Corporate Governance: Does the concept work in transition economies?*

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The paper evaluates the feasibility of employing mainstream models of corporate governance in the context of transition economies, using Russia as an example. The issue of corporate governance is considered as an element of an institutional crisis characteristic of post-communist countries. It is maintained that the stakeholder approach provides the closest fit to the realities of corporate governance in a country like Russia.

Dieses Papier untersucht die Möglichkeit der Anwendung von Normalmodellen der Unternehmensführung im Kontext der Volkwirtschaften der Reformländer mit besonderer Bezugnahme auf Rußland. Das Gebiet der Unternehmsführung wird als ein Element der institutionellen Krise in den post-kommunistischen Ländern erachtet. Es wird argumentiert dass der "Stakeholder" Ansatz am ehesten den Realitäten der Unternehmensführung in Ländern wie Rußland enstpricht.

Keywords: Institutional economics / corporate governance / transition / Russia / post-communism

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* Manuscript received: 28.8.02, revised: 21.2.03, accepted: 17.4.03.

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Introduction

References to corporate governance issues in literature on transition economies have become commonplace. Unfortunately, the concept and terminology are often used quite loosely. The absence of any real consensus on the definition and scope of corporate governance in transition economies damages the cognitive value of the ongoing discussion. This paper has an objective, using Russia as an example, to encourage the pursuit of clarity and consistency in applying the conceptual framework of corporate governance to transition economies.

To fulfill this purpose the paper suggests that the issues of corporate governance should be looked upon in a wider context of an institutional build-up as it is a reflection of political, cultural, social and economic circumstances particular to place and time. The paper begins with considering factors that influenced the development of the attitude to corporate governance in post-communist countries as a concept in 1990. It is claimed that the investigation of corporate governance suffered as a result of, first, the tendency to apply theories without essential adaptation to the realities of transition and, second, unwarranted analogies with mature market economies. The paper provides examples of certain conceptual inertia in the literature on transition economics that reveals itself through emphasising commonalities at the expense of variation. The paper concludes with proposals regarding the introduction of a new paradigm intended as an adequate conceptual image of the Russian corporate landscape.

The Concept of Corporate Governance and Post-Communist Transition

Institutions and Market Reforms

Two constituents of post-communist reforms, privatisation and liberalisation, have made the issues of corporate governance a very active area of research. In Russia at the start of reforms both were seen as key elements responsible for an early success of transition. Privatisation in particular was conceived by the architects of reforms as a crucial step towards achieving greater efficiency in the application of resources by way of creating “effective owners” (Chubais/Vishnevskaya 1993). These were seen as a driving force that would assure the more effective employment of assets necessary to prove the superiority of the market mechanism of resources allocation over central planning. In reality improvements in overall economic efficiency have been slow to materialise on the scale originally anticipated. As macro-economists were struggling to offer an unequivocal explanation of events it was not surprising to see concepts developed within managerial and organisational theory being increasingly put to use in transition studies. Under these circumstances the investigation of corporate governance structures has emerged as a promising avenue of research with potentially very serious practical implications.

This follows the growing realisation in literature on transition that the three macroeconomic pillars of the shock therapy applied in Russia and many other post-communist counties - privatisation, stabilisation and liberalisation – will not work in the absence of a particular institutional environment. In the terms of the new institutional economics institutions represent the rules of the game in the society or, more formally, they are the humanly devised constraints that shape human interactions.[1] Institutions equip economy with an infrastructure that is necessary to promote, support and simplify market exchanges. This can be achieved by establishing the ambience of stability and continuity that helps to check the extent of informational asymmetry damaging for the market.

The national system of corporate governance as reflected in norms and provisions required to raise external finance is an important element of the institutional set-up in any country. It has the task of providing means that help to institutionalise, i.e., regulate according to certain established rules, economic conflict between investors in companies and managers, facilitate information flows and procure a solid and cost-efficient foundation for the growth of publicly-held corporations (see North (1990) for the fundamentals of the new institutional economics and World Bank's 2001 World Development Report for the role of institutions in economic growth).

Perceived as an institution, corporate governance transcends the issue of the allocation of control in a corporation. An institutional framework is a major contributor to a mechanism that allows market signals to develop and reach economic agents in a meaningful form. In this sense corporate governance is as important a link between financial and product markets and the firm as competition or prices[2].

In modern Russia institutional arrangements are not only generally weak, but inconsistent and incomplete (Cornia/Popov, 2001, Kolodko, 2000). They reflect the drawbacks and weaknesses associated with a period of systemic change such as domination of short-term interests, poor access to business information, lack of trust, collapse of traditional business ties, poor law enforcement, etc. It is quite clear that in their present form these arrangements have reached their

[1] This is one of the more expanded definitions of an institution by Aoki (1998): an institution is a stable, substantive characteristic of socially-constructed states of a sub-economy which constrains agent's action choices through the convergent expectations it generates, while enabling them to economise on information processing, provided that there can be another such constraint for the same class of environments.

[2] See Nickell et.al. (1996) on corporate governance as substitution for competition.

limits and become a barrier to further development (Kuznetsov/Kuznetsova, 2002). In this context the analysis of corporate governance in Russia cannot help but getting concerned with the task of identifying the optimal pathway for the development of a modern system of corporate governance adjusted to realities of the country. This, in our opinion, is proving to be a considerable theoretical challenge exacerbated by some characteristics of the concept itself as well as the peculiarities of the Russian economic transition. Below we look at two issues that have had impact on the development of the corporate governance concept in relation to contemporary Russia.

Conceptual Choice: Evolution versus Adaptation

The adjustment of the theory of corporate governance to Russian conditions involves overcoming certain difficulties. To begin with, Western practice has to offer more than one proven model of corporate governance. Typically in literature we find references to at least two alternative models, American (also known as Anglo-Saxon or market-oriented system) and continental (also known as Germanic or network-oriented system), although it is becoming increasingly common to identify further models these days.[3] At this stage the important thing to notice is that no matter how scrupulous we want our list of available patterns of corporate governance to be, each individual system has evolved in the course of an evolutionary process in response to the requirements of a particular national environment. For instance, Potthof (1996) brings forward the historical roots of dissimilarities between Anglo-Saxon and German systems. In the 19th century German banks were looking for ways to transform their short-term assets into long-term but they were not interested in managing firms. Therefore the German system emphasises supervision, but not management, by banks of joint-stock companies. By contrast, in Britain and the US capital was scares. Risk-taking individuals wanted more control over their assets and hence demanded extended authority in respect of managers. As a result, the system that developed in Britain and the US put emphasis on the responsibility of managers before shareholders while in Germany on their responsibility before the law. In turn, LaPorta et al (1997) give precedence to a legal framework as the cause of variation in corporate systems, establishing a link between market-oriented model of corporate governance and the dominance of common low in

3 Jong (1997) writes about the Anglo-Saxon, the Germanic and the Latinic types of corporations with the latter represented by firms in France, Italy, Spain, etc. Yoshimori (1995) conducts his discourse in terms of monistic, dualistic and pluralistic concepts of corporation. The first exists in the US and the UK with a focus on shareholders; the second is characteristic of Germany and France and put a premium on the interests of both the shareholder and employees. Japan is the home for the third concept that assumes that the firm belongs to all stakeholders.

Britain and the US, on the one hand, and the network-oriented model and civil law in continental Europe, on the other.

The fact that national systems of corporate governance are products of historical circumstances, i.e., that they have been influenced by cultural, political and socio-economic factors specific to age and nation, has important consequences in countries like Russia. When market reforms started in Russia, no experience and no ready concept of marketisation were available within the country. As a result theoretical underpinnings of reforms had to be imported wholesale from the West. This created a number of immediate and long-term problems related to adaptation and interpretation of utilisable concepts and the evaluation of the consequences of their implementation in Russia. In an ideal world we would expect the decision-maker to choose the best of accessible models. In reality, such a choice, even for a politically unbiased, rational and educated decision-maker, presents probably insurmountable difficulty.

Multinational literature on corporate governance provides an ample score of examples of the relative nature of what different authors tend to see as best arrangement for a corporate system. Their conclusions usually depend on criteria applied, time of writing and often nationality. Not surprisingly, the debate around this issue has been quite vigorous for a long time and shows no signs of recess. Considering the magnitude of discussion we shall perforce satisfy ourselves with just few illustrations, demonstrating that lack of consensus in this area is not incidental. Jong (1997) compares the Anglo-Saxon and Germanic systems. He attacks increase in shareholders' wealth as a criterion of efficiency of corporate governance and instead proposes to look at net present value. Following this methodology, Jong concludes that the German system with its bank and employee orientation is superior and secures higher average growth and productivity. Yoshimori (1995) and Moerland (1995) debate comparative advantages of the US and Japanese systems. In certain respects, in particular the nature of relations between largest banks and largest corporations, the latter is not dissimilar to the Germanic concept. Both authors nominate the existence of intimate and long-term relationship between firms and strategic capital suppliers as a relative strength of the Japanese model. This position, however, had to be revised in the light a major recession that struck Japanese economy in the 1990s. It has been attributed *inter alia* to the "special" relationship between banks and corporations that caused investors to delay bankrupting inefficient clients thus contributing to the crisis.[4] These developments might have been interpreted as a vindication of the Anglo-Saxon system with its emphasis on openness, transparency, short-termism and shareholder. However, the prestige of American corporate governance has suffered an enormous setback following the ENRON and other scandals that

[4] See "The Slow Death of Japan Inc.", *The Economist*, Oct. 14th 2000, pp.140-143.

revealed that the interests of shareholders had been persistently ignored on a great scale and boards of directors had been quite helpless in preventing wrongdoing by managers. Despite the shocking nature of these events they have not turned a page in the analysis of corporations: since as early as 1970s there has been a strong school of thought in the US, amassing evidence that the Anglo-Saxon system of corporate governance in its current form lacks instruments necessary to reduce the opportunism of managers (Williamson 1985, Milgrom and Roberts 1992, Hart 1995).

These examples make evident that every system has its pros and cons but, as Moerland (1995) infers, it is impossible to say that one system is better than the other on theoretical grounds as the optimisation of economic organisation leaves room for multiple configurations. This claim is echoed by Rozman (2000) who, having compared Anglo-Saxon and Germanic systems, reaches a conclusion that both systems are logical and in harmony within themselves despite being different. These outcomes are not surprising in the light of what was said about the origins of national systems of corporate governance earlier, i.e., that their variety is rooted in the nation-specific circumstances of their development. It is not incidental therefore that the process of globalisation has provided a backdrop for some signs of convergence of corporate systems throughout the world although, without doubt, the parallel existence of alternative concepts will continue in the foreseeable future.

Non-economic Factors and Theoretical Bias

First publications dealing with various aspect of corporate governance in modern Russia appeared almost as soon as privatisation was launched. However, initially little interest was shown in studying the developments in the Russian corporate sector in their own context. From the outset the American model had established itself almost uncontested as an implicit benchmark. This reflected the politics of reforms rather than an informed choice of a most suitable conceptual prototype. Russian reformers were inspired by the American-style IMF sponsored ideal of liberal capitalism, which they accepted in its entirety and at face value.[5] This influenced the choice of advisers. References to the Anglo-Saxon concept initially appeared in studies on privatisation and firm management in Russia sponsored by international agencies (e.g., Pohl and Claessens 1994), despite apparent contrasts in the business environment in the US and any of the post-communist countries.

These beginnings have set a long-term trend. Progress in the corporate sphere of post-communist countries has been routinely scrutinised by way of making

[5] Then as now there were people who maintained that this was a superficial and potentially disastrous approach to reforms. For an authoritative analysis, see Stiglitz (1999) and Kornai (2001).

comparisons with established market economies or using the latter as the point of reference. Furthermore, the analysis is almost invariably conducted in terms and within the framework of conceptions developed with mature market economies in mind. It took a surprisingly long time to acknowledge that Russian capitalism and hence the Russian system of corporate governance was emerging under unique circumstances (see, for example, Nellis (1999) on the lessons of privatisation in Russia). On the economic side these were, most notably, the necessity for firms to cope with the incomplete set of incomplete markets and the extreme politicisation of economic policy-making. No wonder that attempts to evaluate the performance of firms in transition countries on the basis of references to "conventional" capitalist firms (see Filatochev 1997 for survey), whatever this may be, do not convince. Equally speculative are the many predictions on the prospect of a shift towards "conventional" corporate governance mechanisms when authors do not foresee for corporate governance structures in Central and Eastern Europe and Russia any other future than imitating existing Western models.

It would be very wrong, of course, to extend this criticism as far as suggesting that modern corporate governance theory is of no use to the analysis of transition economies. Instead this paper suggests that a new paradigm is required incorporating the achievements of the mainstream theory coupled with a clear vision of the realities of transition. Advance in this direction requires an extension and/or re-appraisal of certain aspects of corporate governance theory and in particular its analytical toolkit.

Repetition, Hesitation, Deviation: the Development of a National Model

The evaluation and prognostication of the development of a national model of corporate governance has to be preceded by choosing appropriate analytical instruments. In the recent years, with the debate on corporate governance in transition economies increasing in scale, a greater diversity of theoretical approaches has become noticeable. Yet, as was demonstrated in section two, as far as Russia is concerned, the conceptual build-up has been affected through exposure to particular influences. Their theoretical impact, both in terms of prevailing outlook and the terminological apparatus, is still in evidence in publications appearing in Russia and abroad. Here we identify some of the fallacies associated with this inertia.

Dependence on One Particular Theoretical Paradigm

As was demonstrated in a previous section, Russian reformers had opted for the American model of corporate governance for reasons that were not entirely academic. Of course, by itself this does not mean that the choice had to be wrong as it proved to be. Therefore it is of use to find out what makes this particular model such a bad choice.

Russian reforms are very much a showcase of a compromise between declared intentions and actual policy. When transition just started the government preached faith in the self-regulatory forces of a free market but in fact was keen not to antagonise powerful pressure groups, the employees and managers of state-owned enterprises initially and the so-called oligarchs later. Consequently these forces have never been actually freed up as intended. Nonetheless, the lip service paid to market freedom made it conventional at a certain stage to look at the progress of reforms through the prism of economic liberalism. In terms of corporate governance, ever since the issue of owners' separation from control in big corporations was raised by Berle and Means in the early 1930s, the liberal stream has been spearheaded by the American model. However, there are good reasons to believe that this concept offers far less than a perfect fit when projected on the practice of post-communist economic transition.

At a conceptual level, the model places an efficient market in the centre of the paradigm. Consequently, two important assumptions characterise the American system of corporate governance in its classical form. First, the disciplinary action by equity owners relies on options offered by an efficient equity market. These essentially boil down to the right of free exit for shareholders and the threat of a hostile take-over. Second, the structure of corporate governance is built around a specific criterion of efficiency that emphasises the maximisation of shareholder's wealth.

Williamson (1975) summarised this conceptual focus of the American model by coining the motto "in the beginning there were markets." In transition economies, however, the degree of efficiency achieved by the market remains low in comparison with Western economies. The 2003 Index of Economic Freedom by the *Wall Street Journal*, which may be construed as an indirect measure of the maturity and efficiency of the market in various countries of the world, positions Russia on the border of the "repressed" category in the rankings of economic freedom (*The Wall Street Journal*, November 12, 2002).

A proxy fight is a representative example of a disciplinary action by a shareholder under the American model. In the course of a proxy fight a shareholder puts up his own candidates to oppose current managers and tries to persuade other shareholders to vote for these candidates. Proxy fights place heavy emphasis on access to and reliability of information about the firm: the renegade shareholders must meet the cost of gathering and analysing information proving that the firm may do better under a new management. In Russia the chance of a successful proxy fight is distant if only because the direct and indirect cost of such an action is going to be a multiple of what it could be in a Western economy mainly following the absence of an adequate institutional framework. Gaining reliable information about the firm's performance already looks like an impossible task for anybody outside a very close circle of top managers but even finding the names and mailing addresses of other shareholders may prove to be a difficult task because obstructions caused by managers and frequent abuse of shareholders rights.

The liberal roots of the American model are also evident in the fact that it has some difficulty handling certain important social and economic realities of the modern capitalist society, including the role of the state and changes in the identity of the parties whose interest the corporation has to serve. Consequently this model does not account for situations in which, as is a case in Russia, the controlling interest in corporation is held by the state or in which management is subject to employee supervision. At the same time it incorporates characteristics unique to the United States. For example commercial banks are not allowed by law to invest in corporate equity directly. There are no such restrictions in most other countries though, which is bound to have implications for corporate governance.

Definitions and Terminology

There is a multiplicity of interpretations of what the theory of corporate governance should be concerned with as well as ambiguity in the meaning and usage of some key terms such as "control", "regulate", "manage" and "govern" (Turnbull 1997). This is because the topic of corporate governance is a point of intersection of a variety of disciplines including microeconomics, organisational theory, management, informatics, sociology and politics. Clearly, this situation places additional responsibility on researchers.[6] We could expect those writing on such a relatively new subject as corporate governance in transition economies to be particular rigorous in order to avoid confusion and misleading analogies. Nonetheless, despite certain ambiguity in the meaning of the term corporate governance it is not widespread that papers addressing this topic in the context of a post-communist economy include a statement outlining the theoretical perspective from which they are written. Such omission could have been admissible if there had been consensus regarding the existence of some universally applicable basic truths pertinent to this topic. In the absence of this provision such omission is a sign of a readiness to employ by implication the knowledge and methods provided by theory developed under patently different conditions. This, however, is likely to create conceptual difficulties right from the outset as the following example demonstrates. In accordance with prevailing views, a valid definition of corporate governance in a mature market economy would be "the ways in which suppliers of finance to corporations assure

[6] A separate but congruent consideration is the threat of a possible communication problem between parties involved in the discussion and information exchange. Communication involves the assimilation of information by recipients using unique filters created through their cultural and personal experience. Therefore, considering the difference between foreign and Russian researches of corporate governance in this respect, the task of being clear about conceptual points acquires particular importance.

themselves of getting a return on their investment" (Shleifer/Vishny 1996, p.2). If, however, one applies this definition to a country of voucher privatisation like Russia and the Czech Republic then, strictly speaking, thousands of corporations and their shareholders have to be excluded from analysis as, under this method of privatisation, ownership rights were obtained by individuals without injecting any capital of their own.

Another distinctive example is the indiscriminative use of the term "buy-out" in connection with the governance arrangements following privatisation in the former communist countries (e.g., Filatochev et al 1996, Gurkov 1998). Once again, the critical question here is the extent to which the conceptual framework based on buy-outs in developed market economies may be applicable to countries in Central and Eastern Europe and Russia. In the West the decision to buy out is taken by interested parties, usually managers, voluntarily, either to facilitate the restructuring of troubled firms, or to realise efficiencies that require the full commitment of insiders (Thompson/Wright 1995). In post-communist states, to begin with, property was effectively given away or sold at nominal prices. Therefore, already for this reason the use of the term "buy-out" would be confusing as property rights were appropriated rather than bought or sold. More importantly, though, the acquisition of property by insiders in the course of mandatory privatisation represented an entirely different type of action in terms of motivation, objectives and rational and therefore was utterly unlike anything ever assumed by standard corporate governance models. To name just a few differences, by contrast to proper buy-out, in transition economies "buy-outs" were not initiated by insiders but imposed by governments on sound and ailing firms alike on political ground mainly. For the insiders becoming owners of their enterprises was not so much the issue of increasing efficiency and returns as preserving their very livelihood in a hostile and uncertain environment.[7]

A widespread failure to make a conceptual distinction between largest and dominant shareholders in transition economies (probably because in market economies with a mature and sophisticated institutional set-up this distinction is irrelevant) is yet another case in point. For a long time it was commonplace in literature to maintain that Russian corporations were "controlled by insiders." Accordingly, successes or fiascos of Russian firms were routinely explained in terms of the theory of employee ownership while a move towards ownership by outsiders was propagated as a possible solution to the economic woes of the country (see for example Uvalic, 1995, Frydman et al, 1999, Filatochev/Swain, 1997). This vision would have been correct had "insiders" represented a coherent and united group with aligned interests. As they were not, the

[7] See Kuznetsov and Kuznetsova (1996, 2001) on the issue of survival strategy of enterprises under transition.

aggregation of owners as “insiders” and “outsiders” was concealing the real centres of control and distorted the picture of Russian corporate governance. The latest data demonstrate that even now, ten years in transition, managers and workers remain the largest groups of shareholders: their combined share is about 46% of total stock. This appears to confirm the thesis of “insiders’ control.” However, in 1999, distribution of firms by identity of their first largest shareholder gave a different result: insiders controlled 27% of all firms, outsiders 60% and the state 13% (Kapelyushnikov, 2001a). This is very significant because in the absence of mechanisms that effectively protect the rights of minority shareholders, and most employees fall into this category, small blocks of shares are almost worthless (Atanasov, 2002). In other words, insiders may still be the dominant group of shareholders in aggregate terms, i.e., together they hold the largest portfolio of shares, but most industrial firms have already gone under the control of outsiders who have obtained the largest holding in the company.

Underestimation of Unique Features

A country specific approach to the issues of corporate governance in developed market economies has been a norm. Comparative studies were instrumental in establishing the causes of diversity in corporate governance, including the concentration and structure of ownership, the degree of the development of the equity market, national economic history and political tradition (Backley et al 1998). By contrast, in the literature on transition economics there is a practice of emphasising commonalities at the expense of variations as far as post-communist countries are concerned. The origins of this attitude can be traced back to the very beginning of the transition period when international economic agencies and many experts pulled together in what became known as “Washington consensus.” It gave endorsement to a set of policies, which were thought to be a universal remedy for any economy seeking to achieve stable economic growth and prosperity through the development of markets. Such approach was conducive to emphasising commonalities in the transition process. Later, as the results of the treatment proved to be patchy, some aspects the initial wholesale attitude towards defining the strategy of reforms have attracted criticism indicating a change to a more balanced view. The foundations of this view were provided by two important hypotheses developed as alternatives to “Washington consensus.”

One of them maintains that, for analytical purposes, the post-communist economy should be seen not as a deprived market economy that needs some repair but as an economic system in its own right (e.g., Nuti 1992, Stiglitz 1994, Stiglitz 1998). The other claims that the varying results of reforms across the spectrum of countries reflect a whole range of economic, cultural and social factors determining the readiness of a national economy to accommodate the reform package (Amsden et al 1994). In terms of conceptual implications both hypotheses point in the direction of a recent but growing tendency in the management and business literature to take more explicit account of factors determined by a nation's individuality as elements of its comparative advantage (Dunning 1997). We believe that the concept of corporate governance cannot stay unaffected by this trend, especially when contemplating the theoretical framework for the analysis of corporate governance in post-communist economies. Such a framework is essential for solving one of the major problems facing transition economies, the creation of appropriate institutions through state participation. Institutions are as much a matter of evolution as a matter of a structured effort. According to Arrow (1995), the state has to supervise the operation of the existing of the economic system, while gradually letting them be replaced by new entrants. Therefore, the choice of a concept becomes a practical issue because a distorted conceptual vision will emasculate the creative effort of the state.

New Paradigm Required

The discussion up to this point can be summarised as indicating the necessity for those involved in the exploration of corporate governance in post-communist countries to be, first, very exact in the analysis, second, cautious in applying conventions and, third, very much aware of country specific influences.

Examination in previous section revealed a repetitive pattern in the literature on transition of being dependent on purported analogies borrowed from the research that focuses on the Anglo-Saxon approach. This bias is not accidental. It is a reflection of the general attitude towards the realities existing in post-communist countries as being something temporary and in the process of reshaping. These countries are looked upon as emerging market economies in which the market mechanism is in the process of adjustment and tuning. In this context it appears only natural to try and follow the example of Western countries as market economies in which the market mechanism works far better.

Although there is some truth in such thinking we believe that there is need for more discretion when drawing on the existing experience. In fact the current features may be long lasting. The analysis that follows is an attempt to identify some research opportunities pertaining to the conceptual configuration of the theory of corporate governance on the basis of the criticisms presented earlier.

Definitions of Corporate Governance

The definition of corporate governance is far from being finalised as, according to Tricker (1997), "the theoretical underpinnings of corporate governance are still evolving." Although much attention in the current debate is justifiably given to the pragmatic side of corporate governance, at a more fundamental level the definition of corporate governance depends effectively on an answer to a broader philosophical question, i.e., for whom corporations should be run.

On the one hand, the new neo-classical school has no doubt that the answer must be the stockholders as the only group of residual claimants with consistent and easily identifiable interests (Keasey et al 1997). On the other hand, there has been growing realisation that the implementation of the principle of corporate social responsibility requires looking beyond the standard conception of shareholder wealth. This view has realised itself in a stakeholder approach to the corporation. It enhances the scope of corporate governance by presenting it as concerned with all the influences affecting the institutional processes involved in organising the production and sale of goods and services (Turnbull 1997).

Although there is certainly a variety of opinions regarding what corporate social responsibility might mean and it is a long way to go before this concept will be sufficiently developed, the important thing as far as corporate governance is concerned is the acknowledgement that the society wants corporate decisions to reflect something more than just what is best for shareholders even in parts of the world with a strong liberal attitude to economy as the United States (see, for example, Reich, 1998). For countries like Russia the issue of corporate social responsibility has particular importance, considering the socio-economic tradition of the previous seventy years that gave a lot of weight to social obligations of big enterprises (Clarke, 1995, Standing, 1995). This heritage came into conflict with the objectives of bulk privatisation in the 1990s and was one of the reasons for both mass impoverishment and poor enterprise performance.

The choice of the conceptual starting point is very important for defining the current state and the development path of a national system of corporate governance. In the case of Russia, for someone firmly attached to the neo-classical point of view the system of corporate governance in the country would appear irrational with little to justify its existence. The share ownership is dispersed, the stock market does not play any significant role and institutional investors are weak and disengaged. Consequently, the degree of either influence or protection of the mass of shareholders is appallingly low because the allocation of ownership rights has not been supported by necessary legal and institutional infrastructures (see Kuznetsov/Kuznetsova 1996 for the analysis of the case of Russian and Brada 1996 for other European countries in transition).

A different picture emerges if the same situation is contemplated in terms of the stakeholder theory. In this context some of the idiosyncrasies of the Russian corporate sector, including reliance on formal and informal networks and on barter transactions, equity cross-holding, may be interpreted as the primary building blocks of a valid system of corporate governance.

The stakeholder concept may seem to be quite impractical as a theoretical model as stakeholders are not homogenous and have unclear expectations, which makes it difficult to work out a distinct criterion of efficiency. Yet the stakeholder corporation is not a utopia. For a long time stakeholder institutions and practices have been firmly established in northern Europe, especially in Germany and Scandinavian countries, and in Asian countries, particularly in Japan (Miwa/Ramseyer, 2002). There is a number of similarities in the history of these economies which may be associated with the choice of corporate governance and, what is particularly relevant to this research, which may be traced in post-communist economies of today as well.

First, in all these countries the corporate system acquired its features as a response to a momentous crisis, the Great Depression in Scandinavia, the war in Japan and Germany and the collapse of communism in Central and Eastern Europe. Second, at one stage or another all of them developed a strong tradition of paternalism and egalitarism in comparison to the Anglo-Saxon tradition. Third, in all of them the state plays a prominent economic role.

These analogies are not the only reason why a stakeholder approach deserves recognition as an analytical tool that particularly suits transition economies. In the latter the emphasis of traditional corporate governance theory on the protection of the interests of shareholders misfires. If we take Russia as an example, the method of privatisation ensured that the bulk of shares accumulated in the hands of employees of privatised firms. In such firms one can often suspect a collusion of managers and shareholders-insiders that may be detrimental to the interests of shareholders-outsiders and the society. Because this phenomenon was not known previously on such a great scale the traditional corporate governance theory has no advantage over the stakeholder concept in giving answers to questions that this situation has posed.

Stakeholding and the Efficiency of the Firm

The fundamental reason for the existence of concepts of corporate governance is concern for efficiency in employing capital assets. If the influence of shareholders is weak or potentially detrimental as is the case in transitional economies, increase in the number of external influences on publicly traded firms may be a healthy alternative. This again draws attention towards the stakeholder interpretation of corporate governance claiming that control over a corporation should be spread between the customers, the suppliers, the community, the banks, etc. in addition to the shareholders and the management (Monks and Minow 1996). Then, by contrast to the Anglo-Saxon model, serving best the interests of stakeholders is selected as the measure of efficiency. As previously shown, however, determining the composition of stakeholders is probably the greatest challenge facing this kind of approach. A possible solution, as pointed by Blair (1998), lays in extracting the properties that turn shareholders into "responsible" owners. These are a combination of economic risk and remuneration, which is associated with tying up certain assets in a particular type of investment. However, stockholders are not the only investors in this category. Workers with specific skills, suppliers who invested in developing specific products, local authorities who started a regional programme tailor-made to the requirements of local industry, all these investors are not dissimilar to stockholders in that they have made a long-term investment which outcome depends on the performance of a particular firm. Hence their behaviour towards this firm is likely to be no less rational than that of shareholders. This may be the theoretical explanation to certain facts in the behaviour of newly privatised firms in post-communist countries which contradicted predictions based on conventional views, in particular that insiders generally showed restraint in self-seeking behaviour (see Brada 1996 on situation in Central and Eastern Europe).

External Agencies of Control

Researches generally agree that exposure to multiple interest groups may be able to play a crucial role in precipitating the restructuring of former state owned enterprises and stimulating economic growth (see Filatochev 1997 for literature review). When the issue of opening up publicly traded firms to external influences is discussed in the literature, attention usually focuses on banks and their role as external agencies of control (Aoki/Kim 1995; Frydman et al 1996). Under Russian conditions, however, banks look as unlikely centres of external control at the moment. With few exceptions they are small, weak and poorly fit to get involved in strategic investments as the consequences of the 1998 financial collapse have not been fully overcome yet (Reuters, 1999).

Far less attention, if any, has been given to the role of the state as a shareholder. In Russia, for example, the state has retained control over 30% of industrial firms producing 25% of the GDP but its objectives as owner remain confused and unarticulated. This discourages other stockholders to act strategically. The economic role of the state in transition economies must be revised. For the state to contribute to the economic efficiency of privatisation does not imply it returns to the role it played under central planning, i.e., direct supervision over production. Rather it must join other shareholders in seeking to increase the value of their stake in the firm. It can do this by contributing to the institutional and legal environment that would expose managers, in real terms, to new centres of control and force them to restructure their businesses. A practical way forward may be in finding means to increase the powers of the state without providing more leverage to bureaucrats. This can be achieved if decision-making is concentrated in the more transparent branches of the government while rules and regulations are formulated in a manner that minimises the freedom of the lower levels of bureaucracy to give own interpretations of the law. At the moment there is a noticeable gap between the degree of public accountability of the ministers in the central government and local administrators. At the same time, as some experts have noticed (see Kapelyushnikov, 2001b), the core of the "institutional trap" in Russia is that all new formal institutions immediately acquire a superstructure of informal surrogates that undermine their impact. Therefore, although in the long run decentralisation may prove its worth, strive for transparency and institutional efficiency may justify a shift in the balance of responsibilities towards the centre.

Conclusions

Corporate governance in post-communist economies has attracted much attention because of evidence that privatisation on its own has failed, on many occasions, to deliver efficiency gains. The rapid adoption of the concept has not always been accompanied with due concern for adapting it to the conditions of transition economies. It is sometimes overlooked that economies in transition represent developed and complex systems built according to an idiosyncratic although now defunct logic. Exactly because of this complexity the transitional economic systems cannot easily absorb and integrate properties of another also developed and thus highly complex economic system. This implies that proved and tested theoretical models are in need for adjustments in order to become a suitable guidance for institutional development. This paper has tried to highlight some - and only some - of the problem areas. It has been suggested that the traditional principal-agent model based on dichotomy shareholders-managers does not fit conditions in the former communist countries because markets there are too new and underdeveloped to provide means to restrain effectively managerial opportunism. At the same time the prevalence of undersized and weak banks within the financial system has become an impediment for the development of the continental model. Under these circumstances a stakeholder model emerges as a preferential analytical framework for searching ways to diminish the managerial slack.

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