

## Russian Privatisation Plans Hindered by Government's Grip on Energy Sector

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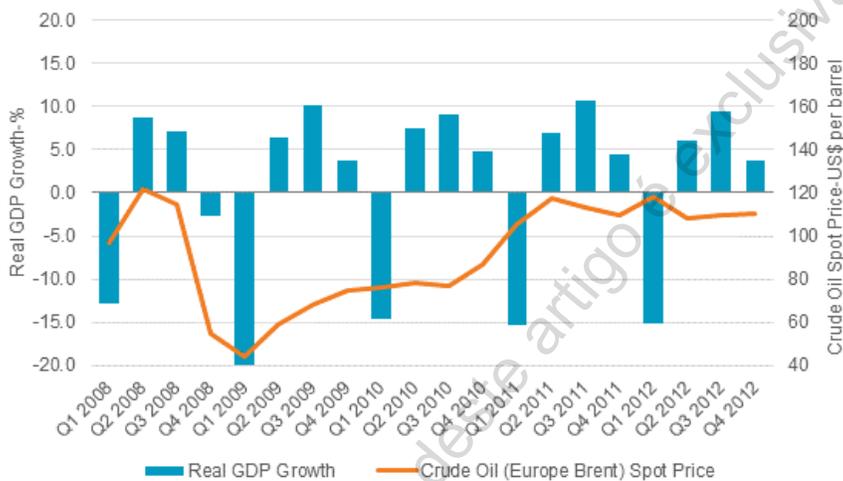
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For a country which rivals China in terms of state involvement in commercial activities, it has come as a surprise to many that Russian President Vladimir Putin is pursuing large-scale

privatisation plans so vigorously. In January 2013, President Putin announced plans to privatise the majority of state-owned enterprises, except for those in the energy sector, in a bid to reform the country's financial markets and kick-start economic growth. These newest privatisation reforms are aimed at fostering investor interest in the country and making it a better place to do business. However, the government's reluctance to let go of controlling stakes in the energy sector reveals a lot about its motives for privatisation and while the private sector may expand, the public sector will still be its key player.

*Russian Quarterly Real GDP Growth vs. Europe Brent Spot Price: Q1 2008-Q4 2012*



Source: Euromonitor International from national statistics/Eurostat/OECD/UN/International Monetary Fund (IMF), World Economic Outlook (WEO)

Note: Real GDP Growth is quarter-on-quarter

### Privatisation needed to lure investors

This privatisation plan is a further step in [Russia's goal of jumping over 88 places to 20th](#) in the World Bank's Ease of Doing Business Ranking by 2018, from its spot at 112th out of 185 economies in 2013.

Foreigners are notoriously cagey about investing in Russia, as are many Russian investors themselves, and with good reason. The level of state-control over the economy's key industries is off-putting thanks to never-ending red tape and high levels of perceived corruption. Putin wants Moscow to be seen as a global financial hub to rival London, primarily

as the London Stock Exchange is the market of choice for Russian companies. The Russian economy is struggling with capital flight issues and it is hoped that by allowing private investors to own larger stakes in key industries such as rail, airports, agriculture and telecoms will encourage money to flow into, rather than out of, the economy. [Foreign Direct Investment](#) (FDI) inflows fell by 16.1% in real terms in 2012 in Russia, having fallen by 37.4% between 2007 and 2012 in real terms. It is hoped this trend will be reversed when investors, both foreign and domestic, can hold greater equity stakes in Russian industry.

**Government's tight rein on energy sector keeps oil prices high and market uncompetitive**

However, the fact remains, energy is the country's single greatest revenue stream and its most important industry. In 2012, oil exports accounted for 55.7% of all Russian exports and 14.7% of total GDP. The energy sector is the backbone of the Russian economy but the government's controlling stake has prevented both domestic and foreign investors from creating a competitive industry and make energy prices fairer.

As the second largest oil producer in the world in 2012, the Russian government claims to be trying to diversify the economy and reduce its dependency on energy but the fact that it's the one industry the government refuses to privatise would ultimately suggest otherwise. In late 2008 when oil prices fell dramatically, it had a greater impact on the Russian economy than the global financial crisis of 2008-2009. Real GDP growth in the country is intrinsically linked to oil prices and any further decline or shock in oil prices will negatively impact the country's economic prospects. Oil prices globally are expected to decline steadily over the medium to long term as countries search for alternative energy sources and new technologies such as fracking precipitate "oil booms" in places like the USA and Western Europe.

This isn't the first time Putin has tried to use privatisation as a means to bolster economic growth, having launched similar plans in 2010 and 2011. While this most recent plan does appear to be more far-reaching given the fact that it's tied up with plans to overhaul the country's financial sector, the government's refusal to loosen its grip on the energy sector will ultimately hinder any significant economic growth in the Russian economy in the long-term.

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