

## **FINANCIAL-INDUSTRIAL GROUPS AT THE MARKETS FOR CORPORATE CONTROL AND INVESTMENTS: THE CASE OF UKRAINE**

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### **Abstract**

This article is devoted to the research of the functioning of financial and industrial groups on Ukraine's markets for corporate control and investments. The largest financial and industrial groups of Ukraine - "Finance & Credit", "Privat-Invest", "Ukrsibbank" and "The Industrial Union of Donbass" - were studied during the research. The research revealed the most important criteria that financial and industrial groups have to meet for the efficient functioning on the Ukrainian markets for corporate control and investments. These are the following criteria: a powerful bank capable of carrying out the function of cash generator within a group; high degree of business diversification; optimum concentration of property; minimal hierarchy of the system of corporate control. The research has studied such criterion as transparency of the structure of property, which is highly valued by the corporate governance in other countries. In Ukraine, the structure of ownership of most of efficiently functioning financial and industrial groups is not transparent, which is paradoxical. This can be explained by the lack of proper legislation for protection of property rights, low activity of small shareholders and reluctance of financial and industrial groups themselves to make transparent the motives of their participation on the market for corporate control.

**Keywords:** corporate control, corporate ownership, financial-industrial groups

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### **1. Introduction**

At this stage of development of the national economy the dominating part of Ukraine's GDP is manufactured by enterprises which are controlled by financial and industrial groups. One should note that, as a rule, the national financial and industrial groups are neither serious investors nor active users of innovations, nor the engine of reforms. At the same time, financial and industrial groups help coordinate the activities of enterprises they control and reduce their expenses. In any case, the activity of financial and industrial groups is a reflection of the real economic situation in Ukraine.

The history of Ukrainian financial and industrial groups started from the Decree of the President of Ukraine "About financial and industrial groups" of

25 January 1995. According to this decree, financial and industrial groups are "legal persons established through amalgamation of industrial enterprises, organizations, banks and other business players with their property and financial resources pooled for centralized management of manufacturing, research and commercial activity".

This Decree set up a system of organizational and legal procedures for the functioning of financial and industrial groups based on principles of transparency of relations and financial accounting. This decree regulated the activity of financial and industrial groups which to some degree limited the possibilities for the groups. Wishing to have the biggest scope of possibilities, the groups were formed by means of informal relations until the abolishment of the decree in 1999. This fact explains the non-

transparent structure of the property of these groups which were founded in the period of the decree's duration. As examples of such financial and industrial groups we can name "Finance & Credit", "Privat-Invest", "Ukrsibbank". As regards "The Industrial Union of Donbass", it went through the restructuring process in 2000, and today it has a fairly transparent structure of property.

Financial and industrial groups include commercial banks. Unfortunately, scientific literature does not clearly define the role of commercial banks in these structures. Moreover, this literature does not pay attention to the efficiency of corporate control within financial and industrial groups. So, the main task of our research is to define the place and role of commercial banks in the structure of financial and industrial groups, as well as factors ensuring the efficiency of corporate control over the property of financial and industrial groups.

## 2. Methodology of research

The research we are planning to carry out will proceed in several stages.

During the first stage we will investigate the general characteristics of Ukrainian financial and industrial groups: "Finance & Credit", "Privat-Invest", "Ukrsibbank" and "The Industrial Union of Donbass". The result of the research on this stage will be a brief description of financial and industrial

groups from the viewpoint of their motives, strategies and role of banks in their structures.

During the second stage we will conduct the modelling of the groups' profiles according to the motives of the property acquisition by these groups. As a result of this modelling we will get two matrices.

The first matrix will be based on such criteria as the place and role of banks in the structure of financial and industrial groups, as well as the range of diversification of the groups' businesses. Using these criteria we will determine the motives behind the acquisition of property by these groups, which range from investment to speculative motives.

Then we will study the peculiar features of the corporate control of financial and industrial groups, juxtaposing the property that they acquired with their motives. These peculiarities will be based on the following criteria: depth of corporate control, the degree of the property transparency, level of property concentration. The right use of the last criterion will provide the corporate control rating. We will study in detail the methodology of its formation. For this purpose we will use a hypothetical example.

There are two financial and industrial groups. Each of them consists of eight enterprises. The distribution of the share of the shareholders capital for enterprises in such groups is shown in Table 1.

**Table 1.** The distribution of the share of the shareholders capital for enterprises in such groups

	Rating	Ownership concentration	Number of companies controlled by certain FIG		Points for each FIG	
			FIG №1	FIG №2	FIG №1	FIG №2
1	1	2	3	4	5	6
2	8	100%	3	2	24	16
3	7	75,1-100%	1	4	7	28
4	6	60-75,1%				
5	5	50,1-60%	2	1	10	5
6	4	40,1-50,1%				
7	3	25,1-40,1%				
8	2	10-25,1%				
9	1	0,1-10%				
10	Total amount		6	7	41	49
11	Average rating		6,8	7		
12	Total number of companies		8	8		
13	The share of companies selected to the total number of companies controlled by FIG		75%	87%		

The methodology for the formation of the corporate control rating has several phases. During the first phase we will give a certain mark to the size of the block of shares. This method gives eight marks (from 1 mark for the smallest size of a block of shares (0,1-10 per cent), till 8 marks for the biggest

possible block of shares (100 per cent)), which is shown in column 1-2 of the Table 1.

During the second phase we enter (into the columns 3-4) the data about the number of enterprises in groups according to their shares of participation which is shown in column 2 of the Table 1. After that, by summing up, we calculate the number of

enterprises, the information about which is given in columns 3-4 of the Table 1. The results are entered into the squares of the Table, which are located on the intersection of the columns 3-4 and the line 10 of the Table 1. Then we divide the number of enterprises (in which financial and industrial groups participate in the nominal capital) by the general number of the group's enterprises. The results will be entered in the line 13 of the Table 1.

During the third phase we calculate the general mark for every financial and industrial group. In order to do that we multiply the number of enterprises in groups by the mark that corresponds to this particular range (columns 5-6 of the Table 1). Then the results of the multiplication are summed up. By doing so we receive the general marks for the groups, which we put at the intersection of columns 5-6 and the line 10 of the Table 1.

During the fourth phase we find an average mark for the group that we enter into the line 11 of the Table 1. We do it by dividing the general mark for the group by the number of enterprises (in which financial and industrial groups participate in the nominal capital and the share of their participation is known).

The final phase is the making of the corporate control rating based on the mark which is average for

the group. For example, the average mark for the first financial and industrial group is 6,8 and for the second financial and industrial group – 7. This shows the advantages of corporate control in the second case.

This rating will enable us to use such criterion of the efficiency of corporate control as the level of property's concentration. As a result we will be able to use all criteria, to carry out the modelling of the group's profile and to get the second matrix.

The last phase will determine the most efficient financial and industrial group for Ukraine based on the modelling of its characteristics.

### 3. Brief outline of financial and industrial groups in Ukraine

#### 3.1. Financial and industrial group "Finance and credit"

The virtual owners of the group are the residents of Ukraine Konstantin Zhevago and Aleksey Kucherenko. The operational governance is carried out by Sergey Veselov and Igor Frunze. The core of the group is the joint-stock bank "Finances and credit". The interests of the bank represent the priorities in the activity of this financial and industrial group.

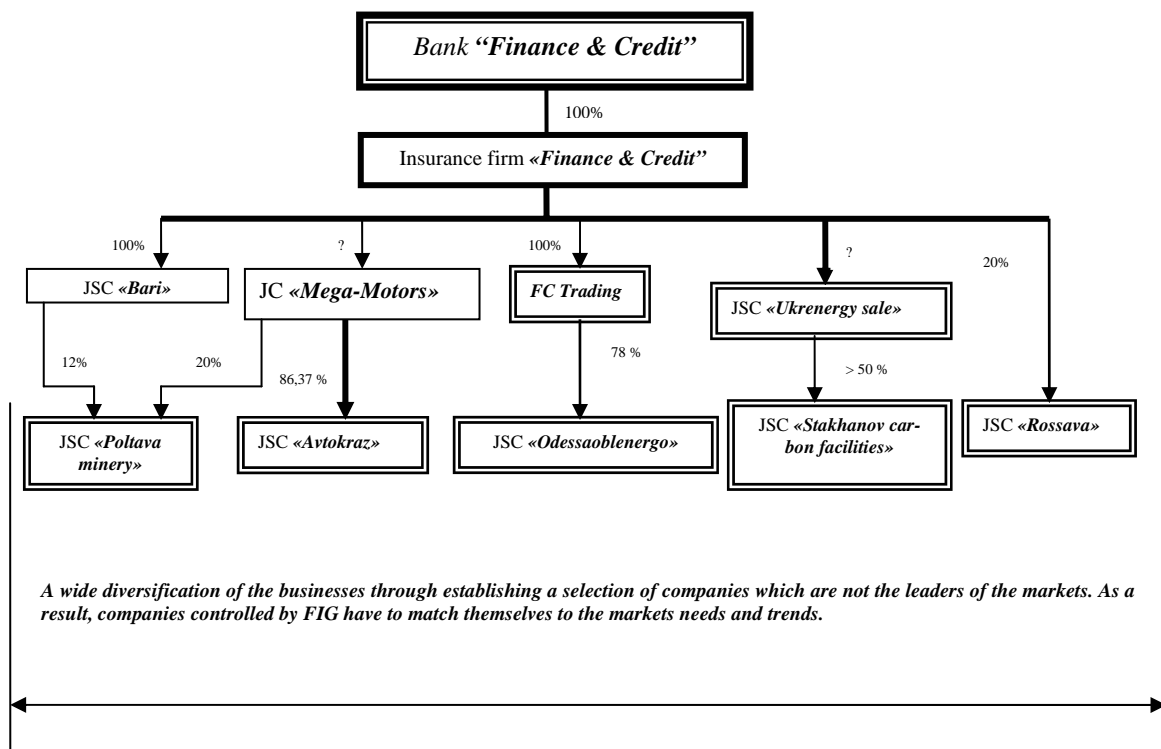


Fig. 1. Financial-industrial group "Finance & Credit"

The motive for the acquisition of property by this group is speculative. The main strategy of the group is diversification. This group consists of enterprises of the following branches: metallurgy, automobile industry and energy distribution. It should be noted that enterprises within the group are not among

the leaders of domestic and foreign markets. That is the reason why they have to adjust to these markets' conditions.

The group tried to achieve the vertical integration in the metallurgical branch as it made the unsuccessful bid to buy 70 per cent worth block of shares

of the open joint-stock company "The Khartsyzsky pipe factory". The ownership of the two enterprises of the automobile branch - the open joint-stock companies "Avtokraz" and "Rossava" - does not allow the group to achieve the effects of the vertical integration, the most important of which is the addition of suppliers' profits. This can be explained by the fact that the tires manufactured by the joint stock company "Rossava" are not an important item of expenses for the open joint-stock company "Avtokraz", unlike metallurgical enterprises in which the expenses for the purchasing of raw materials produced by the mining enterprises make up 38-52 per cent of their expenses. Moreover, in the future one can expect considerable changes in the product policy, which means the renewal of equipment and the uncertainty of the source of tires' acquisition.

The possibility of further privatization of enterprises, which would ensure the vertical integration for the group, is doubtful. The reason for that is the fact that in Ukraine there are some groups, which have a higher potential in the same branches than the financial and industrial group "Finance & credit". Besides, these groups possess considerably bigger financial resources.

The results of our analysis demonstrates that the financial and industrial group "Finance & credit" has widely diversified business areas that logically corresponds to the speculative motives of the group's behavior on the corporate property's market. This confirms the lack of vertical integration within the business areas of the group and the backward position of its enterprises on domestic and foreign markets.

### **3.2. Financial and industrial group "Privat-Invest"**

The core of the group is the joint-stock bank "PrivatBank". Its owners are the residents of Ukraine G. Bogolyubov, I. Kolomoyskiy and A. Martynov. The bank is one of the biggest in Ukraine, but the real foundations of its business are little known to the wide Ukrainian public.

As previously mentioned, the bank is a center of the group's structure, but in contrast to the financial and industrial group "Finance & credit", its interests are not the group's priorities. The bank is used only as a generator of cash.

The group has an investment motive for the acquisition of ownership. The goal of the group is the mastering of different branches of economy. Its interests spread to petrochemical, metallurgical, chemical, agricultural and other branches of economy.

As regards the strategic approach to the formation of the financial and industrial group "Privat-

Invest", its portfolio of corporate property is very diversified. The principle business areas include chemical and petrochemical industry, ferrous metallurgy and agriculture. The group has also diversified its activities in such branches as machine-building, ship-building, trade and communication.

As the remarkable share of the group's profits is generated by enterprises of petrochemical and metallurgical branches, whose earnings are mutually commensurable, we can see the effective measures aimed at reducing the economic risks. This can be explained by the fact that the financial strength of the group is determined by two business areas.

We should also stress that the financial and industrial group "Privat-Invest" is vertically integrated in such branches as petrochemical industry, ferrous metallurgy and agriculture. Let us study in more detail the efficiency of integration in all of these branches.

In petrochemical branch the vertical integration of the group is complete as shown by its enterprises. Such enterprises as open joint-stock companies "Ukrnafta" and "Naftokhimik-Prykarpattya" produce oil and petroleum products, which are sold by the joint-stock companies "Nikolayevnefteprodukt", "Sumynefteprodukt", "Chernikovnefteprodukt" and other companies of the group. The drawback of the vertical integration of the financial and industrial group in this branch is the deficit of production capacity for the secondary refinement of oil (Figure 2).

In the branch of ferrous metallurgy the group has concentrated more than 30 per cent of Ukraine's production capacities for the dressing of iron ore (Southern, Iguletsky, and Suha Balka mining and metallurgical plants). The financial and industrial group "Privat-Invest" has also monopolized the production and dressing of manganese ore in Ukraine (Marganetsky and Ordzhenekinzensky joint-stock companies). The output of these plants is a raw stuff for such enterprises of the group as Nikolayevsky plant of ferroalloys, Zaporozhsky plant of ferroalloys and Petrovsky integrated plant. It is important to say that the production capacities of ore-dressing plants of the group by far exceed the needs of the group's metallurgical plants. As a result, the financial and industrial group "Privat-Invest" works both on the market of the primary processing of metals and the market of metal products.

In the branch of agriculture the financial and industrial group "Privat-Invest" is vertically integrated. Unlike other branches, the integration here is partial (There are no not-sufficiently profitable agricultural enterprises).

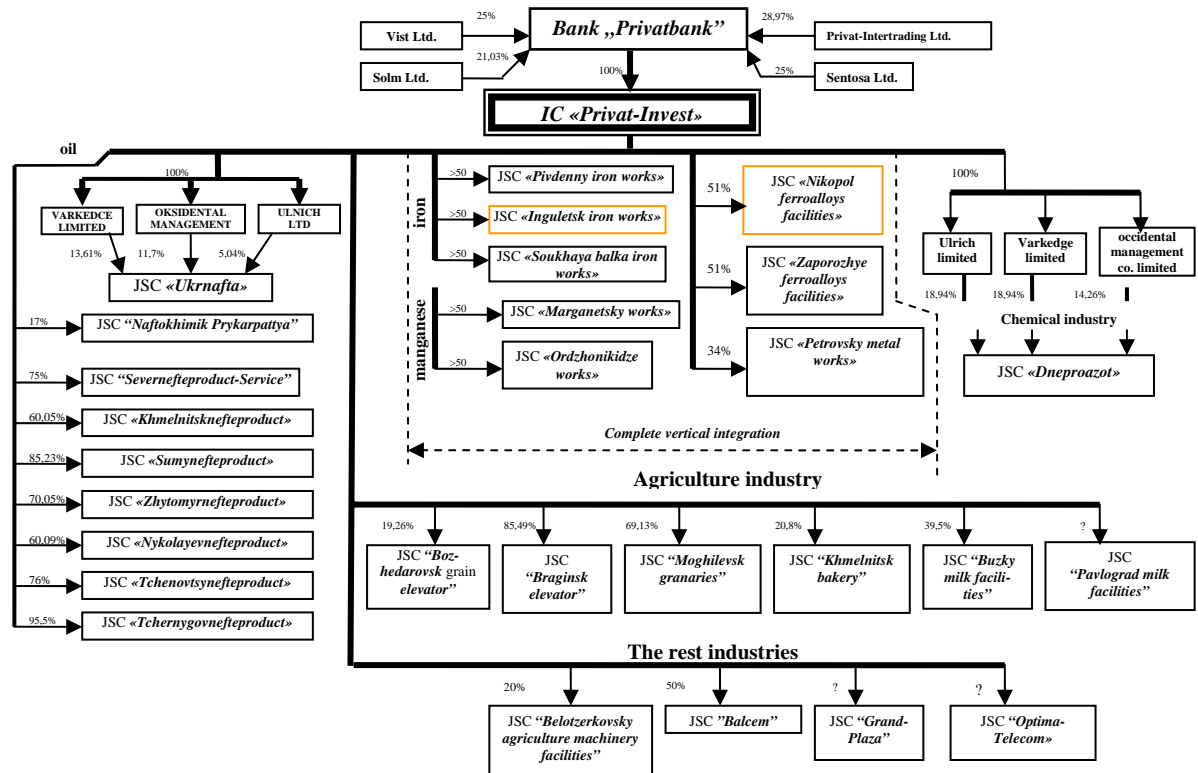


Fig. 2. Financial-industrial group "Privat-Invest"

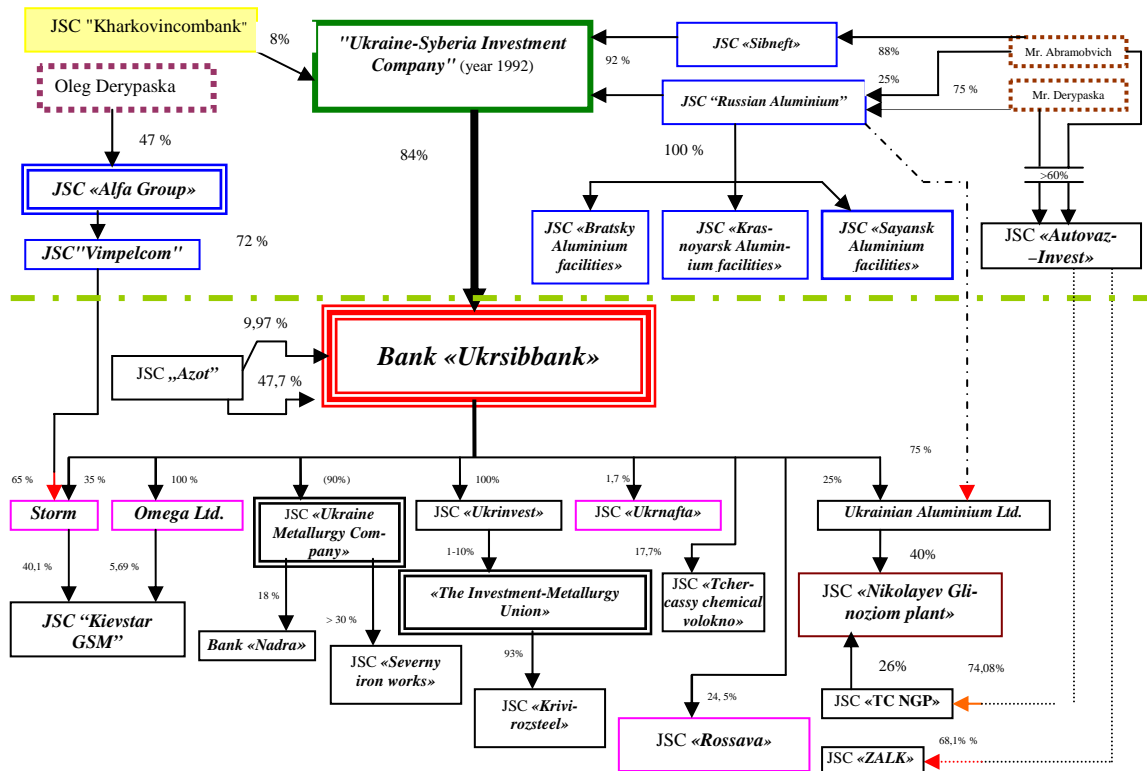
The structure of the chain of the vertical integration is the following. The joint-stock companies "Bozhedarovsk grain elevator" and "Braginsk elevator" store grain and prepare it for further processing. The grain is processed by the joint-stock companies "Moghilevsk granaries" and "Khmelnitsk bakery". These production capacities are very nicely balanced. According to this, the vertical integration of the financial and industrial group "Privat-Invest" is the most efficient in the agricultural branch.

Our analysis shows that the financial and industrial group "Privat-Invest" is engaged in a large-scale and diversified business. Its major branches are petrochemical industry and ferrous metallurgy.

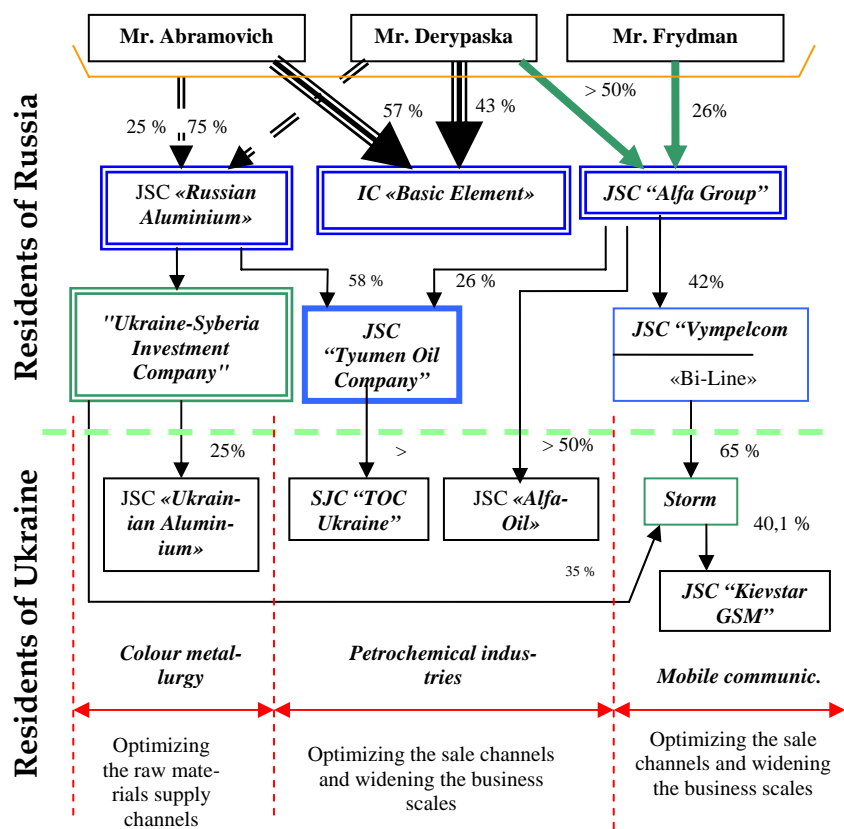
### 3.4. Financial and industrial group "UkrSibbank"

The virtual owners of the group are the residents of the Russian Federation Oleg Derypaska and Roman Abramovich (92 per cent of the registered capital) and the resident of Ukraine, the deputy of Ukraine's parliament Alexander Yaroslavsky (8 per cent of the registered capital). Regarding the place of the bank in the structure of the financial and industrial group, it is an intermediary in the group's financial and investment operations. The bank "UkrSibBank" represents the interests of the Russian residents in Ukraine.

The group has an investment motive for the acquisition of property. The group's objective is to strengthen the positions of the Russian investors in the branches of nonferrous metallurgy, petrochemical industry and cellular communication in Ukraine. A wide range of business areas of "UkrSibbank" demonstrate the level of its diversification. The group includes enterprises of ferrous and nonferrous metallurgy, petrochemical industry, communication, car manufacturing and other branches of the national economy. Speaking of the degree of diversification of "UkrSibBank", we should note that nearly half of the group's revenue is produced by enterprises of nonferrous metallurgy. Another half of the group's profits is brought by other businesses. Figure 4 shows that the financial power of the group depends on one particular business area, which is nonferrous metallurgy. This demonstrates that the business risk is not evenly spread among the business areas of the group. It is also important to remember that the financial and industrial group "UkrSibBank" is not independent. Its objective is the strengthening of positions of the Russian investors in various branches of Ukrainian economy, with the best results achieved in the branch of nonferrous metallurgy. That is why the insufficient degree of the group's diversification needed for the reduction of economic risks is not the group's drawback. The strategy of the group's formation is determined on a higher level (business structures that "UkrSibBank" is a part of).



**Fig. 3.** Ukrsibbank



**Fig. 4.** Business interests of the residents of the Russian Federation in FIG UkrSibbabbk



It is also important to remember that the group is fully vertically integrated in the branches of nonferrous metallurgy and petrochemical industry. 90 per cent of the primary aluminium manufactured by the belonging to the group “Nikolayevsky’s aluminium plant” is exported because of the lack of processing capacities in the domestic branch of nonferrous metallurgy monopolized by “UkrsibBank”.

The results of our analysis demonstrate that the financial and industrial group “UkrsibBank” was set up in order to enable the Russian investors to master the Ukrainian market.

This explains the dependence of the group and the intermediary role of “UkrsibBank” for the consolidation of positions in Ukraine’s economy. The group achieved the biggest success in the branch of nonferrous metallurgy and monopolized the domestic production capacities. That was a goal of the group.

### 3.4. Financial and industrial group “The Industrial Union of Donbass”

The biggest and the most influential financial and industrial group is the “The Industrial Union of Donbass”. It was founded in Donyetsk in December 1995. Its cofounders are the regional branch of the Academy of technologies of Ukraine, Donetsk city chamber of commerce, open joint-stock company “Azovintekx” (the town of Mariupol), closed joint-stock company “Vizavi” (Fig. 5). The last one became the most prominent in the group. The founders of “Vizavi” are Vitaliy Gayduk and Sergey Levochkin. It is believed that the shares of the company are distributed in the following way: with 51 per cent belonging to Gayduk and 49 per cent belonging to Levochkin. The directors of the “The Industrial Union of Donbass” are Sergey Taruta and Oleg Mkrtychan.

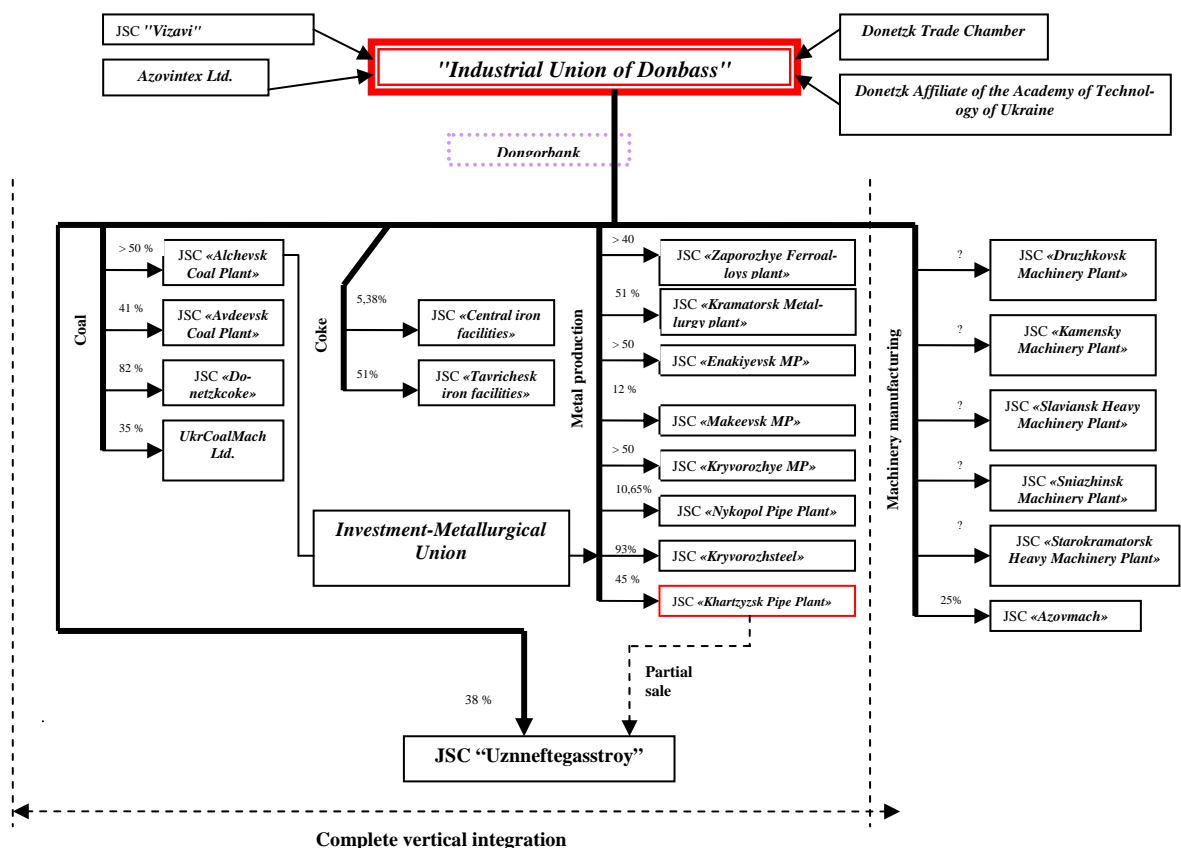


Fig. 5. Financial-industrial group “Industrial union of Donbass”

It is worth mentioning that the group does not include any banks. According to this the “The Industrial union of Donbass” is not a classical case of financial and industrial group. The dominant share of the group’s transactions is carried out through the commercial bank “Dongorbank”, which is connected to the group and which performs the function of the settling organization.

The share of resources generated by the Ukrainian banks serving the group as creditors is rather low in the structure of the group’s financial resources. The reason for that is that the potential of Ukrainian banks does not allow to carry out a full-scale crediting of the big business of the group (Small credits given by the domestic banks and the high interest rate can not satisfy the group’s demand for liquidity).

The main sources of finance for the group's activities are prepayments for the future delivery of products and the group's own revenues. On the one hand, the independence of the "The Industrial Union of Donbass" from the banking institutions is an advantage, but, on the other hand, for such a big group it is very difficult to work for a long time using only its own resources.

The group has a specialized investment interest in the acquisition of property.

The objective of the group is the strengthening of its positions in the branch of nonferrous metallurgy.

The strategy of the group's formation is vertical integration. The group has managed to unite enterprises with a closed technological chain (coal – coke – metal) which represents a vertical integration in the branch of nonferrous metallurgy.

More complex is the definition of the role of machine-building enterprises in the strategy of the group's formation, as it is impossible to define the tools used by the group for gaining control over these enterprises.

If the group has control over the machine-building enterprises through participation in the authorized capital, then the following ways are possible:

- the group carries out interindustrial vertical integration by closing the chain (coal – coke – metal – metal-consuming products);
- the group carries out minor diversification in the branch of machine-building.

Only the motivation of persons making decisions about the purchasing of shares of machine-building enterprises can prove which of the strategic alternatives the group pursued.

Practically all profits of the "The Industrial Union of Donbass" are brought by the coke and chemical plants, metallurgical and tube-producing plants. This means that the dominating business is ferrous metallurgy.

If the group controls the machine-building plants by using instruments different from property rights, then in this case these enterprises do not play an important role in the formation of the group. They are only a segment of the market for the sales of metallurgical products controlled by the group.

The results of our analysis show that the "The Industrial Union of Donbass" is not a classical financial and industrial group because of the absence of a bank in the group's structure.

The commercial bank "Dongorbank" plays a role of a settling organization for the group. The dominant business area is ferrous metallurgy, in which the group has a full vertical integration. The integration of the "Industrial union of Donbass" in this branch is ideal because of the well-balanced production capacities of the coke, chemical and metallurgical plants.

The activity of "Uzneftegasstroy" – an enterprise within the structure of the group – is not the

group's business area. Its shares were bought in order to ensure successful sales of the tubes produced by the open joint-stock company "Khartyzsk Pipe Plant" on the market of Uzbekistan.

#### **4. Motives for the acquisition of property by financial and industrial groups in Ukraine**

##### **4.1. Motives for the acquisition of property by financial and industrial groups**

###### **4.1.1. Speculative motive of the financial and industrial group "Finance & Credit"**

Speculative motive of financial and industrial group "Finance & Credit" is a result of evolutionary development. The initial motive was an investment one, which is proved by the fact that earlier the group took part in privatization tenders, which could have ensured its vertical integration in some branches. But these attempts were not successful. On this stage the chances of "Finance & Credit" victory in these privatization tenders have been significantly reduced.

This is explained by the fact that, besides "Finance & Credit", there are some groups in Ukraine which have a higher potential in the same branches of economy and have bigger financial resources. These particular features ensure their competitive advantages in privatization tenders. Further development of the group by means of organic growth within the existing enterprises is not possible, because the organic growth within the existing enterprises is possible only on the stages of the market's formation and development, whereas the group's enterprises carry out their operations on the markets which are already mature. Poor prospects for the development of the "Finance & Credit" group and its enterprises contradict the investment motive of the property's acquisition.

As a result of such circumstances the investment motive of the group has been transformed into speculative motive consisting in the acquisition of property, which, later on, is to be sold at a higher price.

The conclusion that on this stage the "Finance & Credit" is driven by this motive was made on the basis of the following facts: business areas of the group are diversified, vertical integration has not been achieved in any of these business areas, enterprises within the group's structure are not among the markets' leaders. As mentioned earlier, these peculiarities of the group are logically correlated with the speculative motive of the property's acquisition.

In our view, the following alternatives of "Finance & Credit" development are possible:

- The merger with a bigger group, which will be able to increase its market share and production capacities using the assets of "Finances and credit".
- Selling by "Finance & Credit" of all of its other enterprises with the exception of the



open joint-stock company "Finance & Credit".

In case of the merger with a bigger group, the range of corporate rights of the owners of "Finance & Credit" would be considerably narrowed. Because of that we believe that more preferable is the second option as the money received from the sale of assets can be used for the development of the open joint-stock company "Finance & Credit", which operates on the promising Ukrainian market of banking services.

#### **4.1.2. Diversified investment motive of the financial and industrial group "Privat-Invest"**

This motive means that the group invests in enterprises of different branches with the goal of their development. By doing this the financial and industrial group forms such group of enterprises, which can ensure the increase of its market share, production capacities and attainment of vertical integration. In case of successful realization of this motive's activities, diversified financial and industrial groups are formed. These groups have several business areas, they are vertically integrated and have strong positions. Such financial and industrial groups manage to reduce their economic risks (as a result of diversification) and to achieve cost saving (by adding the profits of suppliers through vertical integration), which ensure the viability of these groups.

The financial and industrial group "Privat-invest" diversifies its activities in various branches of the national economy. The main business areas are ferrous metallurgy and petrochemical industry, where the group has managed to achieve vertical integration, increase its production capacities and markets' share. In this way the risk of the group's activity is spread among several business areas, in which the group has strong positions. This proves the diversified investment motive of the group in the acquisition of property.

#### **4.1.3. Investment motive of the financial and industrial group "UkrsibBank"**

Before studying the motive of the property's concentration by this group it is necessary to pay attention to the group's goals. As mentioned earlier, these goals include the strengthening of positions of Russian investors in some branches of Ukraine's economy. That is why the group is not independent. According to this, the vertical integration and the degree of diversification in this case can not be the criteria for determining the motives of the acquisition of property by the financial and industrial group, because its strategy is formed at a higher level (business structure that includes the "UkrSibbank" group as one of its elements).

In our opinion, the group has the investment motive for the acquisition of property, because the

group tries to maximize its potential in certain business areas. For example, the financial and industrial group "UkrSibbank" has monopolized the production of aluminium in Ukraine and gained a considerable share of the domestic market of cellular communication (GSM). Such an enterprise of the group as the joint-stock company "Azot" is a leader of the domestic market of mineral fertilizers. The attainment of such good results in the increase of production capacities and the conquering of the markets make it possible to conclude about the clear-cut investment motive of property's acquisition.

At the moment the portfolio of "UkrSibbank's" enterprises is quite promising. That means that the group can also develop autonomously, and, considering the support that the Russian investors can render, the viability and the prospects of the group are doubtlessly high.

#### **4.1.4. Specialized investment motive of the financial and industrial group "The Industrial Union of Donbass"**

This motive means that the group buys property in order to increase the production capacities, expand its market share and achieve the vertical integration in certain branches of economy.

Such groups have a substantial number of enterprises belonging to the same branch. Various technological cycles that make a closed production process are carried out within these enterprises. During the formation of the group one tries to achieve such a combination of enterprises that would not allow any disbalance of production capacities within the production process of the branch.

Groups that were formed in this way conduct a large-scale activity, have an opportunity to save costs (adding the profits of suppliers as a result of vertical integration). Very often these groups achieve a monopolistic position on the market. The drawback of such financial and industrial groups is that they are highly risk-prone as a result of the lack of diversification.

We have already mentioned the high potential of the "The Industrial Union of Donbass" in the branch of ferrous metallurgy, where it has an efficient vertical integration. This branch is a major business area of the group that made it possible for the group to increase its production capacities and occupy a substantial market share. These facts demonstrate the high specialized investment motive of the group in the concentration of its property.

It becomes obvious that Ukrainian financial and industrial groups have totally different motives in the acquisition of property, which is proved by their wide range from investment to speculative motives. Each of these motives can influence the strategic approach to the group's formation, its potential and prospects, which is shown in Fig. 6.

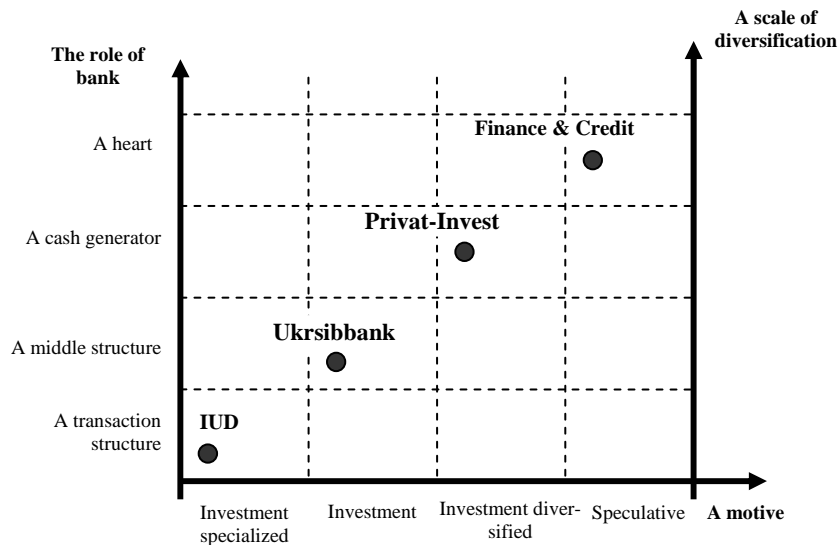


Рис. 6. The profiles of FIGs

In our opinion, in accordance with this profile, the most promising financial and industrial group is “Privat-Invest”. This opinion is based on the fact that by means of diversification this group has spread its economic risk among several business areas. Moreover, in some business areas the group has integrated vertically and achieved some leading positions, which enabled it not only to adjust itself to the market’s conditions, but also to influence it in a certain way. The liquidity generated by financial and industrial group “Privat-Invest” made it possible to mobilize significant resources. That is the group’s advantage for the participation in privatization tenders. We can see that the role of “Privat-Invest” as the group’s cash generator does not consist in assisting the enterprises within this group, which are quite liquid themselves.

#### 4.2. Peculiarities, which determine the efficiency of corporate control of the property acquired by the groups and their motives

As mentioned earlier, the main criteria, which determine the efficiency of corporate control within the group, are the system hierarchy, degree of property’s concentration and degree of property’s transparency. Within these criteria we will analyze the efficiency of corporate control for each financial and industrial group.

##### 4.2.1. Peculiarities, which determine the efficiency of corporate control within the financial and industrial group “Finance & Credit”

The degree of property’s concentration by the group is high. The average size of a block shares is 53,3 per

cent. The group’s participation in the authorized capital of some enterprises differs considerably. For example, having consolidated with the German partners, “Finance & Credit” can vote with the number of shares equal 86,37 per cent at the meeting of shareholders of the joint-stock company “Avtokraz”. That makes it possible to make any decisions regarding the joint-stock company. Such rights, but without consolidation with others, the group enjoys with 78 per cent worth block of shares of the joint-stock company “Odessaoblenergo”. Having consolidated with foreign partners, the group controls 32 per cent of shares of the joint-stock company “Poltava Iron Facilities”, which enables the group to nominate its candidates to the company’s managerial bodies, initiate extraordinary meetings of shareholders and block any decisions concerning reorganization, liquidation and changes of the company’s charter. 20 per cent worth block of shares of the joint-stock company “Rossava” allows the group only to nominate its candidates to the managerial bodies and initiate extraordinary meetings of shareholders. Having the control over the joint-stock company “Ukrenergobyt”, which in its turn has the controlling block of shares of the joint-stock company “Stahanovsky plant of technical carbon”, makes it possible for the group to make any decisions concerning the company with an exception of its liquidation and changes in the charter.

The property of the group is not transparent. It is impossible to trace its structure on the basis of official data. The reason for that is the fact that most of its assets the group owns through joint enterprises, off-shore companies and other intermediaries. The non-transparent structure of ownership prevents the group from using its full potential, which is a drawback if the group wants to participate in privatisation tenders, receive credits and attract investors.

The system of corporate control of the financial and industrial group "Finance & Credit" consists of two levels. The first level is the financial and investment company "Finance & Credit", which completely belongs to the commercial bank "Finances and credit". We suppose that the creation of this level of corporate control is explained by the desire of owners to make within the group's structure some centres responsible for financial and investment activity (commercial bank "Finance & Credit" and investment company "Finance & Credit"). 80 per cent of enterprises within the group have the second level of corporate management and control that covers off-shore companies, joint ventures and other enterprises. The multi-level system of corporate control reduces their efficiency, but in some cases it is necessary. For example, foreign partners, with whom joint enterprises are founded, can have considerable financial resources, experience and potential for working in particular branches. We believe that this explains the existence of joint ventures ("Bari" and "Mega-Motors") on the second level of corporate management and control over such enterprises of the group as joint-stock companies "Poltavsky Iron Facilities" and "Avtokraz". The necessity of off-shore companies FC "Trading" on the second level of corporate control of the joint-stock company "Odes-saoblenergo" is doubtful.

The level of concentration of the property of the group "Finance & Credit" (consolidated with foreign partners) is high. This reflects the specific character of Ukraine's corporate control market. In comparison with foreign experience of speculative transactions, in which the buying of blocks of shares of enterprises worth 5 per cent results in considerable changes in the structure of property, the Ukrainian market of corporate control is less susceptible to changes in equity participation. Such situation can be explained by nonsufficient development of the stock market and main instruments of corporate control. The structure of the group's property is not transparent, which is a drawback for participation in privatization tenders and attraction of investments. The multi-level system of corporate control reduces its efficiency, but in case of some enterprises it is a necessity.

#### **4.2.2. Peculiarities, which determine the efficiency of corporate control of the financial and industrial group "Privat-Invest"**

The level of concentration of the group's property is average. The group has controlling block of shares in more than 65 per cent of its enterprises. In more than 30 per cent of enterprises the financial and industrial group "PrivatBank" owns blocks of shares, which give it the quorum at shareholders' meetings. Such level of the property's concentration gives the group a wide range of rights at the meetings of shareholders.

The property of this group, as well as the "Finance & Credit" group is not transparent. Off-shore companies own the major part of enterprises. It is very difficult to determine their connection with the group on the basis of official data. The non-transparent structure of ownership limits the possibilities of the group, which is a drawback for the group's participation in privatization tenders.

The system of corporate control of the financial and industrial group "PrivatBank" is very efficient as shown by the purposeful and efficient realization of the strategy. We can surmise that all blocks of shares of the group are managed by one organ in spite of the fact that enterprises are owned by off-shore companies. In our opinion, the management of enterprises, which are under control of the group, is carried out by the commercial bank "Privat-Invest", which is a property of the commercial bank "PrivatBank". That is why the multi-level system of corporate management and control is non-existent.

We can make a conclusion that, in spite of the intricate and non-transparent structure of the property owned by the financial and industrial group "PrivatBank", the management of the group is efficient enough. This is explained by the high degree of the property's concentration and the efficient system of corporate control mechanisms, where the major place belongs to the transfer of assets' management to the single organ within the group "Privat-Invest".

#### **4.2.3. Peculiarities, which determine the efficiency of corporate control within the financial and industrial group "UkrSibbank"**

The level of the property's concentration of "UkrSibbank" is not high. The average size of blocks of shares is about 37 per cent. According to the national legislation, this size of equity participation allows to nominate candidates to the managerial bodies of joint-stock companies, initiate extraordinary meetings of shareholders, block decisions concerning reorganization, liquidation and changes in the company's charter. If the group consolidates with its Russian owners it can receive a wide spectrum of rights at the meetings of shareholders of ferrous metallurgy enterprises. For example, the commercial bank "UkrSibbank" together with the joint-stock company "Russian aluminium" owns 100 per cent of shares of the open joint-stock company "Ukrainian aluminium", which makes it possible to make any decisions regarding the company's activity. In its turn, the open joint-stock company "Ukrainian aluminium" owns 40 per cent of shares of the open joint-stock company "Nikolayevsky aluminium plant". Further 26 per cent of this plant's shares belong to the joint-stock company "Avtozaz-Invest", which belongs to the Russian owners of "UkrSibbank". Consequently, the owners of the financial and industrial group "UkrSibbank" can concentrate 66 per cent of shares of the open joint-stock company

“Nikolayevsky aluminium plant”. This makes it possible to make any decisions concerning this enterprise with an exception of reorganization, liquidation and changes in the company’s charter.

Compared with the structure of property of the groups “Finances and credit” and “PrivatBank”, the structure of property of “UkrSibbank” is more transparent. This enabled us to determine that the commercial bank “UkrSibbank” performs the function of an intermediary in the activity of the group. To some extent, the relatively transparent structure of property reveals the potential of the group, which is an advantage during the participation in privatisation tenders.

The system of corporate control is rather complex and has two levels. The first level is the “Ukrainian-Siberian investment corporation”. Its Ukrainian owners were the founders of the commercial bank “UkrSibbank”. The commercial bank “UkrSibbank” is the second level. It carries out the management of the blocks of shares that belong to the group. The multi-level system of corporate management and control reduces its efficiency, but considering the dependency of the group, the two-level system of corporate control is the most acceptable option.

By analysing the efficiency of corporate control within the financial and industrial group “UkrSibbank” we have found out that the multi-level system of corporate control is an objective necessity and reflects the specific character of this group. The transparent structure of property shows the group’s potential, and therefore it is an advantage during participation in privatisation tenders.

#### **4.4.4. Peculiarities, which determine the efficiency of corporate management and control within the financial and industrial group “The Industrial Union of Donbass”**

The level of concentration of property by the group is not high. The average block of shares of the group is 36 per cent. It is necessary to point out that the group’s participation in the authorized capital of certain enterprises differs significantly. For example, the group has controlling blocks of shares in more than 26 per cent of enterprises, which makes it possible to make any decisions concerning the activities of an enterprise with an exception of reorganization, liquidation and changes in the company’s charter. In 6 per cent of enterprises the group has blocks of shares allowing it to make any decision concerning these enterprises. In 20 per cent of enterprises the group owns blocks of shares allowing it to block any decisions made at the meetings of shareholders. In 27 per cent of enterprises the group owns up to 12 per cent of shares, which enables it to nominate candidates to the managerial bodies of these enterprises and initiate the extraordinary meetings of shareholders. In 21 per cent of enterprises the group owns 25-35 per cent of shares, which allows the group to nominate its candidates to the managerial

nominate its candidates to the managerial bodies of these enterprises, initiate the extraordinary meetings of shareholders and block decisions concerning reorganization, liquidation and changes in the company’s charter.

Most sources indicate that at the meetings of shareholders the “The Industrial Union of Donbass” consolidates with other owners, which helps broaden the scope of its rights.

Unlike groups like “Finance & Credit”, “PrivatBank” and “UkrSibbank”, the property of the “the Industrial Union of Donbass” is transparent, as one can verify the information about it in the official sources. The transparent structure of the property shows the group’s potential, which is an advantage during the participation in privatisation tenders, receiving of credits and attraction of investments.

The system of corporate control does not have the hierarchy with the exception of the joint-stock company “Kryvorozhstal”. The lack of hierarchy is partially explained by the transparency of the property’s structure and ensures a sound control over the enterprises within the group’s structure.

The degree of the property’s concentration is not high. The efficient management of the “The Industrial Union of Donbass” ensures consolidation with other owners of enterprises within the group, transparent structure of property and lack of hierarchy in the corporate control system.

We will try to model the profile of the financial and industrial group, which characterizes the efficiency of corporate control within the property acquired by the group in accordance with the motive. As mentioned earlier, the main criteria determining the efficiency of the group’s corporate control is its depth, degree of transparency, degree of property’s concentration and depth of corporate control. The table of the rating of corporate control in accordance with the level of property’s concentration will provide us with the right use of the last criterion.

Having the rating of corporate control, we can use all the criteria, which determine its efficiency within the property acquired by the group and in accordance with the motive. Using these criteria we build a new matrix (Fig. 7).

In our opinion, this matrix does not allow us to make a positive conclusion about the efficiency of corporate control within the property acquired by the financial and industrial group. The reason for that is the fact that in accordance with this matrix, the groups that we analyze have advantages and disadvantages depending on the criterion we use. So, this matrix shows only the peculiarities of the groups.

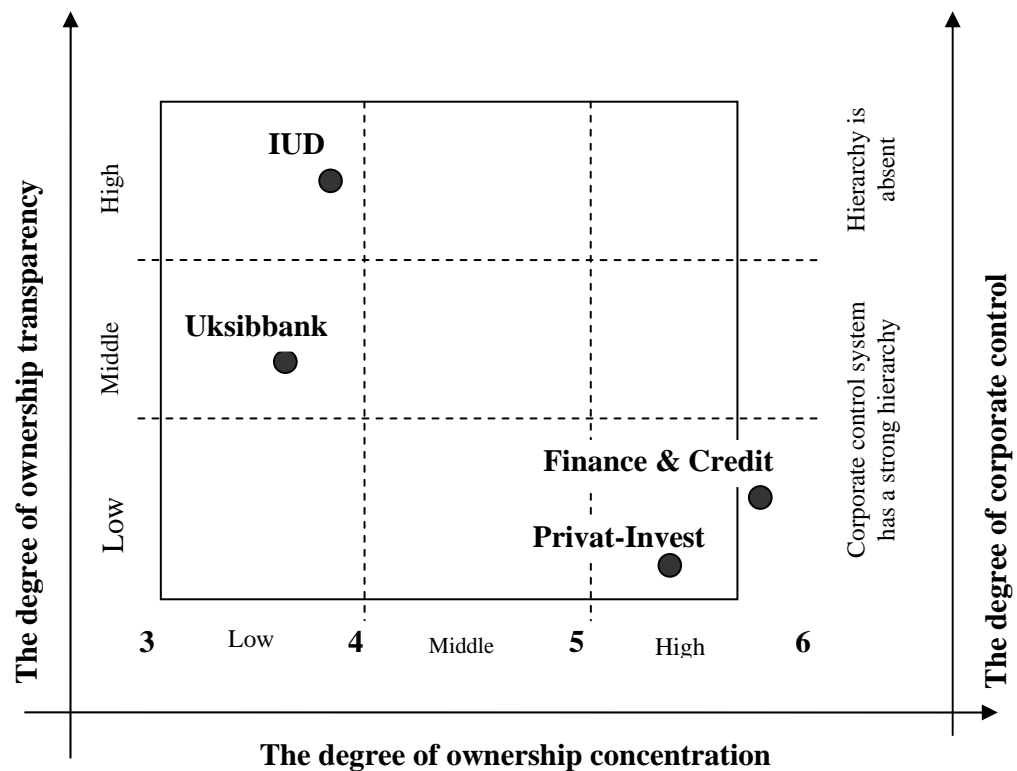
The only possibility to determine the financial and industrial group with the best control of the acquired property is to find out, by which means the group carries out the efficient control. For example, the financial and industrial groups like “Finance & Credit” and “Privat-Invest” have the highest degree of property’s concentration. It is worth mentioning that “Privat-Invest” manages big blocks of shares

independently. It differs from the financial and industrial group “Finances and credit”, which has a high level of property’s concentration due to the consolidation with foreign partners. Among the groups

that we have analyzed “Privat-Invest” has the biggest corporate rights due to the degree of the property’s concentration.

**Table 2.** The rating of corporate control

Rating	Ownership concentration degree	Number of companies controlled by FIGs				Points for each FIG			
		Finance & Credit	Privat-Invest	Ukrsibbank	IUD	Finance & Credit	Privat-Invest	Ukrsibbank	IUD
8	100%	2	6	2	0	16	48	16	0
7	75,1-100%	2	4	1	1	14	28	7	7
6	60-75,1%	0	5	0	0	0	30	0	0
5	50,1-60%	1	8	0	5	5	40	0	25
4	40,1-50,1%	0	1	2	3	0	4	8	12
3	25,1-40,1%	1	3	3	2	3	9	9	6
2	10-25,1%	1	4	4	3	2	8	8	6
1	0,1-10%	0	0	2	1	0	0	2	1
Total amount		7	31	14	15	40	167	50	57
Average mean		<b>5,71</b>	<b>5,39</b>	<b>3,57</b>	<b>3,80</b>				
Total number of companies, controlled by FIGs		11	35	15	21				
The share of companies selected to the total number of companies controlled by FIG		63,64	88,57	93,33	71,43				



**Fig. 7.** The profiles of FIGs



The next criterion is the degree of the property's transparency and the depth of corporate control. The matrix shows that the "The Industrial Union of Donbass" has the highest indicators according to these criteria (Fig. 6). At the same time, we believe that the management of shares in the group "Privat-Invest" is carried out by a single organ. This makes it possible to liquidate the hierarchy of the corporate control system in spite of the complex and nontransparent structure of property.

As we see, the financial and industrial group "Privat-Invest" has the highest concentration of property. The management of the group is carried out very efficiently which leads us to the conclusion that this group could considerably minimize such drawbacks as nontransparent structure of property and hierarchy of the corporate control system. That is the reason why, in our opinion, the financial and industrial group "Privat-Invest" has the most efficient control of the acquired property.

## Conclusions

As a result of our research we have discovered that the role of banks in the functioning of various financial and industrial groups is different. Frequently, the whole group works in the interests of some particular bank. But, there are also cases when a group uses a bank as a generator of cash, as intermediary or when a bank plays an auxiliary role.

The strategic approaches to the groups' activities are also different. Some groups integrate vertically, other groups diversify their activity.

The efficiency of corporate control within groups is determined by such criteria as the degree of property's concentration and the depth of corporate control. Financial and industrial groups differ much in accordance with these criteria.

The role of banks, strategic approach to the formation of financial and industrial groups, the efficiency of corporate control of the property acquired by the groups depend on the motive of the property's acquisition, as well as such factors as the group's size, the branch and the group's relationship with its environment. This is shown by the results of our research of the biggest financial and industrial groups in Ukraine "Finance & Credit", "Privat-Invest", "UkrSibbank", "The Industrial Union of Donbass".

From the viewpoint of the motive of property's acquisition and the efficiency of its management, the best model of the financial and industrial group is "Privat-Invest" with the commercial bank "Privat-Bank" at its core. The conclusion about the advantages of "Privat-Invest" in comparison with other groups in our research is based on the following facts. The function of cash generator carried out by the commercial bank "PrivatBank" allows the group in short periods of time to mobilize considerable sums of money needed for the acquisition of property, which is impossible for the financial and industrial groups without powerful banks in their structure. It is also important that "Privat-Invest" diversifies its activity. This makes it possible to reduce the economic risks. Moreover, in some business areas the group is vertically integrated and has the leading positions, which enables it not only to adjust to the markets' condition, but also to influence it. The efficiency of corporate control of the property acquired by "Privat-Invest" is explained by the high degree of its concentration, as well as by the liquidation of the excessive hierarchy of the corporate control system.

The most important criteria that financial and industrial groups have to meet for the efficient functioning on the Ukrainian markets are:

- ✓ a powerful bank capable of carrying out the function of cash generator within a group;
- ✓ high degree of business diversification;
- ✓ optimum vertical integration within the chosen business areas;
- ✓ high degree of property's concentration;
- ✓ minimized hierarchy of the system of corporate control.

During the research we studied one more criterion – the degree of property's transparency. The foreign experience highly values the degree of property's transparency, but Ukrainian practice of corporate management still follows another principle – a principle of information nontransparency within the structure. Under the present conditions of Ukraine's corporate control market the efficient work of groups is possible even when this principle is ignored. This is explained by the lack of appropriate legislation protecting the property rights, low activity of small shareholders and unwillingness of the groups themselves to make transparent their motives of participation on the corporate control market.