Restructuring with What Success?
A Case Study of Russian Firms

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This case study of enterprise restructuring utilizes data collected from thirty-two former state-owned firms in Taganrog, Russia, in the summer and fall of 1999. These data are used to construct three composite measures of enterprise restructuring. When defined broadly to include several dimensions of the restructuring process, the "restructuring threshold" is achieved by half of the privatized firms participating in the project. The firms achieving this threshold are distributed across all industries included in the sample. Regardless of the composite measure used, more than one-third of the former state-owned firms participating in this project attained the "active" restructuring designation. The results indicate that (1) production assortment changes appear to be ongoing among those firms engaged in restructuring activities, (2) employment changes appear to involve a mixed strategy with regard to timely wage payments, workforce size, and the benefits package; and (3) outsider ownership is more prevalent among the group of firms designated as restructuring than among those firms that failed to achieve the "restructuring threshold". To put into perspective the economic and business environment in which these former state-owned firms operate, a comparison is made to a group of *de novo* firms that were surveyed under the auspices of the same project.

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Introduction

Little debate surrounds the proposition that former state-owned firms in Russia must restructure their organization and operations in order to survive the transition from a planned economy to a market economy. Moreover, little debate surrounds the nature and scope of enterprise restructuring that must take place for firm survival to be an option. Restructuring involves changes in the quantity and assortment of production, with corresponding changes in the size and skill composition of the workforce, the quantity and quality of the physical capital stock, the organization of production, and the number and location of suppliers and buyers, for example. Few debate whether enterprise restructuring in Russia has been hampered by new financial arrangements associated with new ownership structures and reduced financial support from banking and other central or local authorities.

Given persistent adverse economic conditions throughout the 1990s, however, considerable and spirited debate among researchers and policy makers continues to surround the query: *With what success are Russian firms restructuring?* Throughout the 1990s, Russia experienced industrial production declines more than double that of corresponding employment reductions; investment expenditures failed to reach 25% of the pre-transition level despite the need to renovate more than 50% of the capital stock; a growing proportion of manufacturing firms each year reported zero profits (Goskomstat 1999). Aggregate data suggested that throughout the 1990s, Russian firms, if restructuring at all, were failing to restructure at a pace that would facilitate the transition to a market economy. A growing literature purports to demonstrate how Russian firms purposefully avoided changes that would have improved their overall operations.[1] At the same time, however, firm-level

[1] Ickes and Gaddy (1998 1999), Ickes and Ericson (2000); see also, Pervalov *et al* (1999).

data collected in numerous small-scale survey projects[2] detail a wide variety of efforts by managers to change production, employment and financing in order to ensure the ongoing operation and survival of their firm. The 20th century ended with the jury still out regarding the restructuring success experienced by Russian firms.

Why does it matter whether Russian firms are restructuring? If we take as the premise - *Russian firms are not restructuring* - then a set of policy options designed to initiate restructuring would be appropriate to consider. If we take as the premise - *Russian firms are restructuring but their efforts have been impeded or the outcomes have not been accurately recorded* - then a different set of policy options would be appropriate to adopt. Thus, the greater the detail provided about the operation and performance of Russian firms, the better able policy makers will be to adopt the appropriate measures to facilitate enterprise restructuring and the overall transition process, and the more informed business leaders in the global community will be in terms of investment strategies in Russia.

This case study of enterprise restructuring utilizes data collected from thirty-two former state-owned firms in Taganrog,[3] Russia, in the summer and fall of 1999. These data are used to construct three composite measures of enterprise restructuring. The results illustrate the variation in

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[2] See, for example, Blasi *et al* (1997), Boycko *et al* (1995), Buck *et al* (1994), Commander and Mumssen (1998), Dolgopyatova (1995), Earle and Estrin (1997), Hendley *et al* (1997), Ickes *et al* (1995), Jones (1998), Krueger (1995), Linz (1993 1997 1998), Linz and Biddle (1998), Linz and Krueger (1996 1998), Nelson and Kuzes (1994), Standing (1996).

[3] Financial constraints limited the project to a single location. Previously-established connections with local officials made it possible to complete the project in Taganrog. While it is the case that Taganrog has been identified by Soviet and Russian researchers as the "average city" of Russia, the former Soviet Union (see, for example, Grushin (1980), Rimashevskaya (1992), and Chichiliymov (1999), among others), it is not the case that the thirty-two firms participating in this project were selected in such a way as to reflect the composition of former state-owned firms in all of Russia, or even Taganrog. The selection process targeted including one-third heavy industry, one third light/food industry, and one-third "other industry."

restructuring activities across privatized firms, as well as identify the most commonly adopted changes. The case study also draws on a survey of 87 never state-owned (*de novo*) firms conducted in Taganrog at the same time. Where variables are comparable between the two groups of firms,[4] it is possible to identify similarities and differences among the survival strategies of these firms. Detailed and comparative information on enterprise operations is invaluable in gauging the impact of economic conditions on business operations, as well as to highlight policy options that would be most effective in stimulating improved performance. Detailed and comparative information delineating enterprise operations also puts into perspective some fraction of what is required for former state-owned firms in Russia to initiate and sustain restructuring activities.

The paper is divided into five sections. The first section specifies the composite measure of enterprise restructuring. The second presents the methodology employed to evaluate the relative success of Russian firms in this regard. The third section describes the firms participating in the project. Restructuring results are presented in the fourth section. The final section offers concluding remarks.

I. Measures of Enterprise Restructuring

With what success are Russian firms restructuring? To address this question, one must first decide by what measure restructuring success will be gauged,[5] and second, how to determine whether

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[4] Top-level managers in former state-owned firms and in firms that never were state owned were asked about the ongoing operations and performance of their company. Twenty-two questions were the same in both surveys. Data collected from *de novo* firms are not applied to the composite measures of enterprise restructuring.

[5] Restructuring measures typically include: installation of new director or new management team, profits, sustained or increased production volume, change in the assortment of production (including quality improvements), timely wage payments, payment of above-average wages, absence of barter transactions, foreign capital investment, workforce downsizing equal to or greater than production declines, self-financed investment expenditures, new suppliers and/or new buyers, for example. See Blasi *et al* (1997), Djankov and Murrell (2000),

enterprise restructuring is “active” (firm-initiated) or “passive” (imposed by economic conditions).[6] Djankov and Murrell (2000) canvassed the transition literature for empirical analyses of enterprise restructuring, dividing the 125+ papers into two categories: those focusing on quantitative measures of firm performance (volume of output, sales, profits, for example), and those focusing on qualitative measures (timeliness of wage payments, introduction of new products or processes, organizational change, for example). If we take the broadest interpretation of enterprise restructuring - changes which former state-owned enterprises must undertake in order to produce with the requisite degree of efficiency to survive in a market-oriented economy - it is evident that both types of measures are required to evaluate the restructuring success of Russian firms. Both types of measures are problematic, however, because both may reflect demand or market share conditions rather than firm-initiated restructuring activities.

This case study of former state-owned enterprises in Taganrog, Russia, utilizes three composite measures to evaluate the nature and scope of enterprise restructuring. The composite measures include both quantitative and qualitative variables. For analytical purposes, the variables included in the composite measures are grouped into three broad categories of restructuring activities: changes in management / organization, changes in production, and changes in employment.

Changes in management / organization

Several basic themes relating to management change appear in the restructuring literature.

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and Linz and Krueger (1998).

[6] For example, “active” restructuring might involve a firm changing the size and composition of the workforce in response to profitability considerations arising from production or marketing decisions. Passive restructuring would involve workforce downsizing driven by lack of cash for wage payments.

First, it is posited that for enterprise restructuring to be successful top-level managers of former state-owned enterprises, the red directors,[7] must be removed in order to terminate the Soviet legacy of maximizing output and employment rather than profits (see, for example, Aghion and Blanchard 1996, Claessens and Djankov 1999, Djankov 1999, Frydman, Pistor and Rapaczynski 1996, Pinto, Belka and Krajewski 1993, Roland and Sekkat 2000). Alternatively, for current managers to be successful in the transition and post-transition market-oriented environment, they must receive special training, perhaps even in the West (Dickenson, Campbell and Azarov 2000).

Second, it is posited that re-organization of enterprise operations to accommodate the new economic environment where former state-owned firms must identify and satisfy clients' demands is an integral component of enterprise restructuring (Brown and Earle 1999, Brown and Earle 2000, Brown and Brown 1999, Ickes, Rytermann and Tenev 1995, Joskow, Schmalensee and Tsukanova 1994, Linz and Krueger 1998, McDonald 1993, Shleifer 1998, Svejnar 1996). This is especially important for firms which sell the majority of their product to non-state-owned firms.

Third, a growing literature examines the relationship between ownership structure - insiders (employees) versus outsiders (non-employees) - and enterprise performance, taking the position that enterprise restructuring will be most active when the ownership structure is dominated by outsiders (Aghion and Carlin 1996, Claessens and Djankov 1999a, Earle, Estrin and Leshchenko 1996, Estrin and Rosevear 1999, Frydman Gray, Hessel and Rapaczynski 1999, Jones 1998). It further is posited that if individual insiders (i.e., top-level managers) own substantial blocks of shares (10% or more), enterprise restructuring is unlikely to be "active".

To utilize management change as a measure of enterprise restructuring, data collected from

[7] Term coined by David Granick, ***The Red Executive*** (New York: Columbia University Press, 1954).

the former state-owned firms participating in this study focused on whether: (i) the director and/or production manager had been replaced since 1992; (ii) the current director received special training since 1992; (iii) outsiders own more than 25% of the company's shares; (iv) anyone (insider or outsider) owns a 10% or more block of shares. While positive responses to these conditions cannot establish the existence of "active" restructuring at the firm, they tend to undermine support for the proposition that firms headed by red directors are continuing to operate in socialist production and employment modes.

Changes in production

To produce with the requisite degree of efficiency to survive in a market-oriented economy, restructuring of former state-owned enterprises will require changes in the volume and assortment of production. One simple measure of production change compares the current volume of output with that of the previous year. Frequently, however, managers offer information on the value rather than the volume of output, with little explanation of the valuation procedure. Consequently, questions targeted at capacity utilization and how it compares to the previous year are better suited to estimate changes in production. Yet, since both volume and capacity utilization may reflect demand conditions rather than restructuring efforts, neither are well-suited as single measures to evaluate enterprise restructuring.

Change in production assortment frequently is viewed as the key component in enterprise restructuring measures (Blasi *et al* 1997, Ernst *et al* 1996, Krueger 1995, Linz and Krueger 1998). Identifying the nature and scope of changes in production assortment incorporates a variety of components: (i) did the firm eliminate any products or services from their assortment; (ii) were existing products improved in any way; (iii) have new products or services (transportation or delivery, for example) been added; (iv) has the firm changed suppliers or customers; (v) is the firm currently buying from other firms what it used to self-supply? Production assortment changes also are likely to be associated with the acquisition of new machinery, as well as with expenditures on research and development.

Changes in employment

Enterprise restructuring involves not only changes in the size and skill composition of the workforce (Clarke 1997, Commander and Coricelli 1995, Konings, Lehman and Schaffer 1996, Konings and Walsh 1999, Linz 2000, World Bank 1996), but also changes in the benefits offered to employees by former state-owned firms (Clarke 1999, Standing 1996). Both of these dimensions are likely to have consequences for the magnitude and timeliness of wage payments, which in turn are correlated with the privatized firm's ability to successfully restructure (Linz and Krueger 1998).

The nature and scope of employment change would be captured, in part, from data collected on the former state-owned firm's current workforce size, the percent of workers released annually since 1992, changes in labor productivity, the percent of current workers who regularly show up for work, and the probability that workers would be released or hired during the current year. In addition, data relating to benefits offered by the privatized firm are relevant. In particular, it is important to know: (i) the number of workers currently receiving benefits and how that compares to the situation in 1992, (ii) the type of benefits currently offered, (iii) how the benefits compare to the size of the wage bill and the firm's profits, (iv) whether nature and scope of benefits have been reduced since 1995, (v) whether any formerly-offered benefits have been transferred to local authorities, and (vi) whether employees pay for benefits.

Wage payment conditions tend to reflect the firm's current financial condition. Whether wages are being paid on time, and how the current wage payment situation compares with the previous year, as well as with earlier years reflects on the firm's ability to succeed in Russia's chaotic economic environment, which in turn seems to proxy successful restructuring efforts (Linz and Krueger 1998).

As is evident from the discussion above, no single quantitative or qualitative variable or measure captures the full scope of restructuring efforts that must be undertaken for Russian firms to survive the transition from a planned economy to a market economy. Composite measures which include both quantitative and qualitative variables are more enlightening in terms of the nature and scope of enterprise restructuring, simply because they incorporate more dimensions of the overall undertaking. Moreover, by developing a composite measure, and a simple rule for evaluating success, it is possible to make comparisons across industries and regions. This information is easily digestible by policy makers, should they become inclined to seriously consider ways of improving the economic environment in which Russian firms operate. It is not the case, however, that composite measures are unambiguous in evaluations of the extent of "active" versus "passive" enterprise restructuring in Russia. Composite measures simply serve as a mechanism for identifying a pattern (or lack thereof) in restructuring activities across firms, industries, and regions, as well as over time. Understanding the pattern of restructuring activities makes possible identification of factors which enhance or impede successful restructuring efforts. Establishing a "restructuring threshold" makes it possible to separate former state-owned firms into "winners" and "losers" with regard to adopting changes that will enable them to produce with the requisite degree of efficiency to survive in a market-oriented economy.

II. Methodology

The original research project was designed to investigate enterprise strategies for survival in Russia's transition economy. Since former (and current) state-owned firms inherited a capital stock, workforce, and organizational structure from the Soviet economy, their initial conditions and objective functions are likely to be quite different from firms which never acted as an instrument of central planners or local authorities (Ericson 1996, Ickes and Ericson 2000). Consequently, two questionnaires were developed for the original research project: one to be given to firms that were formerly (or currently) state-owned, and one to be given to firms that had never been state-owned (*de novo* firms).

To keep the time requirements for completing the questionnaire to a minimum, given the number of questions included in both survey instruments, the majority of questions asked top-level managers to select "yes" or "no," or fill in a number. Twenty-two of the 60+ questions included on each version were identical, yielding a core set of responses relating to the organization and operation of the entire set of participating firms. Data collected from the privatized firms participating in this project are used to construct the composite measures of enterprise restructuring. Where warranted, data collected from the *de novo* firms will be used to put the restructuring results into a broader perspective. While not strictly a control group, because the *de novo* firms encompass different sectors of the economy, the comparison is useful for highlighting how Russian firms in general are managing to cope with adverse economic conditions.

To evaluate the nature and scope of enterprise restructuring, three composite measures are developed. For each, the "restructuring threshold" is achieved when the firm responds positively to one-third of the variables included in the composite measure. "Active" (firm-initiated) restructuring is designated by positive responses to over 55% of the variables included in the composite measure. These levels (33% and 55%), while arbitrarily established, are based on my observations over the past eight years of nearly 200 firms in Moscow, Novosibirsk, Taganrog and Volgograd. If the levels are set higher (55% and 75%), the number of firms designated as restructuring falls (by about half), but the rank order of firms by positive responses remain the same. Regardless of where the levels are set, the composite measures capture the restructuring activities of former state-owned firms more accurately than any single variable.

The first composite measure, ***Restrct1***, focuses exclusively on changes in the assortment of production because of the predominance of this indicator in the restructuring literature. Eighteen variables, equally weighted, are included in ***Restrct1*** (see Table 1). The "restructuring threshold," a positive response to one-third of the variables, is six for ***Restrct1***. "Active" restructuring requires more than ten positive responses. Given that changes in the main assortment of production are less costly the lower the capital intensity of the production process - assortment changes among food processing firms are more easily accomplished than among machine building firms, for example - ***Restrct1*** is likely to be industry-biased with regard to measuring restructuring success.

The second composite measure, ***Restrct2***, designed to capture as broadly as possible the restructuring process, includes a total of thirty-three variables, representing all three categories of restructuring activities: change in management/organization, change in production assortment, and change in employment (see Table 1). As with ***Restrct1***, each variable is given an equal weight. A positive response to eleven of the thirty-three variables puts a firm over the "restructuring threshold." A positive response to more than seventeen variables signals "active" restructuring.

The distribution of variables in ***Restrct2*** across the three categories of restructuring activities is unequal -the number of variables related to changes in production (18) is at least double that of the variables related to changes in employment (9) and changes in management/organization (6). Thus, ***Restrct2*** is biased in favor of firms that have been active in production changes, which may reflect changes in demand conditions rather than active restructuring efforts, and may, as described above, introduce an industry bias in the evaluation of successful restructuring. Consequently, a third composite measure of restructuring, ***Restrct3***, imposes weights so that each category (management, production, employment) contributes equally to the outcome. In effect, introducing the weights reduces the number of variables, so ***Restrct3*** utilizes the same threshold values as ***Restrct1***: the "restructuring threshold" is six; "active" restructuring requires a score of ten or more points.

In what way will these composite measures be used? The first objective is to identify the distribution of scores by the privatized firms participating in this project: how many former state-owned firms achieve the "restructuring threshold;" how many fall into the category of "active" restructuring? The second objective is to identify the activities typically associated in the literature with enterprise restructuring that are **not common practice** among privatized firms. It is important to know, for example, whether or not the majority of privatized firms have replaced top-level managers or discontinued the free provision a wide array of social services to their employees. While a large representative sample of the population of privatized firms in Russia would be invaluable, case study information also is indispensable for evaluating patterns in restructuring activities. The third objective is to identify systematic differences between privatized and *de novo* firms in response to economic conditions. While *de novo* firms cannot act as a control group for gauging the restructuring efforts of privatized firms because they incorporate rather different initial conditions and ongoing activities, response patterns from managers of *de novo* firms help to illuminate the economic environment in which Russian firms operate. When designing or adopting policies to improve business conditions, it is important to know, for example, whether response patterns differ significantly between the two types of firms for any given variable influenced by the economic environment. If so, the policy outcome will vary depending upon the relative share of privatized and *de novo* firms in the community.

III. Sample Characteristics

Of the 35 former state-owned firms contacted in the June and October 1999 to participate in this project,[8] 32 completed at least three-quarters of the designated questionnaire, for a response rate of 91%. The ownership distribution of privatized firms participating in this project includes: 22 registered as joint stock companies (of which 6 were "closed"), 4 registered as privately-owned, and 6 registered as partnership. The industry distribution of these firms includes: 3 in transportation, 4 in construction and construction materials, 10 in heavy industry, 3 in light industry, 6 in food processing, and the remainder in utilities, R&D, and services.[9] Workforce size among the participating privatized firms ranged from under 20 employees to over 10,000 employees. Of the twenty-seven firms responding to questions about capacity utilization,[10] nine reported capacity utilization at 50% or less for the current month; eighteen top-level managers reported capacity utilization exceeding 60% at the time they completed the questionnaire. In comparison to capacity

[8] The population of former state-owned firms in Taganrog was, for the first time in the city's history, available in a telephone directory. About half of the firms were contacted initially by phone; the balance involved an initial contact by person. Assistance with this project was provided by colleagues at Taganrog State University for Radio Engineering.

[9] All but one of the former state-owned "service" companies participating in this project are engaged in activities related to Taganrog's sea port.

[10] One question asked the respondent to report the percent of total capacity used by the firm during the current month. A second question asked the respondent to compare the percent of capacity used during the current month with the same month in the previous year.

utilization during the same month in the previous year, nine reported that their current capacity utilization was higher than in the same month in the previous year; two reported lower capacity utilization, fifteen reported the same level of capacity utilization. Sixteen firms reported exporting; of these, eight reported exporting to countries outside the former Soviet Union.[11]

The former state-owned firms participating in the project were not selected to be representative of the population of privatized firms in Russia, or in Taganrog. To conduct such a survey was well beyond the financial resources available for the project. The sample selection objective was to target the inclusion of firms in the following way: one-third from heavy industry, one-third from light industry (including food processing), and one-third from "other industry." More than half of the privatized firms contacted for this project were included because they participated in survey projects I conducted in previous years, and I would like eventually to be able to write up individual case studies of several of these firms. Albeit not necessarily representative, the distribution of privatized firms participating in this project by industry and ownership structure is diverse enough to capture a variety of restructuring activities and survival strategies.

Sample characteristics most informative for this paper are the positive responses by top-level managers of former state-owned enterprises to questions addressing different components of the restructuring process (see Table 1). In terms of production assortment change, for example, just under 40% reported changing their **main** assortment of production since 1992 (CHGASRT2). Yet, since 1992, at least half of the former state-owned firms added new products and new buyers. At least half since 1995 added new products (NEWPROD5), new suppliers (NEWCUST5) and obtained

[11] Firms were asked first to designate how their totals sales are distributed among buyers in local market and in regional market. Later in the survey instrument, firms were asked what percent of their total sales are within Russia, within the CIS, and to countries outside of the former Soviet Union.

new office equipment (including computers). About 40% discontinued production of at least one product (STOP92, STOP95). A similar percentage reported adding new suppliers since 1992 (NEWSUP92), although these firms were significantly more likely to have added new suppliers since 1995 (NEWSUP95). Fourteen of sixteen firms responding reported outsourcing their former activities (OURSOURC); that is, buying materials or components from other firms that it used to produce itself. Nearly half of the privatized firms participating in this project obtained new production equipment since 1995 (NEWMCH95). In terms of management/organizational change, about half of the privatized firms experienced turnover in the top-level management positions (NEWBOSS, NEWMGR). One quarter of the managers completing the questionnaire reported receiving specialized training since 1992 for their management position (TRAIN). In more than half of the privatized firms participating in this project, there is at least one block holder (person owning at least 10% of the company's shares). Fifteen of 18 firms responding reported outsiders (non-employees) owning shares in the company (OUTSIDER). In terms of changes related to employment, three-quarters of the firms **did not** expect to release workers in 1999 (RELEASE), nor did they expect to hire additional workers (HIREMORE). Just over 40% reported labor productivity improvements since 1995.

Former state-owned firms provided the data for the restructuring measures used in this paper, but the research project also involved a survey of 87 *de novo* firms conducted at the same time in Taganrog.[12] While not strictly a control group,[13] data collected from the *de novo* firms will be used

[12] Contacts were made by colleagues at Taganrog State University for Radio Engineering, as well as one official from the city administration. I do not know how many *de novo* firms were contacted about participating in the project, thus I have no concrete information about the response rate.

[13] For example, the privatized firms in this sample, in comparison to the *de novo* firms: (i) were less likely to be in services/trade; (ii) employed significantly more workers; (iii) reported that a significantly lower

where warranted to illuminate economic conditions facing Russian firms, as well as to put into perspective the restructuring activities undertaken by former state-owned firms. The industry distribution of the *de novo* firms participating in the project includes: 6 in construction,[14] 7 in light industry, 5 in food processing, 55 in retail and other services, and the remainder in R&D. The ownership distribution includes 27 firms registered as privately-owned, 51 firms registered as partnerships, and 7 firms registered as joint stock companies (of which 4 were "closed"). Of the eighty-six firms responding, 63 reported a workforce size of 20 or fewer employees, only three reported a workforce size in excess of 100 employees.

IV. Restructuring with What Success?

Three composite measures are used here to gauge the relative success of Russian firms in restructuring their operations. The first gives equal weight to 18 variables associated with changes in production assortment (see ***Restrct1*** in Table 1). Using this measure, twenty privatized firms achieved the "restructuring threshold" (positive response to at least 6 questions). This represents over 60% of the privatized firms participating in the project, and includes: 8 heavy industry firms, 5 food processing firms, 1 light industry firm, 2 construction and construction materials firms, and 3 firms in services. The anticipated industry bias - favoring firms with lower capital intensity - is not evident in ***Restrct1***: all but two of the firms in heavy industry and two of the four firms in

proportion of their workforce showed up regularly for work; (iv) were less likely to be considering hiring additional workers in the coming year; (v) were less likely to pay wages on time; (vi) reported paying a significantly lower percentage of sales revenues to tax authorities; (vii) were more likely to be involved in export activities; (viii) were more likely to have a marketing department; (ix) were more likely to be involved in barter transactions, (x) were headed by significantly older managers; and (xi) were significantly more likely to be adding new products or services. However, there were no significant differences between privatized and *de novo* firms in terms of recent changes in the volume of activities, or the purchase of new equipment.

[14] None of the *de novo* firms manufactured construction materials.

construction and construction materials achieved the “restructuring threshold;” only one in three of the light industry firms was similarly successful. It is not surprising that the R&D organizations participating in the project are not included in this composite measure of restructuring. R&D organizations -especially those which remained in operation at the end of the 1990s -tend to involve low capital intensity but specific human capital. That they are not responding positively to changes in assortment may indicate that they are satisfactorily filling a market niche. Similarly, transportation firms in the 1990s may have faced little need to change their main assortment of services.

Of the twenty privatized firms which achieved the “restructuring threshold,” nine attained the “active” restructuring designation, where positive responses to at least 11 questions signal firm-initiated restructuring. These include: 4 firms in food processing (2 bakeries, 1 fish processing, 1 brewery),[15] 4 firms in heavy industry (of which, two formerly were engaged in defense production, and one supplies materials to the oil industry),[16] and one firm in construction and construction materials supply. Noticeably missing in the “active” restructuring category are the light industry firms participating in this project.

The top three performers with regard to ***Restrct1***, each answering “yes” to 13 of the 18 production assortment change questions, are all in heavy industry; all are open joint stock companies. All report at least one block holder; outsiders own from 30-55% of the shares in these companies. Employment in these firms ranges from 200 - 10,000 workers. All have experienced top-level

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[15] Assortment changes by these food processing firms included, for example: developing new types of beer, adding dark bread, buns and cakes, adding non-alcoholic beverages, and adding new canned goods into the production assortment

[16] Assortment changes by heaving industry firms included: construction of road barriers, construction of security gates and security devices, construction of corrosive-proof pipes, bricks manufactured according to

managerial change. With regard to the restructuring variables, all three report acquiring new production machinery since 1995, yet they still report the need to renovate between 25% and 60% of their capital stock. Despite having vehicles, none of these firms added transportation services since 1992. Differences between these firms arise with regard to outsourcing (2 of 3 do not), discontinuing a product line since 1995 (2 of 3 did not), and receiving management training outside of Russia (2 of 3 did not). In contrast to other privatized firms participating in this project, these three were **less likely** to be selling to new buyers or buying from new suppliers.

Regarding changes in production assortment, **what is not being done** by the thirty-two privatized firms who participated in this project? Given that these firms report needing to renovate on average over 50% of their capital stock, it is not surprising that less than half of the firms report any change in their main assortment of production; three-quarters report not changing or improving the quality or characteristics of any product in their assortment. Approximately three-quarters of the firms did not eliminate any products from their assortment, although 60% report adding new buyers. Less than half of the firms reported the acquisition of new production machinery.[17] None spent money on research and development in the previous year. Rather surprisingly because of its revenue-generating potential, only two of the thirty-two privatized firms participating in this project reported adding transportation services.[18]

The second composite measure, ***Restrct2***, incorporates changes in production, management,

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Italian technology, and production of consumer goods, including televisions, for example.

[17] While the correlation coefficient between NEWMCH95 and ELIMPROD is rather low (0.22), there is a stronger correlation (0.46) between the acquisition of new production machinery and improvements in product quality (IMPROVE).

[18] This stands in marked contrast to the *de novo* firms participating in this project –36% of these firms added transportation services in the last two years.

and employment, giving equal weight to the thirty-three variables associated with enterprise restructuring (see Table 1). Fourteen of the privatized firms participating in this project achieved the "restructuring threshold" of 11 points. Not surprisingly, given the dominance of production assortment variables and the equal weights assigned to each variable in ***Restrct2***, of the fourteen that achieved the "restructuring threshold" in terms of this broader measure, seven were part of the "active" restructuring group using ***Restrct1.*** The newcomers include two companies engaged in activities related to the sea port (ship loading, ship repair), one firm in construction materials, one machine tool firm, one bakery, one firm making electronic devices, and a firm that leases equipment and other materials. All of these firms report at least one block holder; all but two report outsiders owning shares -between 15% and 55%. All replaced the production manager at least once since 1992; all but one experienced a change in the director since 1992. The majority of these firms have introduced new products, improved the quality of existing products, found new buyers and suppliers, acquired new production machinery and established a marketing department. The majority report timely wage payments. The majority have reduced expenditures on benefits/social services, in part by reducing the range of benefits offered and in part by reducing the number of workers employed to provide these services.[19]

Seven firms achieved the "active" restructuring designation using ***Restrct2***. These include three firms in heavy industry, one construction and construction materials firm, one food processing firm, and one firm in services. If these data do reflect the broader population of privatized firms in Russia, the result that less than 25% of the former state-owned enterprises are actively engaged in restructuring activities does not bode well for the future. Nearly a decade after Russia initiated its

[19] The majority of these firms, like the other privatized firms participating in this project, have not transferred benefits to municipal authorities.

transition process to a market-oriented economy, it would still appear that the Soviet legacy is hampering the performance and survival potential of the vast majority of manufacturing firms.

What are the firms who achieved the "restructuring threshold" using ***Restrct2*** **not doing** in terms of restructuring? The majority, like the rest of the privatized firms participating in this project, have not discontinued a product line, and consequently do not report outsourcing any of their activities. Few are spending on research and development. Half report no labor productivity improvements since 1995, yet more than half are not expecting to release any workers this year. More than half do not charge employees for social services offered by the firm.

In the final composite measure of enterprise restructuring, ***Restrct3***, weights were applied to each of the three categories of restructuring activities (management/organization, production assortment, employment) in order to equalize its contribution to the measure despite the difference in number of variables by category. The objective was to see if the relative performance of the firms with regard to the number achieving the "restructuring threshold" changes from that which emerged when all variables were equally weighted. Because the weighting scheme effectively reduces the number of variables included in the measure, the threshold levels established for ***Restrct3*** equal those of ***Restrct1*** (see Table 1).

Using ***Restrct3***, sixteen firms achieved the "restructuring threshold," exactly half of the former state-owned firms participating in this project. Six are firms in heavy industry, three firms are in food processing, two are in construction and construction materials, two are in light industry, and three are in "other industry and services."[20] Included in this group are four firms which did not emerge using the previous measures: an R&D organization, a tannery, a transportation firm, and a

[20] This category includes firms in transportation, utilities, R&D and other services.

clothes manufacturer. Indeed, using ***Restrct3***, at least half of the firms in each of the industries included in the sample are engaged in restructuring activities. While the number of firms achieving the restructuring threshold is not significantly greater using ***Restrct3*** than using the previous measures, the composition of firms included in this group is more diverse.

The six firms designated as engaged in "active" restructuring using ***Restrct3*** include three in heavy industry, one in construction and construction materials, one in food processing and one in services. Five of these six emerge at the top of the ranking under ***Restrct1*** and ***Restrct2***, as well. Noticeably absent in any of the "active" restructuring categories are the firms in this sample in light industry and transportation.

What information do we now have about restructuring patterns of former state-owned enterprises? This case study of thirty-two privatized firms in Taganrog, Russia, suggests several patterns. First, when defined broadly to include several dimensions of the restructuring process, the "restructuring threshold" is achieved by half of the privatized firms participating in the project. The firms achieving this threshold are distributed across all industries included in the sample.[21] Based on this, I would argue there is no inherent industry bias against restructuring,[22] but that the obstacles facing light industry firms in Russia (consumer attitudes toward Russian-made goods, the availability

[21] This statement is true if utilities firms are included in the category of "other industry and services," rather than as a separate industry. None of the utilities firms scored enough points to achieve the "restructuring threshold" using any of the composite measures.

[22] Using probit regression analysis, with CHGASRT5 (CHGASRT2) as the dependent variable for 1995 (1992) and dummy variables for each industry as the independent variables, it is the case that when using the heavy industry firms in this sample as the comparison group, there are no significant differences by industry in either year. Moreover, in terms of the response patterns by managers to the question involving the percentage of their capital stock that needs renovating, there also are no significant industry differences. That is, when RENOVATE is the dependent variable, and dummy variables for each industry are the independent variables, with heavy industry firms are the comparison group, no industry emerges as better or worse off than heavy industry.

of cheap imports, for example) may be more severe than for other industries.[23] If the "restructuring threshold" is raised from 33% to 55%, for example, the light industry firms no longer are included in the restructuring group.

Second, regardless of the composite measure used, more than one-third of the former state-owned firms who reached the "restructuring threshold" also attained the "active" restructuring designation.[24] Is the "active" restructuring threshold (55% positive responses required) too low? Raising it from 55% to 75% reduces the number of firms attaining the designation, but it is still the case that at least two of thirty-two former state-owned firms achieve this higher threshold level: using ***Restrct1,*** one firm in producing steel pipes, one firm producing machine tools are included in the "winning" group; using ***Restrct2***, the steel pipe manufacturer and a construction and construction materials company are included; using ***Restrct3***, these same two firms, plus a machine tools firm are included in the "winning" group. What is to be gained from raising the threshold? Raising the "active" restructuring threshold from 55% to 75% eliminates from the "winning" group at least three former state-owned firms that I know, based on numerous on site visits and in-depth interviews, have undertaken firm-initiated changes over the past eight years to improve the operation and performance of the company. Raising the threshold provides a more conservative estimate of the number of firms actively engaged in restructuring activities, but I do not think the estimate is more accurate than that

[23] A measure of the severity of the impact by industry involves changes in workforce size. All data suggest that Russian firms were reluctant to release workers in the early stage of the transition process (see Goskomstat 1999, Standing 1996, Clarke 1998, for example). In this project, respondents were asked to report the percentage of their workforce released in 1992, and a separate question later in the survey instrument asked them to report the percentage of their workforce released in 1997. The light industry firms participating in this project released a significantly greater share of their workers in 1992 than any other industry group in the sample; there were no significant industry differences for 1997.

[24] Nine of 20 firms (45%) attained "active" restructuring designation using ***Restrct1***; seven of 14 firms (50%) using ***Restrct2***; six of 16 firms (38%) using ***Restrct3***.

which emerges when the threshold is set at 55%.

Third, production assortment changes appear to be ongoing among those firms engaged in restructuring activities: all firms that achieved the "restructuring threshold" using ***Restrct3*** who reported assortment changes since 1995 (CHGASRT5) also reported assortment changes in 1992 (CHGASRT2).[25] No significant difference by industry emerges with regard to this result.[26] It does not appear to be the case, however, that changes in the main assortment of production are highly correlated with product termination.[27] More highly correlated to assortment changes are the introduction of a new product (the correlation coefficient is 0.56 between CHGASRT2 and NEWPROD2;[28] the correlation coefficient between CHGASRT5 and NEWPROD5 is 0.60), and the hiring of a new production manager (0.43 for assortment changes in 1992 and 0.49 for those taking place since 1995).

Fourth, employment changes appear to involve a mixed strategy with regard timely wage payments, workforce size, and the benefits package. For example, even among the firms achieving the "restructuring threshold" using ***Restrct3***, one-quarter were not up-to-date with regard to wage payments; although half of these firms reported an improved situation with regard to wage arrears in comparison to 1995. There was no significant difference between the firms achieving the

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[25] For all privatized firms participating in this project, the correlation coefficient between production assortment change in 1995 and 1992, CHGASRT2 and CHGASRT5, is 0.93.

[26] The only industry effect that emerges with regard to production assortment changes is when CHGASRT2 is used as the dependent variable, and dummy variables for industries included in the sample are used as the independent variables, with "other industry and services" used as the comparison group. In this situation, food processing firms are significantly more likely to respond positively to assortment changes in 1992.

[27] The correlation coefficient between change assortment in 1992 and stop product in 1992 is 0.38; for 1995, the correlation coefficient between these to variables is 0.17.

[28] Interestingly enough, the correlation between change assortment in 1992 and the percent of workforce released in 1992 is -0.32.

"restructuring threshold" using ***Restrct3*** and those who did not in terms of the percent of their workforce that was released in 1992 (on average, 22% and 24%, respectively), or in 1997 (7% and 5%, respectively). Fifteen of the 16 firms achieving the "restructuring threshold" using ***Restrct3*** **did not** transfer benefits to local authorities to provide.[29] Only half of the firms achieving the "restructuring threshold" using ***Restrct3*** reduced the number of employees engaged in the provision of benefits/social services; half require employees to pay for benefits; over two-thirds reduced spending, in real terms, on benefits to workers since 1995. There are no discernable industry or ownership differences in these results.

Finally, outsider ownership is more prevalent among the group of firms designated as restructuring than among those firms that failed to achieve the "restructuring threshold." That is, among the firms achieving the "restructuring threshold" using ***Restrct3***, outsiders own 50% of the transportation company, 10% of the service company and one of the construction companies (the second is privately-owned). Outsiders are reported to own 15% of one heavy industry company, 30% of a second heavy industry company, and 55% of the third heavy industry company included in the restructuring group. Both the light industry and food processing firms report 15% outside ownership. The R&D firm reports no outside owners. In only four of the eleven firms below the "restructuring threshold" using ***Restrct3*** that answered the question was an outside owner reported.[30]

Regarding the concentration of shares, while half of the privatized firms participating in the project report at least one block holder, among the firms achieving the "restructuring threshold" using

[29] None of the firms below the "restructuring threshold" did so.

[30] Among all the privatized firms answering this question, outside ownership averaged 15% for the restructuring firms, and 7% for the non-restructuring firms.

Restrct3, more than two-thirds report at least one block holder.[31]

Having identified and analyzed the firms achieving the restructuring threshold, the third objective addressed by this case study is: How do privatized firms compare with *de novo* firms in terms of changes in organization, operations, and employment?

Regarding organizational changes, the most striking difference is the addition of transportation services: 36% of the *de novo* firms compared to 6% of the privatized firms added transport services to their range of activities. *De novo* firms were less likely to have a marketing department: 25% compared to 38% of the privatized firms. For firms participating in this project, the existence of a marketing department is positively correlated to the export experience of the firm.[32] For privatized firms, the correlation coefficient between export experience and having a marketing department is 0.58 (for exports outside of the former Soviet Union) or 0.74 (for exports outside of Russia); for *de novo* firms, the correlation coefficients are 0.03 and 0.16, respectively.

Regarding changes in operations, fifteen of the twenty-seven privatized firms responding to the question reported capacity utilization the same in 1999 as in the comparable month in 1998; one-third reported a decline in capacity utilization. In contrast, one-third of the *de novo* firms participating in this project reported an increase in the volume of operations in comparison to the same month in 1998. One quarter reported a comparable level of operations. Thirty-three *de novo* firms reported their volume of operations to be lower in 1999 than during the comparable month in 1998. *De novo* firms were no more likely than privatized firms to add new services or activities

[31] Of the five restructuring firms that **did not** report block holder, three are in heavy industry, one is in light industry, and one is in food processing.

[32] That is, 25% of the privatized firms participating in this project reported exporting products outside of the former Soviet Union; 57% exported outside of Russia. Among privately-owned firms, the comparable figures are 11% and 24%, respectively.

(51% compared to 55% since 1992 or 48% since 1995), but were significantly more likely to be adding new suppliers (67% compared to 48%), new buyers (82% compared to 59%), and new equipment (64% compared to 47%). Interestingly enough,the *de novo* firms were even **less likely** than privatized firms participating in this project to discontinue products or services (24% compared to 39%).

Regarding changes in employment, it is first important to note the relative size of the privatized and *de novo* firms participating in this project. The former employ on average 781 workers; the latter, 25 workers. Among privatized firms, the mean response by the top-level managers completing the questionnaire was that over 85% of their employees show up regularly for work. Correspondingly, according to the *de novo* firms participating in this project, 95% of their employees show up regularly for work. While 22% of the privatized firms were planning to hire additional workers in 1999, 41% of the *de novo* firms had plans to do so. Ten percent of the *de novo* firms compared to 25% of the privatized firms expected to release workers. While there was a significant difference between the responses of managers in the privatized and *de novo* firms in the reported timeliness of wage payments to employees -59% of privatized firms reported no wage delays, 88% of the *de novo* firms report timely wage payments -there was no significant difference between them in terms of their response patterns to providing benefits to employees: just over a third responded affirmatively. Managers of *de novo* firms were significantly younger and significantly more likely to have received specialized training (37%) than managers of privatized firms (25%), although managers of privatized firms, if they received training, were more likely to have participated in training programs outside of Russia (10% compared to 5% of the mangers of the *de novo* firms participating in this project).

While differences outnumber similarities between the privatized and *de novo* firms participating in this project, it remains instructive to compare the operation and performance of both types of firms in order to obtain a broader picture of the economic conditions and business environment in Russia.

IV. Conclusions

This case study of thirty-two former state-owned enterprises in Taganrog, Russia, utilizes three composite measures to gauge the relative success of their restructuring efforts. When a "restructuring threshold" of 33% positive responses is applied to the broadest composite measure, ***Restrct3***, half of the privatized firms participating in this project achieved the threshold level. These include firms from each industry included in the project: heavy industry, light industry, food processing, transportation, construction and construction materials, and "other industry and services." Yet, less than 20% of the former state-owned firms attained the "active" restructuring designation. That is, fewer than one in five firms participating in this project responded positively to over 55% of the requisite questions. Firm-initiated restructuring, while occurring among firms in heavy industry, food processing, construction and construction materials, and services, was not typical among the former state-owned enterprises in this case study. This result is hardly surprising, given the aggregate data describing production, investment and employment throughout the 1990s, as well as what is known about the legal and financial environment in which Russian firms operate.

While this case study is not at odds with the larger picture of enterprise restructuring and economic transition in Russia, these data and results do much more than simply confirm what we already know. The case study results indicate, for example, that among the former state-owned enterprises participating in this project, ownership structure differs significantly between the firms that are restructuring and firms that are not: firms engaged in restructuring are more likely to have outsiders own shares, and are more likely to have at least one block holder. With regard to production assortment changes, restructuring firms are more likely to have introduced new products, added new buyers and suppliers, and acquired new production equipment than firms not engaged in restructuring. Moreover, production assortment changes appear to be ongoing for those firms that achieved the "restructuring threshold." Finally, firms achieving the "restructuring threshold" are more likely to have reduced the range of benefits offered to employees, as well as to have reduced the number of employees engaged in the provision of social services at the firm. Only one of these firms, however, reports transferring to local authorities at least some portion of the social services formerly offered by the firm.

The case study results also indicate a number of areas where restructuring firms might still need to devote more attention. For example, firms achieving the "restructuring threshold" reported not experiencing labor productivity improvements since 1995, yet they are not necessarily more likely to report plans to release workers than other privatized firms participating in this project. Moreover, they are not any more likely to charge employees for social services offered by the company. Nor do they report discontinuing the production of a product line or service.

When asked what they would need to successfully restructure their firm, top-level managers report "money." While money would certainly be helpful, it appears to me that the Soviet production and employment legacy are still strong enough among former state-owned enterprises to undermine the effective utilization of additional financial resources. Moreover, all firms participating in this project, privatized and *de novo* alike, reported obstacles imposed by the federal (including customs) bureaucracy, the tax system, the inadequate enforcement of existing laws, as well as by ineffective and inappropriate regulations and inspections, and corruption as more problematic than financing in terms of their operations and performance.

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Table 1: Composite Measures of Enterprise Restructuring

Index 1	***Production Assortment Change***	***% Yes***	***N***	
CHGASRT2	Has the company changed the main assortment of production since 1992?		39	31
ELIMPROD	Has company eliminated one or more products since 1992?	44	16	
IMPROVE	Has the company changed or improved quality or characteristics of product since 1992?	50	16	
NEWPROD2	Has the company added new products since 1992?		59	29
TRNZPRT1	Has the company added transport services or changed transport activities since 1992?	7	30	
STOP92	Has the company discontinued production of any products since 1992?	42	31	
NEWSUP92	Has company added new suppliers since 1992?	43	28	
NEWCUST2	Has company added new customers (buyers) since 1992?	69	29	
CHGASRT5	Has the company changed the main assortment of production since 1995?		42	31
NEWPROD5	Has the company added new products since 1995?		50	30
STOP95	Has the company discontinued production of any products since 1995?	39	31	
MKTGDEPT	Does company have a marketing department?	39	31	
NEWMCH95	Has company obtained new production equipment since 1995?	48	31	
COMPUTR5	Has company obtained other new equipment - office equipment, computer - since 1995?	72	32	
RDNOW	This year, is the company spending money on research and development?	25	32	
OUTSOURC	Does the company now buy materials or components that it used to produce itself?	82	16	
NEWSUP95	Has company added new suppliers since 1995?	50	30	
NEWCUST5	Has company added new customers (buyers) since 1995?		63	30

Index 2	*Management / Organizational Change*	*% Yes*	*N*	
NEWBOSS	Has the company replaced or acquired a new director since 1992?	47	32	
NEWMGR	Has the production manager been replaced since 1992?	52	31	
TRAIN	Since 1992, have you received specialized training for this job as manager/director?		25	32
WEST	Have you received management training outside of Russia?	10	31	
BLOCK	Does anyone own a block of shares - 10% or more shares owned by 1 person/organization?		57	28
OUTSIDER	Do non-employees -outsiders -own shares in this company?	83	18	

Index 3	***Employment Change***	***% Yes***	***N***
RELEASE	Do you (does the company) expect to release workers this year?	25	32
HIREMORE	Does the company expect to hire additional workers this year?	23	31
PRODUP95	Has labor productivity improved since 1995?	47	30
BENEFITS	Does the company offer employees any social services or benefits?		35
			31
TRANSFRB	Has the company transferred social services to municipal authorities since 1992?	6	31
FEEFORB	Has the company transferred expenses for social services to employees; that is, the company still provides the service or benefit, but employees must pay for the service or benefit?	40	30
REDUCEB5	Since 1995, after adjusting for inflation, has the company reduced spending on social services?	58	24
REDUCEB2	Has the company reduced the number of social service employees since 1992?	67	18
PAYWAGE	Is the company up to date in payment of wages to workers?	59	32

Restrct1 ***Index 1, equal weight on all 18 variables***

Number of firms scoring < 6	10
Number of firms scoring 6 - 10	11
Number of firms scoring > 10	9

Restrct2 ***Sum of Index 1-3, equal weight on all 33 variables***

Number of firms scoring <11	13
Number of firms scoring 11- 17	7
Number of firms scoring > 17	7

Restrct3 ***Sum of Index 1-3, each index with equal weight***

Number of firms scoring < 6	11
Number of firms scoring 6 - 10	10
Number of firms scoring > 10	6

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