

Russian Manufacturing Subsidiaries of Western Corporations

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The position of manufacturing subsidiaries of Western MNCs in the Russian economy at the beginning of 2014

- Complete dominance in several market segments (90% of the tobacco market and car assembly facilities, 85% of the beer market, 75% of the juice market, 60% of the beauty and cosmetics market (by value), certain construction materials and do-it-yourself goods segments)
- Active expansion in transportation equipment, specialized chemicals, and industrial services.
- Limited presence at energy sector (FORTUM, BP, Shell, Total)
- Development of local value chains (especially in car production) – engine factories by Ford and Volkswagen, worldwide suppliers of car components (Bosch, Nemak, Continental, Fuyou Glass, Fijikura, Schaeffler)

The dominant ways of establishing manufacturing subsidiaries

- **1992-2007**- “brownfield” investments (industrial sites and facility to be brought up to “world class manufacturing”) and greenfield investments (mostly in car assembly and chemicals)
- **2008-2012** – acquisitions of modern facilities, market share and strong trademarks from local companies and early entrants
- **2012-2017** – greenfield investments and “fenced investments” coupled with non-equity cooperation

Most interesting early greenfield investments

- P&G acquisition of a plant for home-used chemicals near the city of Tula (see Pepper, J. Pepper, 2012. *Russian Tide*. Cincinnati, OH: P&G)
- Acquisition by Danone of the confectionery factory in Moscow
- Acquisition by KNAUF of a large factory on insulation products near Moscow
- Acquisition by Philip Morris of a tobacco factory in Moscow
- Acquisition by BBH (a joint Finnish-Swedish company) of a large brewery in St.Petersburg (later sold to Carlsberg)

Early unsuccessful (failed) acquisitions

- The attempt of Bombardier to acquire a locomotive factory near Tula (the deal was cancelled at the last moment)
- The attempt of Siemens to acquire the major local producers of energy equipment (the deal was cancelled at the last moment)
- Purchase by Philips a plant producing TV sets (sold 4 years later for 1 Ruble, the plant disappeared in the following years)

The large acquisitions and other investments projects of MNCs in Russia in 2000-2010s

- Car assembly plants by Ford, GM, Hyundai, Volkswagen, Toyota, Peugeot-Citroen-Mitsubishi
- Sakhalin Energy project (oil extraction on a product-sharing agreement by a consortium of the leading oil companies)
- Euro 3 bln. joint project to produce PVC by SIBUR and Solvay
- Acquisition of a local bottler by PepsiCo for US\$1.4 in 2011

Liaison Institution for Foreign Investors in Russia – Foreign Investments Advisory Council (FLAC)

- Annual meetings of global CEOs (Chairmen) with the Prime-Minister of Russia
- Annual reports in English and Russian (350) pages on the amendment of the legislation and the practices of the government regarding foreign investors
- 12 working groups (Technical regulations and elimination of administrative barriers; Improvement of tax law; Improvement of customs law; Financial institutions and capital markets; Trade and consumer sector; Health care and pharmaceuticals; Localization; Efficient use of natural resources in Russia; Image of Russia; Energy efficiency; Innovation development; Development of Far East and Siberia) headed by a particular corporation
- Overall coordination of the working groups -- EY

FIAC Members (2017)

No	Company	Country
1	3M Company	USA
2	ABB Ltd.	Switzerland
3	Abbott Laboratories	USA
4	Arconic Inc.	USA
5	AstraZeneca	Sweden / Great Britain
6	BASF SE	Germany
7	Bayer AG	Germany
8	British American Tobacco	Great Britain
9	BP	Great Britain
10	Cargill, Inc.	USA
11	Carlsberg Breweries A/S	Denmark
12	Danone	France
13	Deutsche Bank AG	Germany
14	The EBRD	International financial organizations
15	ENEL S.p.A.	Italy
16	eni S.p.A.	Italy
17	Essity Aktiebolag (publ)	Sweden

FLAC Members (2017)

No	Company	Country
18	EY	USA
19	Exxon Mobil Corporation	USA
20	Fortum Corporation	Finland
21	Henkel AG & Co. KGaA	Germany
22	Hyundai Heavy Industries Co., Ltd.	The Republic of Korea
23	International Paper	USA
24	Kinross Gold Corporation	Canada
25	LafargeHolcim	Switzerland
26	Leonardo S.p.a.	Italy
27	Mars, Incorporated	USA
28	METRO AG	Germany
29	Mitsubishi Corporation	Japan
30	Mitsui & Co., Ltd.	Japan

FLAC Members (2017)

No	Company	Country
31	Mondelēz International, Inc.	USA
32	Nestle S.A.	Switzerland
33	Novartis AG	Switzerland
34	Olam International Limited	Singapore
35	PepsiCo	USA
36	The Procter & Gamble Company	USA
37	Royal Dutch Shell plc.	Great Britain / the Netherlands
38	Saint-Gobain	France
39	Samsung Electronics Co., Ltd.	the Republic of Korea
40	SANOFI	France
41	Schneider Electric	France
42	Siemens AG	Germany
43	Société Générale Group	France

FIAC Members (2017)

No	Company	Country
44	SOLVAY Group	Belgium
45	SUN Group	India
46	Takeda Pharmaceutical Company Limited	Japan
47	Telenor Group	Norway
48	Tetra Pak	Sweden
49	The Coca-Cola Company	USA
50	Total S.A.	France
51	UniCredit	Italy
52	Unilever	Great Britain / the Netherlands
53	Uniper	Germany
54	World Bank	International financial organizations

The subsidiary mandate of Russian manufacturing subsidiaries of Western corporations

- The relatively narrow mandate (minimal authority for business development, capital investments and R&D),
- The position of a subsidiary as a “revenues center” or a “profit center”
- Concentration on the effective use of the existing facilities and on quick installation, putting in motion and reaching the planned level of robustness of operations of new facilities

The major elements of HRM systems of Russian manufacturing subsidiaries of Western corporations

- Permanent job contracts
- Moderate monetary benefits depending on technical performance of a shop or a factory
- A wide range of additional (“social”) benefits – additional (“voluntary”) medical insurance, free meals, credits for employees etc.
- Limited use of different forms of ‘moral recognition’ for employees as the exemplary behavior is presented as the norm

The usual response to job announcements of
Russian manufacturing subsidiaries of MNCs
(number of applicants per a vacancy)



← Expatriate managers

← Plant managers/Plant
superintendents

← Shop managers and foremen

← Qualified adjusters and repairmen
of equipment

← Workers at assembly lines

Robustness and mutation of HRM systems of Russian manufacturing subsidiaries of MNCs in 2014-2017

- **Maintaining** the system of permanent job contracts
- **Maintaining** the system of moderate monetary benefits depending on technical performance of a shop or a factory
- **Narrowing** the range of “social benefits”
- **Intensification** of the use of different forms of ‘moral recognition”

Evolution of the post-Crimea Russian economy

- Economic sanctions of USA, EU and some other countries against the largest Russian banks, oil companies, military enterprises and selected physical persons (since March 2014)
- Self-imposed Russian embargo on imports of foodstuffs from USA, EU and some other countries (August 2014)
- Sharp devaluation of the national currency (the end of December 2014)
- Fall in oil prices and budget revenues
- Economic recession

The consequences of the self-imposed Russian embargo on imports of foodstuffs from USA, EU and some other countries

- The necessity to revise supply schemes for many food categories, especially in dairy
- The necessity to develop contract manufacturing and wholly-owned Russian subsidiaries to maintain the known brands on the markets
- Stronger competition from local brands and from Western corporations with the established Russian manufacturing subsidiaries

The struggles of Valio

- The sanctions were announced the 8th of August 2014
- In 2013 Russia absorbed 50% of Valio's exports, 13% of the global production volume and 20% of the global sales
- Valio occupied 33% of dairy products imports of Russia in 2013, 90% of Valio's sales in Russia came from imports
- Pekka Laaksonen retired in September 2014
- The global sales of Valio decreased in 2014 by Euro 120 mln.
- At the end of 2014 the assortment of Valio in Russia decreased by 10 times, monthly sales – by 4 times
- Valio used the local contractors (a Russian subsidiary of German Ehrmann and the local “Galaktika” Co.) and its own small factory in Moscow
- In 2015-2017 the own factory was expanded by four production lines, restoring assortment to processed cheese (Viola brand), butter, yogurt, packaged milk etc.

The consequences of the sharp devaluation of the national currency (the end of December 2014)

- Reduction of the invested capital on consolidated balance sheets
- Brand impairment (because future sales forecasts of particular brands that were expressed in a foreign currency also deteriorated)
- Impairment of other tangible and intangible assets.

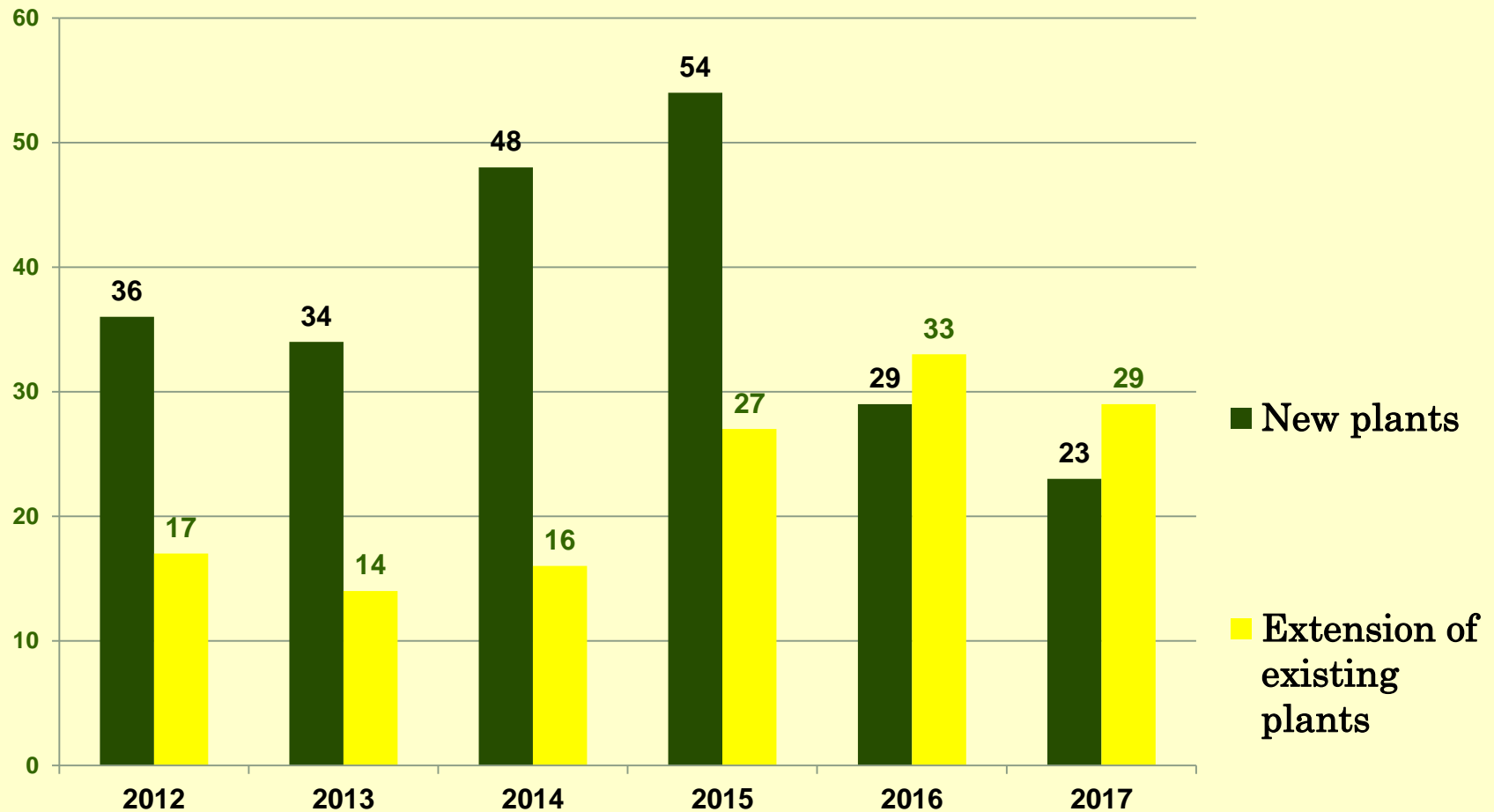
Consequences of the fall in oil prices and budget revenues

- Limited decrease in consumer markets for goods of daily use (by 10-30%)
- Deep recession in consumer markets for long term use (cars)
- Deep recession in industrial markets (up to 80%)

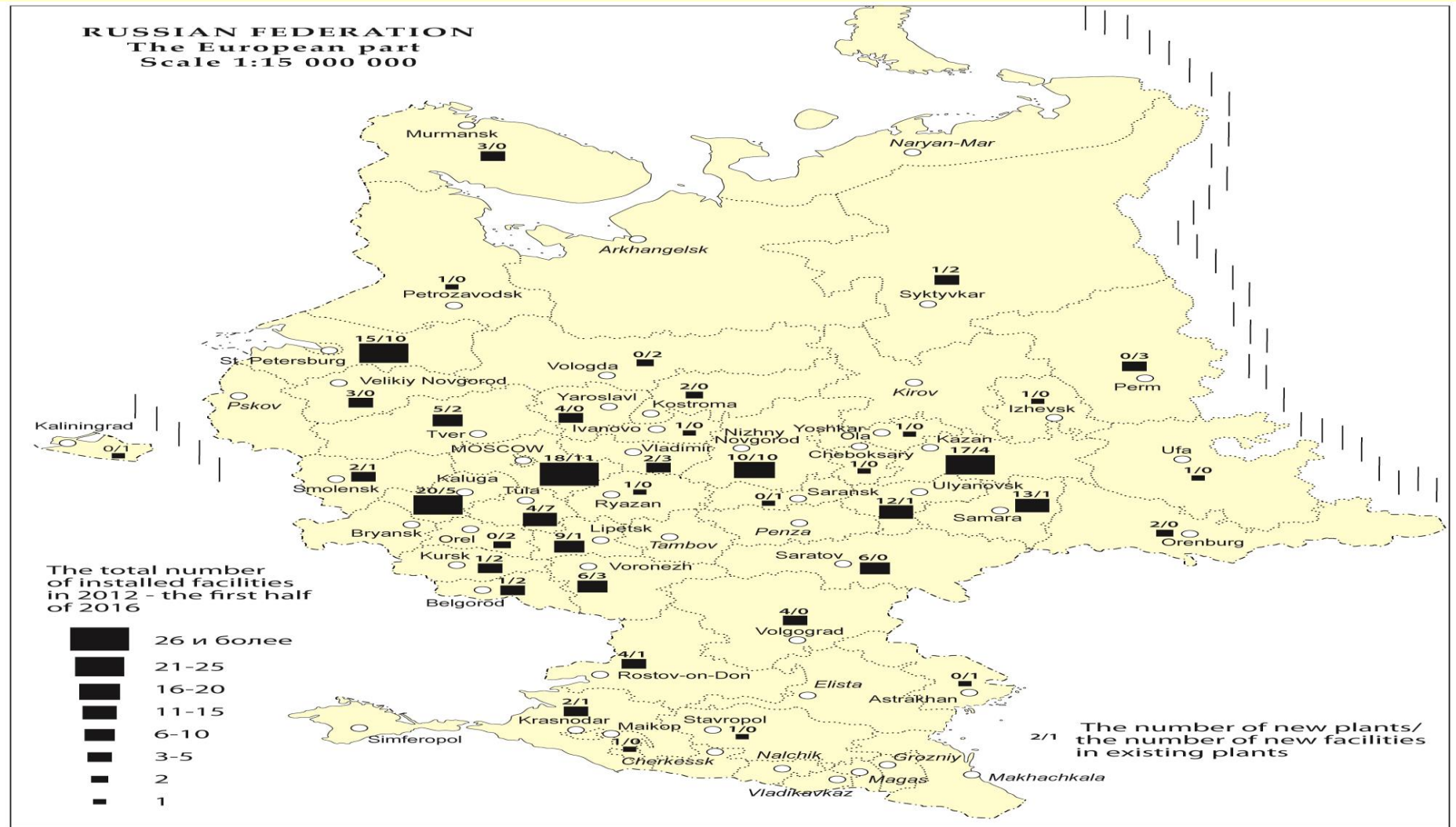
General anti-crisis measures

- Simplification of product mix (margin generators and volume generators) –
(<https://youtu.be/WTh8WNJjM5Y?t=641>)
- Looking for local suppliers
- Continuous process innovations
- Supportive investments to increase the share of Ruble-denominated costs (car production, foodstuffs, cosmetics)
- Accelerated opening of “facilities-in-progress”
- Minimal and cautious divestments (less than 20 cases in 2012-2017)

Accelerated opening of “facilities-in-progress” in 2014-2015



Location of new facilities (1)- European Russia



Location of new facilities (2) – Asian Russia

RUSSIAN FEDERATION
The Asian part
Scale 1:40 000 000



Specific measures to cope with the long-term stagnation

- Attempts to export from Russian manufacturing facilities (exports of insulation materials by ROCKWOOL from Russia to Finland)
- Expansion in specific niches (baby food, pet food, chemicals, light trucks, components for consumer and industrial markets)
- The use of direct and indirect state aid measures (export support, support for agriculture etc.)
- Adjustment of HRM systems
- Combination of greenfield investments, “fenced investments” and reverse contract manufacturing

German corporations which actively developed their manufacturing facilities in Russia (opening new plants and extension of existing plants) in 2016-2017

Name	Type of development
BASF	One new factory and three new production lines
Henkel	One new factory and one new production line in another factory
Volkswagen	New production lines
Edscha	New factory
Huesker	New factory
Guhring	New factory
Jungheinrich	New factory
Linde Gas	New factory
MC-Bauchemie	New factory
OBO Bettermann	New factory
Viessmann	New factory
VOSSLOH	New factory
Wilo	New factory
Eberspacher	New production facilities in the existing factories
Hochland	New production facilities in the existing factories
Horsch Maschinen GmbH	New production facilities in the existing factories
Lorenz Snack World	New production facilities in the existing factories
Schlemmer Group	New production facilities in the existing factories
Sulzer Chemtech	New production facilities in the existing factories
BSH Bosch und Siemens Hausgerate GmbH	New production facilities in the existing factories
Bucher-Guyer AG, Giletta	New production facilities in the existing factories

Combination of greenfield investments, “fenced investments” and reverse contract manufacturing- the case of Volkswagen

- **2007 -- opening of a new car-assembly plant near Kaluga (greenfield investments of Euro 1,042) to produce Skoda (Octavia, Superb, Roomster, Yeti) and Volkswagen (Passat, Golf, Tuareg, Jetta, Caddy)**
- **2011 - general agreement with “Russian Machines” (Chairman - Siegfried Wolf, former co-CEO of Magna, CEO -- Manfred Aibek, also from Magna, previously worked in Opel) to assemble Skoda in “GAZ” (Nijny Novgorod) on leased facilities**
- **2014 - import of Scania buses (Scania was acquired by VW) for Sochi Olympic Games**
- **2015 - opening an engine factory in Kaluga for Euro 200 Mln.**
- **2017 - a contract to supply 550 bus shassis of SCANIA to make buses on a factory controlled by the “Russian Machines”**
- **2018 - opening of a new production line in GAZ for Euro 87,5 mln. to Produce Skoda Kodiaq**

What can be expected during your work in a Russian subsidiary

- Simultaneous working on several overlapping or contradicting projects
- Unexpected changes of the situation of a subsidiary (government regulations, market situation, attitudes of HQs or of the local authorities)
- Necessity to show ingenuity and initiative at any position
- High chances for intensive contacts outside the subsidiaries with local companies
- Opportunities to learn from both expatriate and local employees

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