

PUBLIC ENTERPRISE SECTOR IN RUSSIA IN THE XXI CENTURY

Historically the State and State owned enterprises (SOEs) or public enterprises have always played a vital role in Russian economy. The bureaucratic management of SOEs in centralized planned economy (CPE) became a symbol of inefficiency. Since 1990s scholars have analysed the role of the State in CPE featured by monopolistic position of State ownership. In the 2000s Russian science mostly dealt with the transformation of the State's role in the country. After 2007, a new topic of State and private capital interaction emerged. Great attention is paid to SOEs activity in various branches of the economy.

The Government controls and creates enterprises to support infrastructure and high technologies. It also acts in sectors attractive for private capital due to rent income (oil and gas industries). High State's influence in Russian economy is not caused mainly by a legacy of the Soviet era. It rather stems from the reliance of public finance on income from natural resource extraction[†] and natural monopolies that remain under State control. The State intervention in management of business enterprises aims to provide for expansion of the State budget revenues.

There is no uniformity of clear common understanding of public enterprises and the estimate of their contribution to GDP. UNCTAD considers a company State-owned if at least 10% of its capital belongs to State or public entities, or if State/Public entity is the largest stakeholder. The Central Bank of Russia provides a more detailed definition. According to it, public enterprise sector covers 'the General Government, the Central Bank, and those entities in the banking and other sectors that are public corporations, i.e. non-financial or financial corporations which are subject to *control* by Government and the Central bank. Control is established (directly or indirectly) through ownership of more than half of the voting shares or otherwise controlling more than half of the shareholder voting power'. Therefore, public sector covers all the resources that State owns and manages. However, the criterion 'more than 50% of all equities (shares)' does not reflect the real State influence in decision-making process in joint-stock companies (JSCs). The share of the State in such entities can be less than 50% but the State can control the functioning of such enterprises.

The complicated composition of public (or quasi-public) enterprise sector in Russia hampers statistical evaluation of its contribution to GDP, especially after the creation of State Corporations

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[†] 43% of Federal budget revenues in 2015 were from oil and gas according to the data of Ministry of Finance of the Russian Federation.

(SCs), which formally do not belong to public enterprise sector. Difference in figures goes far beyond statistical errors and confirms the fact that there are different definitions of public enterprise sector.

1 The Size of Public Enterprise Sector

During the 1990s the State property shrank after large-scale privatization. One of the peculiarities of the 1990s privatization in Russia (in contrast to Central and Eastern Europe countries) was the absence of influential foreign investors. In 1991, the State accounted for 91% of fixed assets in the economy. By early 2001, this rate was 42%. Over 80% of enterprises were private. SOEs, which had produced 70% of GDP by the 2000s, belonged to private entities. Then, during the late 2000s, the trend has changed, as well as economic landscape. The number of employees in SOEs as a share of the economically active population was growing. This share was 24.6% in 2009; 24.9% in 2011; 25.7% in 2012 and so on. Such a trend reflects overall growth of the State influence after the Great Recession 2008-2009. Foreign scholars also notice the growth of State influence in the economy since 2005.

The Gaidar Institute for Economic Policy estimated the public sector share in GDP as 38% in 2006 and at more than 40% in 2008 (it means that the trend changed *before* the crisis). The Ministry of Economic Development estimated it at 45-50% in 2008-2009. The international average indicator then was 30%, such as it was in Russia in 1997. These estimates refer to all forms of State ownership, including shares in the largest companies (Gazprom, Rosneft); banks (Sberbank, VTB, other banks); SCs.

According to IMF experts, the public enterprises share in Russian economy is considerably higher. It accounts for the revenues of at least 71% of GDP. Public enterprises have an extensive balance sheets with assets amounting to 381% of GDP, more than half of which (200%) belongs to sub-soil assets. The estimates of IMF seem to be more accurate and plausible. At the Panel Discussion as a part of the Gaidar Forum (GF) 2016,[‡] very different figures on public sector enterprises in GDP in 2015 were declared, including 70% of GDP at the highest. It means that for the last decade this figure doubled (in 2005 – 35%). Even in China, with its specific economic model, this figure is significantly lower (45%).

A build-up of State interference in the economy began even before the Great Recession. In 2000s the State began to regain its positions; the model of ‘State capitalism’ began to form. In this context Russian economy at first sight can be compared with the French one, which ‘Statist liberalism’ tried to embrace both the State’s leading role in economic policymaking and a substantive (but constrained) liberal vision of the content of economic policies.

The State in Russia began to dominate again in some strategic sectors (such as oil and gas industries) through large companies, banks with State participation and SCs. The ‘Concept of long-

term socio-economic development of the Russian Federation until 2020' sets forth the recognition of the important role of public enterprises, mainly in industries related to defense, national security, and infrastructure (the latter is typical for any country). Public enterprises strengthen their role in key sectors, even amid the formal reduction in number of SOEs, especially of Federal State Unitary Enterprises (FSUEs). The State declares the ambitious goal to develop new industries and to modernize the existing ones. On the one hand, some Russian researchers depict the evolution of public enterprises in post-Soviet economy in the form of U letter. On the other hand, the pace of creation of new enterprises with State participation in capital is comparable with the pace of privatization.

Table 1

Public enterprise sector share in the economy, %

Indicator	2007	2010	2012	2013	1st half-year of 2014
Volume of shipped own produced goods, works performed and services rendered:					
- mining	12.8	9.8	16.5	21.6	22.4
- fossil fuel production	11.8	9.0	16.6	22.1	22.5
- manufacturing	8.4	8.7	9.8	12.0	12.5
- production and distribution of electricity, natural gas and water	11.4	17.8	25.7	25.0	19.2
Communication services*	9.8	15.2	14.2	13.7	13.2
Gross-fixed capital formation	19.5/	24.5/	28.8/	30.3/	25.6/
From all sources of finding**	15.0	17.8	20.9	21.0	19.2

* Net proceeds from sale of goods, products, works and services (less VAT, excises and other similar mandatory payments)

** The denominator does not include the small-sized entrepreneurs and the volume of investment, which cannot be estimated directly on the basis of available statistical reports.

Source: Russian Economy in 2013, 2014 Trends and Outlooks (Iss. 35, 36). Gaidar Institute for Economic Policy, edition 1, volume 35, by S. Sinelnikov-Mourylev & A. Radygin & L. Freinkman & N. Glavatskaya, Moscow: Gaidar Institute Publishers, 367, 346.

Table 1 data reveal a significant increase of public enterprises share in mining (including fuel and energy production), electricity, gas and water production and distribution as well as in gross fixed capital formation. The share of public enterprises in oil and gas industries expanded in the 2005-2008s (before the Great Recession) from 32 to 47%. However, these estimates do not seem complete. The SCs are not included in the calculation but they are to be in the list. They are subject to direct or indirect control by the State.

Consolidation of SOEs and enterprises with mixed capital into large State-controlled holdings became ubiquitous (nuclear; defense; rail, air and sea transport etc.). Large-scale public enterprises may take the form of joint-stock company (JSCs), as well as that of unitary enterprises – Federal State Unitary Enterprise (FSUE) and Municipal Unitary Enterprise (MUE). State Unitary enterprise is 'not

† Such a topic as a separate discussion symposium appeared in the Program for the first time since the creation of GF in 2010.

endowed with the right of ownership to the property, allotted to it by the property owner'. Such enterprise belongs on the property law right of the Russian Federation (RF), to the subject of the RF or to municipality. The Federal Agency for State Property Management ('Rosimushchestvo') on behalf of the State exercises the 'power of the owner', including privatization.

As of 2016, March 1 there were 1 178 FSUEs. Government considers this form of property inefficient. By 2018, all FSUEs are to be closed down according to the plan, but it is highly uncertain, given the scale of the privatization (about 60 FSUEs annually). There is a risk of missing the target of the State program of the RF on managing of the State property (the absence of FSUEs by 2018, according to the Accounts Chamber). Moreover, Ministries and branch departments urge to conserve 155 FSUEs. During 2015, the number of enterprises that branch departments propose to transform into Federal State institutions (FSIs) and Federal Treasury enterprises (FTEs) had jumped from 79 to 247. This would not contribute to the reduction of the public enterprise sector and could entail additional burden for the State budget.

At the beginning of 2000s the State was a stakeholder in 3704 JSCs, in 75 FTE and in almost 10000 of FSUEs. It also possessed of property of over 37000 Federal State institutions (FSIs). In 2008, the number of FSUEs was 9864, and we can observe the fall of this number to 4236 by 2014. The number of business enterprises with State participation has slightly grown from 5019 to 5226 (Table 2).

Table 2

Number of Russian economy public sector enterprises in 2008-2014

Date	Federal State unitary enterprises	Business enterprises which 50% of the shares are:	
		in the direct public ownership	in the ownership of business companies that are parts of the public sector
As of 1 July 2008	9864	3930	1089
As of 1 July 2009	8706	4007	1350
As of 1 July 2010	7230	3915	2229
As of 1 July 2011	6245	3928	2391
As of 1 July 2012	5282	3593	2327
As of 1 July 2013	4589	3201	2241
As of 1 July 2014	4236	2988	2238

Source: compiled from: Russian Economy in 2013, 2014. Trends and Outlooks; Kuzyk M., Mal'ginov G., Radygin A., Simachev Yu., Shmeleva N. (2011).

According to the data from the Federal State Information Systems Operator Single Federal Property Management System (FGIAS ESUGI) presented in the Report, as of 2015, August 1, the Federal Property Register contained information on 1864 JSCs with State participation (in Federal ownership). This data include those 103 JSCs where the State held the special right to participate in a company's management granted by 'golden share'. 'Rosimushchestvo' could fully exercise its stakeholder power in only 980 JSCs out of 1864 JSCs (or only 52.6% of all JSCs vs. 54.7% as of

summer 2014 and vs. 57.7% as of summer 2013). However, during the same period, one of the low-level OECD indicators ‘Direct control over enterprises’ almost doubled: from 1.64 to 2.87 (range 0-6 in which the indicator normally varies). High-level officials (including Ministers) are made incorporated as members of the Boards of directors of the State-controlled companies and the direct control over enterprises is growing.

Experts of the Gaidar Institute for Economic Policy argue that the movement of the public sector of the national economy in 2016 cannot be estimated more or less accurately for lack of necessary statistics. The switchover to a new methodology of accounting is to blame for the trouble with the statistics.

2 *Public Enterprises by Industry and their Efficiency*

The necessity of national enterprises belonging to public sector in Russia is based on its political, defence and social functions. It is especially relevant for such a special form of State participation in the economy as State corporations (SCs) which have low economic efficiency combined with the major role in the national economy.

In 2013, the average of SOEs shares of sales, assets and market values among the 10 Top Russian companies ranked by revenue was 80%. The share of SOEs in the RTS index is nearly 50%, while the share in total revenues in the economy is 46%. The role of small and medium enterprises (SMEs) is low. Only 25% of Russian employees work in SMEs against 50% on average in OECD countries. This situation is mostly due to domination of SOEs, urgent need to improve the business climate, complicated access to financing and unstable taxation rates. Such problems affect economic growth and economy efficiency in Russia.

Public enterprises sector in Russia covers traditional spheres of State presence – infrastructure (except telecommunication) and defense industry. The State has the dominant position in transport, primarily through RJD (Russian Railways) and Aeroflot. RJD (100% of State capital) controls railways; Gazprom controls gas trunklines; Transneft controls oil pipelines. Railway transport, gas and oil pipelines dominated by SOEs account for more than 90% of all Russian freight turnover.

The State controls production of ships, aircraft and spacecraft. This field of activity is on the second place in terms of so called ‘Statification’. This situation is due to the domination of leading companies controlled by the State: United Aircraft Corporation (UAC); United Engine Corporation (UEC), and by strong position of the State in the major shipbuilding enterprise – United Shipbuilding Corporation (USC).

The similar situation is in natural gas extraction. The State owns more than 50% of Gazprom shares. Meanwhile Gazprom not only extracts around 80% of Russian gas, but also is a monopolist in its export.

The high share of the State in electric power generation is due to its strong positions in the energy heavyweights of Moscow region. For example, Gazprom owns 53.5% in MOSENERGO, the largest regional generating company in Russia. The State is a shareholder in Federal government Agencies (Federal Grid, RusHydro, Inter RAO, Rosseti). Rosseti (85.31% share of State capital) in turn owns controlling stake or large blocks of shares in most of the regional electricity companies (for example, in Moscow United Electric Grid Company, MOESK – 50.9%).

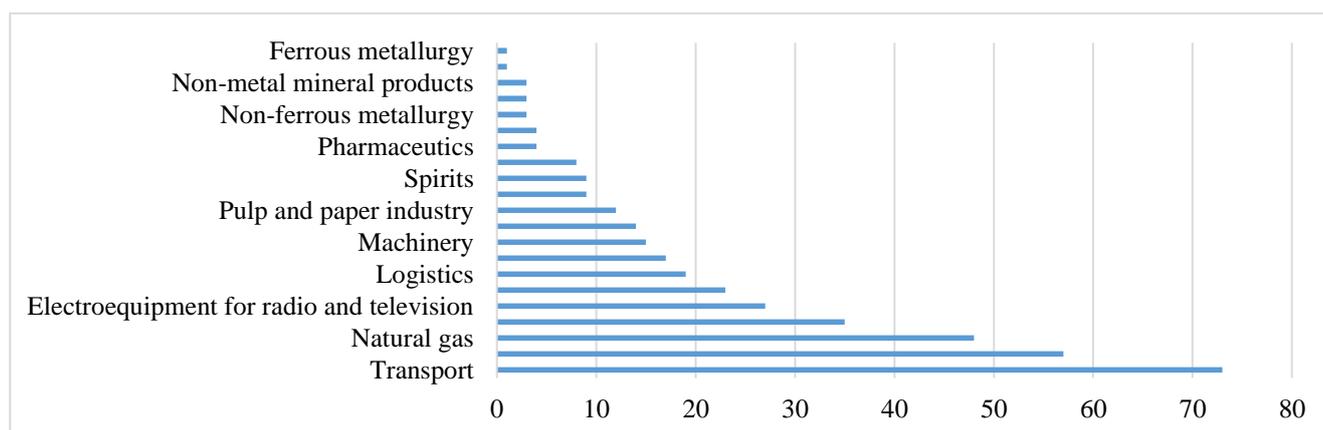
The situation in the production of electronic components, equipment for radio and TV (27%) reflects strong positions of a number of SOEs of military-industrial complex. The State's share is considerable in cargo handling and transport organization.

We can observe consolidation of actors and internationalization of capital in Russian infrastructure due to globalization. The State exercises control in oil extraction through the equity stake in Rosneft and Gazprom Neft. These two companies represent the State also in refining. The State's role in refining capacities of Rosneft and Gazprom Neft as a share of total production accounts for about 19%.

There are also other estimates. SOEs controlled more than 52% of oil production in 2014, while the share worked out at 40–45% in 2012 and less than 10% at the end of the 1990s. 35% of the State share in oil production came from Rosneft. State is virtually absent in the coal-mining industry, but it controls energy sector, which consumes half of the country's coal. In other industries, the share of the State is insignificant. The rating of State participation in some key business sectors is in Chart 1.

Chart 1

Rating of State participation in some key business sectors



Source: Rossijskaja business gazeta. Available at: <http://www.rg.ru/2011/06/28/biznes.html>

As can be seen, the State prevails in high-tech branches, connected with defense and national security sectors (such as airspace), as well as in oil and gas industries and transport (infrastructure). Private businesses have dominant role in such branches of manufacturing, as pharmaceutics,

electronics, telecommunications and some others. In developed countries, these branches are main drivers of R&D and economic growth. However, in Russia net revenues (after taxes payed) of these sectors are relatively small compared with oil and gas industries.

As to the efficiency of public enterprises, it is to be accounted not only for their commercial performance, but also for their role in the national economy performance. Expert estimates of comparative efficiency of public and private enterprises are contradictory. Some experts claim the absence of public enterprises among the top working efficiency leaders. In some cases, public enterprises operational efficiency was 30% of the industry average. However, the leaders in the ranking of new high-performance, capital-intensive jobs creation are public enterprises – Gazprom, Transneft, Rosenergoatom, Inter RAO. The North Stream pipeline declared by the EC to be a part of the EU TENs, for example, created such jobs.

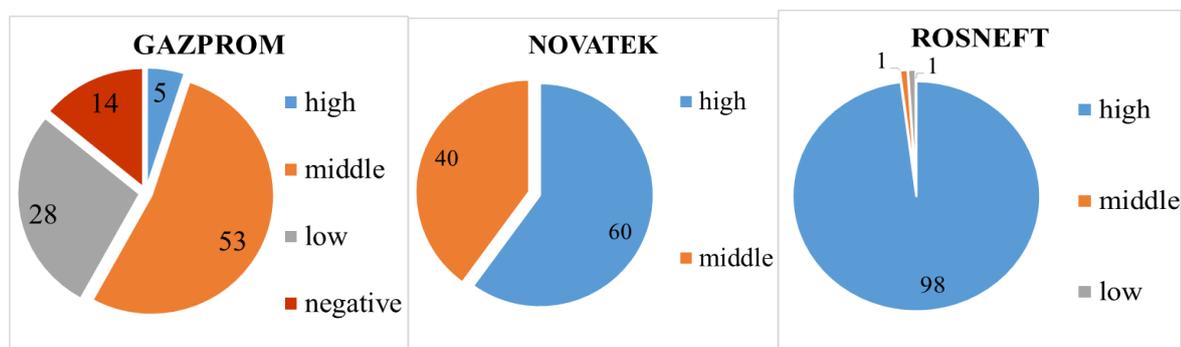
In advanced market economies, the growth of labor productivity and efficiency is largely due to market competition between enterprises on the domestic market and to the professional skills of corporate governors or the quality of human capital. Russian SOEs have more financial stability than private enterprises, but significantly less efficient on human capital return. Such situation can be explained by distorted competition. Contrary to popular opinion on the management and production inefficiencies of SOEs (compared to private ones), there are some expert estimates, that modern State unitary enterprises in Russia have successfully adapted to market conditions. They demonstrated performance comparable or even superior to that of the private sector. In our opinion, such performance in Russia is partly due to various non-economic and administrative factors.

A similar estimates of good performance of public enterprises based on CEEP statistics and our calculations on public enterprises in the EU, relate to entities competing as equal with business enterprises. As to natural monopolies, in some cases their privatization may be even harmful.

We can accentuate that it is incorrect to estimate public enterprises efficiency according to financial indicators only. According to financial statements of gas-and-oil industry *Return on Equity (ROE)* of Gazprom was 7.71% (2015) and that of the private Novatek – 26.8% (2014). The cause of such a lag of Gazprom is the high maintenance costs of pipeline system and large social responsibility (Chart 2).

Chart 2

Gas supply structure by Returns on Sales (%)



Source: 'Oil and Gas Vertical' (Neftegazovaja vertikal'). 2015. No 1, p. 71.

Higher yields of Novatek and Rosneft is due to their natural gas supplies to industries, unlike Gazprom, that is the supplier to housing and utilities. By the way, there is less difference in ROE between public Rosneft – 12.2% in 2015 (11.5% in 2014 and 20% in 2013) and private Lukoil – 9.3% in 2015 (13.9% in 2014 and 26.18% in 2013).

3. Russian phenomenon of State Corporations

State corporation were initially created in the 1970-s in Asia. Such a policy first found its successful realization in Singapore. SCs as a 'coalitional form of interaction between State and market' represent the first stage of innovational economy formation, when the model of 'catch up growth' prevailed along with vast import of technologies.

The State in Russia created vertically integrated structures, SCs, since 2007, to fulfill long-term strategic goals in specific economic spheres. The purpose was to shift from the raw material export-oriented model to modernization and development of manufacturing industries competitive in the world market. By 2016, such an aim has not been achieved.

The experts are looking for a new form of State participation in the economy, which faces certain difficulties. Legal contradictions in Russian SCs functioning are due to the lack of clear theoretical view on the ratio between private initiative and State activities.

Table 3

List of State Corporations

State Corporation	Federal Law
Deposit Insurance Agency	N 177-FZ of December 23, 2003 'On Insurance of Deposits of Households in Banks of the Russian Federation'
Bank for Development and Foreign Economic Affairs, Vnesheconombank	N 82-FZ of May 17 2007 'On Bank for Development'
Russian Corporation of Nanotechnologies,* Rusnano	N 139-FZ of July 19, 2007 'On the Russian Nanotechnology Corporation'
Fund of assistance to reforming housing and communal services	N 185-FZ of July 21, 2007 'On the Fund of assistance to reforming housing and communal services'
State Corporation on Construction of Olympic Venues and Development of	N 238-FZ of October 30, 2007 'On the State Corporation on Construction of Olympic Venues and Development of Sochi

Sochi as Mountain Climatic Resort, Olympstroy**	as Mountain Climatic Resort Olympstroy'
State Corporation for Assistance to Development, Production and Export of Advanced Technology Industrial Product, RosTec	N 270-FZ of November 23, 2007 'On the State Corporation for Assistance to Development, Production and Export of Advanced Technology Industrial Product RosTec'
State Atomic Energy Corporation, Rosatom	N 317-FZ of December 1, 2007 'On the State Atomic Energy Corporation Rosatom'
The Federal Space Agency Roskosmos	N 215-FZ of July 13, 2015 'On the State Corporation for Space Activities Roskosmos'

* Re-registered as Joint-stock company since the 11 March 2011.

** liquidated on the basis of the Federal Law N 210-FZ of July, 2014.

There is a certain misunderstanding concerning the definition of SCs in Russia. For example, IMF experts claim that there are around 300 Government corporations established under specific legislation. SCs (each established under a special Federal Law) play different roles in the economy. SCs in Russia are legally defined as non-profit organizations and their activities involve the implementation of Government policies. The list of SCs includes now only 7 (Table 3). The rest 294 companies by law are not SCs *per se*.

Each Russian SC is in fact a monopoly without real competitors in the internal market. Enterprises of sectors where SC exists are forced to merger with it or to reshape. SCs possess such broad rights that neither private nor public companies have. However, SCs incur risks of expanding the 'shadow lobbying', *ad hoc* decision-making.

SCs have some features not typical for private nor public companies.

a) SCs are different from private enterprises: SCs have limited powers to dispose of their income and property; SCs are different from State unitary enterprises – SCs have more powers to dispose of their profit, to rent their property.

b) SC property is *derived from public ownership* and from application of the Federal Law N 127-FZ (dated 26.10.2002 and amended 29.12.2014) 'On Insolvency (Bankruptcy)'. *The real responsibility* for the safety and effectiveness of functioning of the property that SCs received from the State *gratuitously* lays on the *Government* (State) who forms some of their key activities.

c) SCs are exempted from a number of forms of State control, provided by the Federal Law dated 12.01.1996 N 7-FZ (amended 06.04.2015) 'On Non-commercial Organizations'. The SCs activity is not enough *transparent*. The lack of effective monitoring of its effectiveness and budget-spending leads to an increase of burden of wasteful production with low-impact factors, as it was in the late Soviet economy.

We emphasize that the market economy managed by *ad hoc* administrative methods ('manually operated Model') does not create a competitive economy. Inevitable consequence of the excessive State interference in business is 'the growth of bureaucracy and wastefulness, the economic slowdown

and the threat of stagnation'. The SCs contribute to the State-monopoly character of the 'State capitalism' model and distort market competition in Russia, which is already poor.

It should be noted however that SCs as well as major public enterprises could finance expensive R&D and support PPP (with participation of SMEs). SMEs are to produce components for large companies, to master the output of new products, to use advanced technology. SMEs show high international competitiveness 'in narrow niches'. The State should give an initial investing impetus to modernization, to large strategic investment projects in market conditions based on PPP. FDI attraction and support are also important, but the degradation of business climate, entailing an outflow of capital, makes the economic development bet on the State at Federal and Regional level.

Overall, the growing State intervention in the economy – 'Statification', even in the form of JSC, aimed at the economy modernization and transformation, has few tangible results. Excessive State intervention becomes an obstacle for economic growth. However, authorities' privatization programs are often adjusted or downsized. In 2011-2013, the ambitious Privatization plan was scaled down due to unfavorable market and general business conditions. The stipulated in the 2014-2016 withdrawal of the State from non-oil sector companies not related to the natural monopolies and the defense industry did not take place. The State did not leave the capital of non-commodity sector companies that do not belong to natural monopolies and defense, as it was planned for the period of 2014-2016.

Some enterprises from this Plan were included into the 'The Forecast Plan of privatization for 2014–2016'. The privatization is to increase Federal budget revenues. The main object of privatization is Rosneft State share (19.5%) at the price not lower than that of the first IPO. Such a stipulation in current economic situation makes Rosneft privatization highly dubious. In addition, State shares in Russian Railways, Bashneft, Sovkomflot (each 25%) as well as Alrosa (19%), Bank VTB (10.99%) and Aeroflot (10%) are to be privatized. The first big deal in 2016 after a long break in mass privatization was Alrosa. 10.9% of Alrosa shares were sold by the State in July, the rest 8% are to be sold in 2017.

The Privatization Plan for 2014-2016 originally provided for privatization of 992 companies, 522 FSUEs. In 2014, the Plan of income from privatization was implemented by 168%. The revised Privatization Plan for 2014-2016 (as of the 1 January 2015) has 2 sections. Section I includes 21 JSCs. Section II includes 981 JSCs and limited companies (Table 4); 535 FSUEs; 294 real estate entities.

Table 4

Operations of the Forecast plan (program) of federal property privatization for 2014-2016

Operations	31.12.2014	31.12.2015
Included in the Privatization Program	981	977
Sold the previous year	0	107
To be sold	773	513

sold	107	103
To be privatize next year	666	410

Source: The Report on the implementation of the Forecast plan (program) of federal property privatization for 2014–2016 in 2015. P. 23.

The Plan of privatization is ambitious, but dubious. The goals for 2014 has been over-fulfilled, the realization of plans for next two years had been delayed. The Plan that provided for State's share reduction in Transneft from 78.3% (equals to 100% of voting shares) to 75% plus one share is permanently postponed since 2013. Rostelecom privatization was also delayed.

Conclusions

a) Russia faces a number of serious problems: lack of comfortable conditions for the prosperity of SMEs, the existence of non-economic impetus (connected also with widespread corruption). The real influence of public enterprises in Russian economy is so dominant, that any discussion on its future means the choice of the economy's development way.

b) The Russian economy revealed a 'Renaissance of Statification' in 2001-2016, long before the Great Recession. State participation in business is growing in Russia in respect of the share in output as well as of that in employment. The role of public and mixed enterprises (with State participation) in the economy continues to grow despite of declared privatization plans. Only formal decline in number of FSUEs and MUEs as well as of the transformation of State entities into shareholding forms took place.

c) The reaction of the people to the privatization of the 1990s as 'unfair' has some reason. According to the public opinion, the privatization was the main cause for a profound increase in income inequality and for the emergence of a few over-rich people ('oligarchs'). Such public mood trends influence any future privatization plan in Russia even now.

d) The performance of the public enterprises may be better that of the private one. The high share of their profits in the Federal budget income may be explained by the domination of public enterprises in Russia in oil and gas industries. Oil and gas industries are more profitable than manufacturing. That problem in the developed countries is solved by taxation policy. The volume of public sector in the developed countries is preordained by public services volume and by its significance for industrial policy. The State in Russia is always present and attentive to the problems of profitable branches, and not to those, where private enterprises are really in need of State support by means of slashing income tax rates. SOE-s fulfil in Russia specific political and social functions.

e) SCs in Russia are declared as the means to transform the economic model of the country from raw material export-oriented into the diversified one. Sanctions against Russia have given a new

impetus to follow this way. The raw material export-oriented model and low efficient and imbalanced fiscal system are named among the major threats to the national security in the renewed 'Strategy of National Security in the Russian Federation until 2020'.

The expansion of the public enterprises influence in Russia actually undermines and distorts the efficiency and competitiveness. The development of the economy by administrative means is rooted in Soviet times (so called 'vertical of power'). It is contrary to the nature of market economy that has proved its superiority over the centralized planned one.

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