract with the world leader Cargill before the deal with Eurokhim. Eurokhim was needed mainly in the quality of main raw material supplier and that is seen by the 5 members of the board of directors – Eurokhim president Nikolai Levackii and executive director Alexei Kabin representing the owners, the Lifosa minority shareholder Danas Tvarijonavichus and Lifosa general director Jonas Dastikas as the operational management and the Cargill representative Arian Van den Blink as the company's main distributor. Amo9ng other things the board decided that the audit of the company would be done by Price Waterhouse (*Finmarket, 2002*).

The business and managerial success of Lifosa and Mazeikiu Nafta helped to ease the suspicion of the Lithuanian political establishment towards the nature and the true intentions behind the Russian investments in Lithuania. The suspicion though is still there. It took Gazprom more than one and a half years to negotiate the Lietuvos Dujos stake purchase. There are voices among the conservatives for the government to buy out the Mazeikiu Nafta from Yukos. They also suggest establishing a list of strategic assets that will be of limits for capital from Russia. Others insist to use a more liberal approach described as the "capital balance" such as in the case of Lietuvos Dujos (*Skripov, 2004*).

## Conclusions

The Russian investments in Lithuania are playing increasingly important role in the economic life of the country. For quite some time the Lithuanian politicians tried to prevent Russian companies from actively investing and operating in the country. The political and economic pressure that Russia inserted on Lithuania in the first half of the 1990s is a lesson that Lithuania will not easily forget and one that taught the Lithuanian decisions makers that it is important to be not only politically but also economically independent from the colossus neighbour.

However, the closer Lithuania became to NATO and EU memberships the easier it became for Russian investors to establish themselves in the country. Several factors contributed for it: the growing security confidence stemming from the membership in both organisations, the mutual interest of buyer and supplier of raw materials to find a mutual business partnership and lastly the understanding that for an investment to work it is not enough to have it coming from the West.

As of the beginning of 2004, the volume of Russian investments in Lithuania puts Russia in only 7$^{th}$ place. Still, it is the qualitative dimension of Russian investments that impresses. Russian companies control the 4$^{th}$ biggest Lithuanian bank, approximately 25% of the retail fuel market, the Kaunas power plant, and stakes in the biggest gas distribution company. Russian company owns Mazeikiu Nafta. According to some experts as of 2001 some 30% of Lithuania's GDP were associated with the refinery (*Roe et al., 2001*). The importance of Mazeikiu Nafta in the Lithuanian economy is further underlined by the fact that in the year 2000 the company contributed almost a quarter of the country's gross tax revenues (*IBN, 2001*). The 5$^{th}$ biggest (in terms of sales volume) industrial producer is also owned by a Russian investor. That is if not taking into account the 839 joint Lithuania-Russian enterprises and 234 enterprises of Russian capital (*Miskinis, 2002*).

Therefore the importance of what corporate culture and business ethics Russian companies spread when they internationalise for Lithuania could be more than an academic elaboration.

A brief review of the main factors that assemble the contemporary Russian business culture provides with enough information to consider as the main concerns of Russian corporate culture abroad the unbroken dependence of Russian companies from the state, the attitude towards corruption and bribes and finally the productivity and efficiency issues. These concerns do not cover the entire spectrum of problem areas but could be considered as top priorities from country recipient of Russian investments point of view. The preliminary evidence based on the operations of three investors and four investments reviewed provides with an opportunity to draw several preliminary conclusions.

The unbroken link and dependence on the state is perhaps the most worrying particularity of Russian investors as their decision-making could be easily influenced / distorted by political considerations of the Russian state machine as opposed to economics-based decisions. While Gazprom is state owned, Yukos recent destiny shows that private companies in Russia are not secured even if efficient and transparent (as for the Russian conditions). Along the same lines Lukoil and MDM Group are in good standing with Kremlin but it is not possible to predict for how long.

In terms of attitude towards corruption and bribery it is not possible to collect credible evidence and provide clear-cut examples of such. Still, the Russian business environment for the last several hundred years and the fuzzy ways companies such as Yukos, Lukoil and MDM group were built in the 1990s suggests strongly that whenever opportunity exists to use bribery as a business tool, a Russian company will not hesitate to use it.

Finally the efficiency and productivity issues are less an area of concern, as it could be expected when observing the general situation in Russia in this respect. There is a clear distinction between the state owned Gazprom and the privately owned Yukos, Lukoil and MDM Group. In addition it also depends on specifics such as if the purchased company was restructured before the purchase etc.

The more important findings of this report are summarized Table 3.

Table3

| Assumption | Concern | Finding |
|---|---|---|
| **Russian investments start playing serious role in the Lithuanian economy** | **Still fresh from their Soviet experience, Lithuanian politicians fear that Russia is gaining economic power in Lithuania and the related to it greater opportunities of political influence.** | **Even though Russia officially qualifies as only 7th biggest investor in Lithuania, its investments are in key areas and indeed provide with great economic power.** |
| **Russian corporations form their business culture in Russia. To some extent they will utilize their business culture during their international expansion.** | **There are three main concerns highlighted from point of view of the country recipient of Russian investments.** | **These are:**<br>**- unbroken link of Russian companies with the state**<br>**- attitude towards corruption and bribing**<br>**- efficiency and productivity** |
| **- unbroken link of Russian companies with the state** | **No matter private or state owned Russian corporations depend on the state and thus could be used as leverages in the Russian foreign policy.** | **There is enough evidence to argue that this should be the biggest concern. Gazprom is directly controlled by the state. Yukos is privately owned but that did not help to be almost ruined by the state. Lukoil and MDM Group are privately owned and favoured by the state. But for how long? The dominance of Russian state over Russian companies (big and small, state owned or private) suggests that Russian companies could be used by the state as leverages of foreign policies.** |
| **- attitude towards corruption and bribing** | **Russian corporations were created in an environment where corruption and bribing were and to large extent still are within the rules of the game. Are Russian companies using bribing in their foreign operations?** | **There is no evidence to claim that the Russian investors observed in the paper used bribing in their operations in Lithuania. Still, as Russian companies use bribing on a daily basis in Russia, it is very likely that they will use any existing opportunity provided the country hosting Russian investments lacks the instruments to fight corruption.** |
| **- efficiency and productivity** | **If companies in Russia are plagued by inefficiency, poor management and low productivity, is there a danger that these could be brought to the Russian owned companies abroad.** | **There is no enough evidence to claim that Russian investments are bringing efficiency and productivity down. In fact, the observed cases in Lithuania demonstrate growth in earning and profitability after the Russian investors is present. Still this issue needs a more thorough elaboration as efficiency and productivity are result of more complex factors than simply ownership.** |

Still the main findings of this paper are based on mainly secondary sources of information and thus should be subject of critical scrutiny. A further study based on primary sources such as interviews and questionnaires will definitely help better understand the corporate culture Russian companies export together with their foreign investments.

However, even at this stage it is possible to provide some policy recommendations to decision makers. Combining Russian capital with the investment of established Western investors seem to be a better formula. It could guarantee transparent and efficient management, lessen the danger of using corruptive practices and block the danger of having politically based business decisions.

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