

THE KEY COMMANDMENTS FOR DOING BUSINESS IN RUSSIA

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EXECUTIVE SUMMARY

Russia possesses many opportunities for the development of business. It is the world's largest country in terms of territory, possesses vast natural resources, has a population of over 140 million people, has had of the world's fastest GDP growth rates of 7.4% from 2001-2008, and has less competition in many industries than in many countries. Like many countries, the global financial crisis caused some challenges for Russia in 2008, but Russia still obtained a 6% GDP growth in 2008 (World Fact Book, www.cia.gov, viewed June 19, 2009).

Russia, however, also has a dynamic, unique, challenging, and sometimes complex business environment that has caused problems for some foreign firms. As a result, many associate risk rather than opportunity with Russia. There is no denying that doing business in Russia is not for the faint at heart. The difficulty in understanding Russia's business environment, however, can also be an advantage as it serves as an entry barrier that assists those who do enter and learn to operate effectively to reap higher returns.

Based on interviews with executives from 36 foreign firms operating in Russia and supplemented by our extensive experience in Russia as executives, consultants, executive trainers, and researchers over the last fifteen years, this article suggests eight commandments that will enable foreign firms to avoid mistakes and skip the trial and error learning required of many of their predecessors to achieve success.

THE KEY COMMANDMENTS FOR DOING BUSINESS IN RUSSIA

Russia is the world's largest country spanning 11 time zones and has business opportunities equal its size. Indeed, today Russia offers exciting business opportunities propelled by significant growth in the economy as evidenced by an average gross domestic product (GDP) growth rate of 7.4% per year from 2001-2008. Like in many countries, the global financial crisis has caused some challenges for Russia in 2008, but Russia still achieved a 6% growth rate in GDP in 2008 (World Fact Book, www.cia.gov, viewed June 19, 2009).

In Russia it is not uncommon to hear businessmen discussing possible investment opportunities and saying that anything less than a 30% return on investment is uninteresting. However, large risks are also associated with doing business in Russia, and thus for many observers when they hear the word Russia it is the word *risk* rather than *opportunity* which comes to mind. There is no denying that doing business in Russia is not for the faint at heart. However, Russia's unique, challenging, and sometimes difficult to understand business environment can also be an advantage as it serves as an entry barrier helping those who enter and learn how to operate effectively reap higher returns.

With one of the fastest GDP growth rates in the world in recent years, substantial growth in purchasing power (more Mercedes cars are sold in Moscow than in Berlin today and dollar denominated wages grew on average more than 400% from 2001-2007), a population of 144 million people (World Fact Book, www.cia.gov; Goskomstat, www.gks.ru; viewed June 19, 2009), and a relative lack of competition in some sectors, Russia shows some signs of becoming an attractive destination for foreign investment. Indeed, diverse international companies such as Raiffaissen Bank, Telenor, McKinsey, SAP, Tetra Pak, Phillip Morris, Mars, Wrigley, and McDonalds have already penetrated the Russian market and enjoyed success. Their successes support our view that today Russia presents good opportunities for skillfully-designed foreign investment projects that take into account local specifics. The challenge for foreign firms

starting businesses in Russia is to determine how to mitigate the risks and capture the profits. This article addresses that challenge.

The article aims to enable foreign firms and individuals interested in doing business in Russia to move further up on the learning curve and thus avoid mistakes that many foreign firms have previously experienced when launching operations in Russia. Based on interviews with executives from 36 foreign firms operating in Russia (see Table 1 for a list of companies interviewed) and supplemented by our extensive experience in Russia as executives, consultants, executive trainers, and researchers over the last fifteen years, we have developed eight commandments that will enable foreign firms to achieve success in the Russian market place. Appendix A briefly summarizes the methodology used for this research. Below, we present our eight commandments and illustrate each of them with examples from the firms that we interviewed.

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Commandment 1: Practice Authoritative not Authoritarian Leadership

Leaders are important in any society, and by making their followers rise to new heights, they drive economic and social progress at macro and micro levels. Such leadership also provides meaning for employees. These roles are universal; however, the way people enact them differs from country to country. Russia has a tradition of strong, larger-than-life mavericks such as Peter the Great, Josef Stalin, and World War II hero general Georgy Zhukov. The new wave of Russian capitalism confirms this tradition: regardless of a successful Russian entrepreneur's competencies and management style, he or she invariably has enormous power within the organization. Followers look to the leader as a superior being who has unique rights and, by definition, deserves compliance. Russians have a need for powerful charismatic leaders and tend to create them often irrespective of the leaders' intentions.

Russians' expectations of foreigners in leadership positions, however, are more complex. The formal title of CEO does not guarantee its holder the same level of compliance from Russian subordinates when a Russian does not hold that position. Respect and conformity will come only if the foreign leader demonstrates superior competence and delivers tangible results. When a leader is recognized as having such competence, Russian employees expect from him or her specific actions that address their problems and improve their working lives and the performance of their company. To some degree foreign executives must live up to a higher ideal than Russian managers since in Russia the general belief is that foreigners are more progressive and can do more for their staff than Russian bosses. When the above conditions are met, Russian employees led by foreign managers can perform wonders. When these conditions are not met, problems are likely to occur.

Robert Sheppard became Sidanco's de-facto president in February 1999 shortly after one of Moscow's courts declared the company, owned by Russian private shareholders and BP, bankrupt. One could hardly imagine a more difficult time to take over the leadership of a company. However, when Sheppard left Sidanco in 2002, the company was probably the most advanced oil major in the country--with hefty profits, a new business model, and as internal surveys showed, extremely satisfied employees. Sheppard changed the company by practicing what we call *authoritative leadership*--when a strong and highly-involved executive leads from authority gained from the followers by virtue of competence possessed rather than just through the power of the position.

We assert that it is important how a leader gains authority. Entering the company where turmoil and despair reigned, Sheppard remained cool, listened much to employees, traveled to regional subsidiaries, and did not rush to give orders. After this initial reconnaissance he concentrated on a limited number of issues that were key for the company's survival and on establishing his authority. Sheppard picked low-hanging fruit by introducing simple financial

controls, centralizing cash management, and sending reliable people to key jobs in the regional subsidiaries.

At meetings with Russian executives in the head office and in the regions, he demonstrated superior industry knowledge and established himself as a high authority on the oil business. He met with key external counterparts--regional governors, federal ministers, regulators, bankers--and spoke with confidence about Sidanco's future and BP's commitment to the company and the country.

Sheppard also hired a few capable Russians and expatriates and moved out some crooks and drunks. He made it clear that he was the sole point of contact for board members and shareholders and shielded his management from such forces. Using his contacts at BP, Sheppard restructured Sidanco's debt. Improved results followed his efforts: by the beginning of 2000, Sidanco had returned to the black. Its oil production was on the rise, costs were declining, and salaries and taxes began to be paid on time. People inside and outside of the company recognized success and associated it with the new leader. Sheppard had firmly established his authority, and he moved on to reform the company.

Having both significant power and a clear vision of what he wanted for the new Sidanco, he nevertheless decided to involve his subordinates in the process of designing the new organization, planning the change process, and carrying out the transformation. A team consisting of key executives from the head office and the regions met regularly and debated available options, agreed on action plans, and followed up on previous decisions. From day one of the change program, Sheppard emphasized the importance of extensive communication about the change process. To support it and ensure success, Sheppard became the speaking head for the transformation process. He communicated about the changes by frequent articles in the company's magazine, conducting town-hall meetings in the regions, and meeting with governors, suppliers, and unions. To support the change program, Sidanco made significant

investments in employee development and created a corporate university where Sheppard was president and an instructor.

Sheppard launched the change program, established the general direction, set limits, and developed well-defined targets and criteria for success, but he left his subordinates enough room for creative implementation. In addition, Sidanco's newly-created compensation and review systems reinforced the spirit of executives' individual and collective accountability. Gradually withdrawing himself from day-to-day management, Sheppard spent much time and effort selling the change program to the board and winning its support. As Bob Sheppard said:

I could fix one or two things single-handedly, but I never would have succeeded in implementing the vision of "Operational Excellence" alone. There was no choice but to get other people involved. And they, at the end, responded very positively, even though initially they spent an enormous amount of intellectual energy explaining to me why that could never be done in Russia. But, you have to be firm in important things and use your authority. Later in details you can, and even should, be very flexible.

We can also learn from the experience of others what not to do. Ron Chapman (a pseudonym) also led a multinational manufacturing and service company's expansion into Russia. The company swiftly established a number of joint ventures with local partners, and Ron decided to appoint representatives of the Russian parents to be General Managers(GMs) of the joint ventures and manage his firm's Russian operation through them.

A seasoned international executive with experience in the US, Japan, Taiwan, and Western Europe, Ron believed in delegation of authority, management by objectives, and a hands-off approach. He worked with his GMs through semi-annual country meetings usually held in resorts outside of Russia, annual performance reviews, casual visits to the factories, and informal meetings over a meal. He never interfered with operational issues but left these to the GMs. Chatman judged the managers by year-end results. When the results were not as good as hoped for, Ron blamed them on unfavorable external conditions that were likely to improve in the future and thus normally recommended to pay his GMs full bonuses.

Chapman felt that his Russian GMs were his key asset and tried to do everything he could to support and protect them. For example, he helped one general manager to send his daughter to the US to study, financed an apartment for two other GMs, and arranged medical treatment abroad for the fourth one. When expatriate deputy GMs criticized their bosses or brought to Ron's attention problems at the JVs, the Country Manager publicly sided with the GMs and then tried to address the issues behind closed doors.

Ron Chapman was overall pleased with the way the business was developing in Russia when he received his first unexpected blow. One of his GMs left the company to return to his old factory—the Russian partner in the JV, which he had secretly privatized. With the new owner turned CEO, the competitor factory modernized its product, launched an aggressive sales campaign, and became a significant competitor for the multinational. Just one year later an internal audit found that another GM had used company assets for personal enrichment and had conducted some questionable transactions with suppliers. Ron was furious. He felt that he was personally betrayed by his protégé and immediately fired the GM.

Unfortunate events continued for the firm. The whole group of young high-potential managers, who had spent a year at the multinational's operations in the US, left the company's largest Russian JV, citing the authoritarian style of its GM as the reason for their departure. Just a month later three senior managers followed suit and started a service company to compete with the JV. The multinational's market share started to decline rapidly and it lost its leading position. Soon its financial results began seriously to worry its parent company. Ron was transferred to managing another country, and the JVs were consolidated into one legal entity, which is still struggling.

One of the GMs who worked for Ron described him as “a nice guy, but a weak leader who did not know or care about the business.” Ron's subordinates took his informality for weakness, hands off style for lack of professional knowledge, and empowerment for lack of interest. Having established that diagnosis early on, they went on to work on their own agendas,

which often had little to do with the multinational's vision for Russian operations. Ron chose a style that was unknown, and therefore incomprehensible, to his followers. In contrast, Sheppard chose to establish his authority first and to teach his followers his style from the position of authority. These cases indicate that it is important to match leadership style with followers' expectations and readiness.

Foreign executives who become effective in Russia realize the importance of choosing leadership styles that work in Russia. They establish, recognize, and use their authority to promote what INSEAD professor Manfred Kets de Vries calls an organizational model based on 3Is – information, involvement, and innovation. They start by assuming responsibility for company results and its people and proving their leadership capabilities. They lead from a position of power, but they articulate and communicate to the followers a compelling vision for the future. They deliver superior results by focusing on people; they respect employees as human beings and demand the same level of respect from them; they involve followers in the process of deciding where to go and how to get there; they share information, responsibility and success; they develop trust by walking the talk and having others accountable for their words and deeds also; they develop, support, and personally mentor their followers; and they instill a culture of development and innovation. Acting in this way, they tap the better qualities of Russian employees—creativity, loyalty, endurance, curiosity, resourcefulness, and the ability to work hard—to create great momentum and produce outstanding results.

Commandment 2: Build a Strong One-Company Organizational Culture with Visible Foreign Elements

Our research has found that a strong organizational culture with clear sustainable organizational practices that are used to achieve specific goals has a positive correlation with high-performance in Russia. In the decades of communism most Russian organizations were dull places to work because they provided little meaning or opportunity for the majority of their

members. Office politics, double ethical standards, murky procedures, and unclear goals reigned. Companies that emerged during the first decade of Russian capitalism often suffered from the same diseases of non-transparency and arbitrary rule. As a result, the efforts of some Western companies to build strong and transparent organizational cultures at their Russian subsidiaries have created a very positive response from most Russian employees. This type of environment emulates the famous words from the film *Field of Dreams*: “Build it and they will come.”

The general director of UPM Paper in St. Petersburg—Pavel Sarkov—summarized his firm belief in the importance of a strong organizational culture by saying:

Our organizational culture is a key element that differentiates our firm from other companies and attracts people to our company. Our company’s organizational culture here in St. Petersburg is built on three key principles which are very visible in the organization: 1. Trust – in employees; 2. Openness-- internally and externally, 3. Initiative--we want employees to contribute.

Pavel is confident that the above three principles are an effective basis for organizing. Pavel explains, “One has to trust employees or the costs are too high in terms of time needed for checking up on and controlling actions. A trusting environment is also much more enjoyable to work in and motivates employees.” At UPM the doors to all conference rooms and offices are kept open, and much of the office was designed in an open landscape format such that employees can hear much of what is going on in the company when they sit at their desks or walk through the office.

The UPM example also illustrates another important point regarding organizational culture. Many Russians are attracted to work for foreign firms to experience the organizational culture of an international firm. Thus, it is important that firms live up to their interest by having some visible foreign elements to their organizations. Although most of the specific features depend on the national origin and culture of the mother company, we found four fundamentals that Russian employees seek from their foreign employers: 1) fairness, 2) transparency, 3) meritocracy, and 4) a chance to have an impact on the organization and feel part of something

important. People familiar with Russian national culture and organizational practices know that those elements are not traditional, but when foreign employers create this type of environment, Russian employees do wonders in exchange.

The food giant Mars is another company that benefits from having a strong organizational culture with visible foreign elements that are consistent throughout the company. Mars is a special company and one can quickly feel that when one walks in the doors. It is also clearly a foreign company in terms of how it operates, and it uses this feature to its advantage to attract employees. The company is, however, conscious of the need to adapt to Russian culture and does well in this respect now that it has much experience in Russia.

Through internal processes and procedures, communication, and its leaders, Mars' culture promotes meritocracy, fairness, respect for an individual, and the feeling of being part of an elite institution. These qualities are imbued at the recruitment stage. With about 50 applicants for most managerial jobs, the company makes sure candidates know that it is only the very best who get to work at Mars. The best applicants are invited for testing that includes solving cases, taking an examination, making presentations, and having an interview. Final candidates have additional interviews. This in-depth process enables selection of the most qualified candidates—qualified not only in terms of ability but also in terms of fit with the way Mars works. This extensive selection system also has the positive side-effect of making selected employees feel as though they are part of an elite team.

Mars also has an informal atmosphere that is typically American. All employees, including managers, are called associates. Information flow between all levels is encouraged, and any employee can approach any senior executive. A positive attitude towards openness combined with an open space layout reinforces the special atmosphere of openness.

At Mars the decision making process is transparent, and great emphasis is placed on fairness. For example, in the case of a new opening any employee can apply for the job. All internal candidates are invited to go through an extensive assessment procedure that includes

making a presentation on a prescribed subject, participating in a business game, and having an interview. Human resource managers and potential future managers for whom the employee will work evaluate the results. Employees' past work results do not have much weight because the question is not if the employee can do his/her current job well, but who can do the new job best.

The most important aspect of Mars' organizational culture is its focus on action and individual responsibility fostering an attitude that employees should think creatively to solve problems and be able to take action. Russian employees, especially those with advanced degrees, highly value opportunities to voice their opinions and to be heard by their superiors--a practice that rarely exists in traditional Russian companies.

Organizational culture can indeed have a positive impact on performance of a foreign company in Russia (Fey and Denison, 2003), but it is also a delicate management tool that can backfire if leaders do not live up to proclaimed norms and values. For example, if a foreign firm states that it values employees' opinions, then it needs to implement some ideas provided by employees or employees will lose faith in the organizational culture. This fact is especially important to keep in mind as foreign subsidiaries go through the normal cycle of decreasing the number of expatriates working at their subsidiaries as the subsidiaries become more established. At this phase many firms we have worked with have run into problems with employees claiming that their organizations have become "too Russian." Thus, as the number of expatriates at a company decreases, foreign firms need to make sure to place extra effort on maintaining their organizational cultures, especially in preserving and even highlighting the foreign elements in their organizational cultures.

Commandment 3: to Create an Empowered Organization Step by Step

Many foreign executives suggest that creating an empowered organization in Russia is their largest management challenge. Yet those who have made significant progress down the road to empowerment emphasize the positive impact that it can have on employees' motivation

and performance if implemented correctly, at a reasonable speed, and to the right extent considering employee readiness.

Traditionally, Russian organizations knew very little empowerment and both the top and the bottom of the hierarchy contributed to this situation. On the one hand, the centralized governance model permitted little decision making to occur at lower levels. On the other hand, employees were reluctant to show initiative or make decisions because of Russia's traditions of severe punishments of mistakes and non-traditional behaviors. However, some foreign companies operating in Russia such as Gillette, Microsoft, and Mars have demonstrated that empowerment can be successfully built into predominately Russian organizations.

First and foremost, firms that have been successful with empowering their employees recognize that empowerment should be a process, not an event. It cannot be implemented overnight and requires continuous step by step efforts. At the same time, empowerment should produce some visible results quickly to excite employees. Second, successful firms realize that empowerment requires a profound culture change that can be achieved only when company leaders' actions coincide with their words. Two elements are especially critical here – tolerance of mistakes and refusal to make decisions that have been delegated to an empowered employee. Managers have to control their instincts to criticize an employee who made an honest mistake so as not to stifle future employee initiative. Also, managers should be willing to discuss the pros and cons of different alternatives with empowered employees when asked, but managers should avoid the temptation to make a decision on a previously delegated issue even if the subordinate asks that the manager to do this and it would be quicker.

While empowerment is a challenge in many countries, in Russia it is particularly challenging and important because of Russia's tradition of limited empowerment and severe punishment of mistakes. This tradition leads to a reluctance to make decisions even when management has delegated such power and when employees themselves wish for more power.

Below, we provide some examples of companies that have worked hard to create more empowered organizations by following the above principles with some success.

Gillette employs about 650 workers at its factory in St. Petersburg. As one way to increase empowerment and employee involvement in generating ideas, Gillette has implemented a special type of cross-functional improvement project called rapid improvement events. This situation occurs when a cross-functional team with employees from all levels of the organization is given a week off from their normal work to examine and try to solve a specific problem and implement as much of the proposed solution as possible. Gillette has gone to this intense week format because of the realization that since time is a team's most scarce resource, little progress is made when teams are competing against team members' daily work responsibilities. The ideas for these projects can be proposed by anyone and a committee of managers decides which ideas will be pursued. The teams receive good top management support when needed. The projects have proved quite successful.

In some instances when one tries to empower employees in Russia, the actions are met with some resistance. For example, one manager at Gillette commented that several times after he had delegated a decision he would find employees returning to him asking him to make the decision. He found that three tactics were helpful in solving this problem. First, the manager worked hard to explain that one can not have progress without some risk. He stressed that people who took calculated risks and failed would not be punished. He stressed that the most important factor was that everyone learned from these failures such that they occurred only once. He also publicly advertised some examples of this principle. Second, the manager developed a policy whereby he would discuss the pros and cons of different options for a decision with his employees if they came to him, but once a decision was delegated he would not make the decision himself. He also found it useful in such discussions to say to employees, "If you were me what would you do?" Putting themselves in their boss's shoes often made it easier for

employees to make the decision. Third, this manager found it was helpful to clarify explicitly which items an employee was empowered to act upon to the extent possible.

Ford St. Petersburg also has found it important to place significant effort on creating an empowered organization. Its managers acknowledge that creating an empowered atmosphere is a slow process and, unlike some companies, they acknowledge that change cannot be made overnight. Ford St. Petersburg focuses not just on empowering people to act, but also on making employees responsible for the outcome of their actions. At the same time, Ford employees are not punished for honest mistakes. As a Production Manager at the Ford factory informed us, Ford does not want to increase quality by increasing the number of inspectors. Instead, Ford wants to make employees fully responsible for quality work.

As an example of the above, if an employee knows that the threads on a screw are stripped, Ford does not want the employee to use the damaged screw to screw something into a car to save time because it was the end of the shift, because there was no replacement part, or because the employee did not know how to fix the piece. To resolve this problem, a sheet of paper is attached to each car at Ford on which employees should write remaining problems to be fixed by the next person working on the car. Ford St. Petersburg also encourages employees to see the importance of improving their work and of considering ways to prevent problems so that next time the same problem will not reoccur. The minimal first step that Ford requires is getting employees to be open about mistakes.

It is hard to find companies in Russia where employees are not punished for honest mistakes. This situation is one of the most important traditions to change if empowerment is to work. A production manager at Ford explained that Ford Russia has worked to minimize this problem by repeating time and time again that employees will not be punished for mistakes resulting from taking a calculated risk that did not work out, for highlighting a problem, or for making an honest mistake. Employees should, however, make the same mistake only once.

Changing behavior takes much effort, but Ford is convinced that such change is worth the investment as it will substantially benefit Ford's productivity in Russia.

Commandment 4: Respect Local Rules, But Play Your Own Game

“This is Russia—things are different here” is something every foreign executive in Russia hears daily, if not hourly. We do agree with the first part of this conclusion— that Russia is a distinct market with specific rules of which one needs to be aware. However, our research shows that foreign companies trying to create Russian-specific operating models by copying what local businesses do often fail, while foreign companies that intelligently apply (with some local adaptation) the business models that have helped them to succeed elsewhere more often flourish.

When the management-consulting firm McKinsey entered the Russian market in the early 1990s, many predicted a fiasco. Who needs strategy advice at astronomical prices in a country with a contracting economy, skyrocketing inflation, organized crime, and opaque privatization? Yet, within a few years McKinsey was flourishing in Russia. It managed this by providing the services McKinsey is famous for around the world—strategy-consulting to CEOs. Against some local advice, McKinsey refused to compromise on its target audience, pricing, or the quality of its work. However, it did take some local specifics into account, such as high power-concentration in the hands of the owner-CEOs, and the need for ritualism in dealing with these owners, e.g. unusually high levels of secrecy and extensive office politics.

McKinsey quickly recruited and trained many Russian-speaking consultants, but refused to provide services, such as recruiting managers and structuring deals, that its new Russian customers wanted, believing this would distract from core services. By concentrating on high-quality strategy consulting, McKinsey established itself as the unchallenged market leader. By the mid-1990s it had become fashionable among Russian business tycoons to use McKinsey's

consultants. McKinsey's strategic advice was not always followed, but it was always listened to with appreciation.

Citibank, a relative newcomer to Russian retail banking, followed a similar operating model. It didn't compete with local banks on interest rates or staff wages, but offered a civilized retail banking experience to its clients, friendly and knowledgeable staff, reliability, and transparency. The bank takes local specifics into account when it structures products, sets rates, or plans advertising campaigns, but its core business model is the same worldwide.

We have not identified any foreign company that beat local competition in Russia by privatizing assets or acquiring them below market value through sophisticated schemes or legal battles, by optimizing tax and salary payments, by getting special deals with different levels of government, or by cutting corners in the less than clear legal system. Foreign businesses cannot beat the Russians at their own game, but should be aware of how this is played so they can participate in it. Companies that fail to understand Russian specifics pay a high price for their stubbornness. Companies must respect local customs when dealing with clients, suppliers, and employees—not just speaking Russian, drinking vodka, or going to the sauna (although these are all useful) but, rather, showing interest in local people and their way of life, and incorporating this knowledge into the business's operational model.

COMMANDMENT 5: STAND FIRM ON MAJOR GOALS AND BE FLEXIBLE ON DETAILS

Some managers argue that Russian instability makes it impossible to have long-term goals but our research shows the opposite. In Russia's changeable environment, employees need clear goals to provide direction, and flexibility needs to be built into the way in which these goals are achieved. Further, contingency planning can be helpful in facilitating such flexibility.

Nicolas David, general manager of the Swedish white-goods company Electrolux's St. Petersburg factory in 2005, recognized that if the company had not followed our fifth

commandment, it would never have got started. The company's pilot phase was set to last three to five years, during which it aimed to assess whether manufacturing in Russia was feasible. Electrolux aimed to conduct this pilot project with minimal investment, and needed to rent a building for its St. Petersburg factory. Before the venture started, regional European and top Russian management drew up a list of minimum requirements, but failed to find a building that met them all. David decided to focus on the key goal of assessing whether Electrolux could create a factory that could work well in Russia, and be flexible about the building's detailed requirements. Space was found, although with the drawback of being on several floors.

Sales in the Russian market vary dramatically from month to month. Western multinational corporations (MNCs) are built around working towards stability and monitoring carefully all short-term changes in sales. They take action when sales figures go down for one month. Electrolux believes that reacting to short-term changes does not add value in Russia's unstable environment.

VimpelCom has also benefited from focusing on key goals and remaining flexible on the details of how these goals are reached. The brainchild of a young American, Augie Fabela II, and a Soviet radio engineer, Dimitri Zimin, VimpelCom became one of the two largest mobile telecommunications companies in Russia. Their goal was to become a leading mobile telecommunications provider in Russia, while providing good working conditions for their employees. They were flexible in that they switched from the AMPS 800 MHz standard to GSM and also switched from being a totally technology-driven company to becoming one of the first Russian companies to market itself as a distinctive brand (with a logo). VimpelCom then fought off Systema, one of Russia's most powerful financial groups and owner of VimpelCom's largest competitor, MTS, which had acquired the majority of VimpelCom's shares from sleeping Soviet-era institutional shareholders. It was clear that VimpelCom would not thrive under Systema's ownership, because Systema would focus on MTS. VimpelCom regained control of its destiny thanks to the significant political negotiating ability of CEO Zimin together with

Fabela's fundraising efforts among a select group of US investors. VimpelCom subsequently became the first Russian company to be listed on the New York Stock Exchange.

When the company reached a growth point where they needed knowledge about international best practice, they attracted a strategic investor, the telecom company Telenor. VimpelCom then brought in the Russian financial group Alfa Group to help the company survive and thrive in modern day Russia in which CEO Zimin's contacts and charm were not going to be enough and further funding was needed quickly to take advantage of current opportunities which would not last especially relating to regional expansion. At this transition point, Zimin and Fabela voluntarily left VimpelCom, realizing that they had achieved all they could for the company and that further growth was best served by professional management. In all of these significant changes the key goal of the firm was kept in sight--to develop a large, modern, rapidly-growing mobile telecommunications provider in Russia while providing good working conditions for its employees. It was how this goal was pursued, and not the goal itself, that had changed.

COMMANDMENT 6: LEARN TO LIVE AND MANAGE IN CRISIS

It is said that Russia is very predictable—something unexpected is sure to happen every day. Crisis-management is vital for success in Russia. Firms need to recognise that crises normally emerge in Russia because of change in the external environment, and, although initially causing problems, crises can lead to opportunities. Firms must be ready to act quickly at such times. For example, some firms in Russia, such as local food production companies, took advantage of the 1998 financial crisis and gained significant market share when imported foreign food rose in price. Other local Russian companies were so focused on the crisis that they did not recognize this opportunity until it was too late.

Senior managers must stay calm in a crisis and show employees a confident face. Managers must ask people from a range of organizations for their perceptions of the crisis, and solicit their ideas about response rather than being swayed by those whose emotions overcome their analytical ability. For example, the CEO for Russian operations of the American oil company Chevron, Trem Smith, indicated that he strives to keep calm, remain analytical, and seek opinions from different groups—e.g. government (ideally someone from the Kremlin, since state power is increasingly concentrated there today), other foreign firms, local Russian business people, independent analysts, and academic

Nonetheless, crisis-prevention is clearly better than crisis-management. Firms should develop sophisticated early warning and control systems to minimize surprises. Russian employees' prevailing fear of making mistakes means that if there is a risk a project will be late (perhaps because of unexpected external events), many Russians won't warn superiors. Instead they will work very hard to solve the problem on time: Russians can perform last-minute miracles. Sometimes, however, despite everyone's best efforts, a project runs late. It's clearly preferable for a manager to know this possibility in advance, in order to inform customers, make alternative arrangements, or take corrective action.

To deal with this, companies must emphasize that honest mistakes will be tolerated. They should also break up larger projects into smaller ones, have more checkpoints along the way, and spend more time on risk assessment, so all involved anticipate potential problems and evaluate time and alternative plans more seriously.

In International Paper's Svetogorsk plant HR director Steve Derrick realized that changes were needed when the installation of a new multimillion-dollar paper machine was delayed because of a problem with the machine's foundations. Derrick later learned that the Russian employees had known about the problem several months previously, but were afraid to say anything. As a result, International Paper has now started a program advertising that employees'

honest errors will not be met with censure. Motorola Russia has also followed a similar strategy with good results.

COMMANDMENT 7: RECOGNIZE THAT CORRUPTION IS OMNIPRESENT IN RUSSIA AND MUST BE MANAGED

Practices corrupt by western standards run through the fabric of Russian society, from schoolteachers taking cash from parents to give students better grades, to federal ministers and parliamentary deputies running private business empires. Some estimates put the size of Russia's "corruption economy" at 10–15% of GDP—a conservative estimate since it only reflects traditional cash bribes, not more sophisticated practices such as using a government job to promote private business interests (S. Johnson, D. Kaufmann, J. McMillan, and C. Woodruff, "Why Do Firms Hide? Bribes and Unofficial Activity after Communism," *Journal of Public Economics*, 76/3 (2000): 495–510).

Foreign businesses entering the country must be aware of the widespread practice of kickbacks, at all levels and must develop a specific plan to deal with corruption and not just say let's wait and see. "Grease money" is paid to all kinds of deal facilitators acting on behalf of important figures, or directly to important figures. These come in many forms including:

- "voluntary" contributions to special projects, or the funds of regional and local administrations or government departments (police, emergency services, etc.)
- traditional bribes and more complex schemes to influence courts and prosecutors
- extortion demands from power ministries (police, secret services, etc.)
- bribes in return for necessary approvals from various agencies (e.g., fire inspection, building safety inspection) or to obtain licenses (e.g., telecom frequency licenses).
- commissions to high-level officials in the case of high-profile deals requiring their authorization
- petty bribes to traffic inspectors, doctors, teachers, etc.

However, foreign companies and individuals don't necessarily have to compromise their ethical standards in Russia. The Norwegian company Telenor has been active for over 10 years

in the Russian telecom industry, infamous for murky deals. In Russia, Telenor adopted a business model it would not have chosen in other countries. It bought into existing operations instead of trying to obtain a greenfield license. Telenor partnered with local investors or outsourced certain activities, settling for non-controlling stakes. This helped Telenor sidestep the corruption almost unavoidable in obtaining a Russian telecommunications license directly. The company adjusted its business model but did not compromise its ethical standards.

Firms must also be clear about their own ethical standards. One American entrepreneur started a business in Russia in the early 1990s, but was soon in trouble and had to leave the country for six months: “I was not careful and did some things I would not have done back home. They backfired on me and I could not defend myself because I had lost my moral ground. I learned the lesson to stick to my principles.”

Several strategies enable western companies to do business in Russia, preserve their integrity, and prosper. One is to outsource corruption. Firms can subcontract some activities (e.g., bidding, dealing with regulatory authorities, and acquiring land and property) to local companies willing to deal with local customs and good at doing so. A company might make more money performing such activities in-house, but outsourcing them will help them stay clear of corruption.

Pre-emption is another strategy. Instead of waiting for local officials to offer the company a distasteful request, a company can be proactive and offer to cooperate on its own terms. For example, the Ford factory in the Leningrad region gave cars to the local police: but Ford asked the police to test them to Ford specifications and report on the performance of the cars on a daily basis—testing from which Ford benefited.

A third strategy is to enter business at a later stage, when the situation is more stable. That has been BP’s approach, after early attempts to participate in exploration projects failed. A company that follows this strategy usually pays a premium for an asset, but such a premium is often justified by lower risk.

A fourth strategy is simply to abstain. Telenor turned down several lucrative deals because it felt it could not handle the business ethically. It may have sacrificed some quick gains, but it preserved two conditions important for long-term success in Russia—integrity and consistency.

While the above strategies are helpful, the key to success is effective implementation. While flexibility is important at the design stage, firmness and consistency are critical for successful implementation. After drawing a line, it is extremely important not to cross it. Russians will continue to test foreigners' commitment to their proclaimed ethical norms. When the response is consistent with the declared approach, Russians are likely to find ways to work with a company on the latter's terms. Companies such as Telenor, United Technologies, and BP have achieved this successfully.

Commandment 8: Cultivate Relationships with Government Agencies at All Levels in Businesses and Civil Society

Government and government agencies still hold significant levels of arbitrary power that can help or hinder business, whether in the highest or the lowest echelons of government: the local fire inspector can be as difficult as a federal minister. On the day IKEA's first store near Moscow was due to open, the top management, including the company's legendary founder Ingvar Kamprad and hundreds of special guests, were shut out because at the last moment a regional bureaucrat decided that the building had not yet passed inspection.

Foreign companies in Russian must build relationships at all levels to facilitate information channels, development, and the granting of authorizations, and to protect the company from nasty surprises. Regular visits by companies to government officials, as well as invitations issued to bureaucrats to visit, and involvement in local welfare or training programs, all help. Microsoft has refused to pay any money or offer any perks to government officials yet enjoys a high level of respect and influence at both regional and national levels. Microsoft's

executives deal with government officials from a win-win perspective, explaining how specific programs will benefit Russia. They credit officials when projects are successful, and show respect to people in positions of power, using simple but effective measures, such as addressing officials properly in public, sending birthday cards, and observing similar small but significant social gestures.

Some companies successfully delegate relationship-building to their Russian managers, but this strategy only works when the latter have status in the organization. Russian government officials expect to deal with the top person in the organization. If a company does not have a Russian CEO, expatriate company leaders should persevere in such government relationship-building with support from their local staff.

Social capital is also a critical asset. When SAP expanded its operations in Russia in the mid-1990s, it realized that its normal salespeople could not penetrate industries like oil and gas or banking, since without background or contacts in these sectors, they lacked credibility. The company swiftly recruited people with an industry background and trained them about SAP, and won many important contracts.

Conclusions

Doing business in Russia will remain a challenging undertaking for the foreseeable future. Some recent moves by the Russian central government suggest that foreign companies may face new formal and informal hurdles such as restrictions on investing in certain industries without presidential approval. The economic potential of Russia, however, warrants the interest and presence of international companies, who we believe can create a great deal of value for themselves and the country. Although doing business in Russia is difficult, the fact that it is challenging also has some advantages. The current challenging atmosphere creates a situation where companies without specialized knowledge of how to operate businesses in Russia are unlikely to be successful. This lack of knowledge, however, creates greater possibilities for

those firms that acquire this knowledge to reap greater profits since their unique competence will be harder for competitors to copy.

Examples of successful businesses in Russia show that in Russia, as elsewhere in the world, leaders distinguish themselves by engaging actively and intelligently at the same time. They act, reflect on their experience and that of other firms, and continue to act with a new level of awareness. Most foreign firms in Russia, however, have had to engage in trial and error testing to develop an understanding of what works best in Russia. This approach is time-consuming and expensive.

The above commandments for doing business in Russia summarize the collective experience and recent learning of many foreign companies operating in Russia. This knowledge should facilitate the process of understanding the unique facets of how to do business in Russia and thus improve the effectiveness and efficiency of foreign companies and individuals as they enter the Russian arena. Hopefully, these principles will allow foreign companies entering Russia today to skip much of the trial-and-error learning of many of their predecessors. Our commandments create a general framework that we believe can help companies to navigate the Russian business landscape successfully. Even so, with this framework each company has to discover its unique operating model combining its core competencies with an understanding of the local specifics. This unique model can be uncovered only by reflection and experimentation. Companies, however, can reap greater success by intelligently building on the collective knowledge of those who have gone before them. As Russians say: “Knowledge is power.”

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Table 1: Companies Interviewed as Part of the Key Commandments Project

British American Tobacco
BP
Chevron
Cisco
Citibank
Delta Bank
EFES Brewery
Eghon Zender
Electrolux
Ericsson
Ford
Goldman Sachs
Huawei
Herbert Smith
Gillette
IKEA
International Paper
Kone
Lieu Commun
Mars
Marsh
McKinsey
Microsoft
Motorola
Nokia
NewsCorp
Otis Elevators
Raifaissen Bank
SAP
Stockholm School of Economics
Telenor/VimpelCom
United Technologies
UPM
Unilever
Wrigley
Alcoa

APPENDIX A: METHODOLOGY

This study is based on interviews with senior managers (in most cases the general manager) of 36 subsidiaries of foreign firms operating in Russia. Subsidiaries had to be based in the greater Moscow or St. Petersburg areas in order to be included in the study. Further, subsidiaries had to employ at least 30 employees and have operated in Russia for at least two years (such that they had experience to comment on) to be included in the study. The interviews lasted between 60 and 120 minutes. All interviews were conducted by the authors themselves.

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