Convergence & Differentiation

What is success in a connected world?*

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PwC: Russian respondents tend to be very optimistic in their answers: 87% said that they believe firmly in the growth prospects for their companies in the short and long term. The results for European and American companies are somewhat different. Only half as many say this. As the manager of one of the largest companies in Russia are you optimistic about the future of the company, and the economy as a whole?

A.I.K. Well if we're talking about Russia Post, then yes, but on the whole I wouldn't risk making an optimistic forecast. It seems to me that it would be difficult to give any guarantees that growth rates will remain as high as they've been at 8%.

PwC: In other words you think that the growth factors that are currently in effect for us are temporary. Is this related to natural resources, to domestic politics?

A.I.K. No, not at all, it's simply the overall situation shows that it is probable that some kind of slowdown should begin, and that includes Russia.

PwC: And what about your company?

A.I.K. Well I still don't know it all that well, but if you look at the chronology of the last few years, then I have no doubt that the volume indicators will grow. How much the financial indicators grow depends not only on us, since the tariffs are set by the government. We have already encountered the paradox of growing volume while financial investments deteriorate.

PwC: Your company is state-owned, and is virtually a monopoly?

A.I.K. It depends on how you look at it. If we're talking about universal services, then yes, but in fact there are already plenty of independent private operators in the postal market, who compete wholeheartedly with us for cash transfers and for delivery and sending packages. There are only a few certain types of mail that are regulated by law. However, it is these types of mail that bring in the greatest losses. I don't think any of the private operators are greatly offended by this.

PwC: So what do you see as your competitive advantages?

A.I.K. Our competitive advantages include our gigantic branch network, more than 42,000 outlets. That's one. And, accordingly, our geographic reach. That's why, given the right investments, and the proper organisation of the technological processes, the post has every reason to be a revenue-generating, profitable enterprise – as it is in many other countries.

PwC: That is to say, the infrastructure is in fact your competitive advantage?

A.I.K. Well, it is, of course, mainly an infrastructure organisation. In order for the network to work, you have to have all the branches of this infrastructure working appropriately. I can't say it's working optimally right now, for various reasons; if, however, there's investment plus optimisation of technologies, then the future looks quite bright.

PwC: Are we talking here only about government investment or possibly also private investments?

A.I.K. No, really, with this form of ownership other kinds are hardly possible; because, really, how can an investor invest in a state enterprise? In the future if there's talk about turning it into a public company, then I think that the interest will be greater, and it would be possible to raise some private investment.

PwC: But this future is still a long way off and you're not discussing it for now?

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A.I.K. Five to seven years, no sooner. For the time being the main task is to ensure that the four main components coexist organically within the postal system: the mail business, the financial business, the logistics business, and the information business. If, in the future, there will be four more or less autonomous divisions within the overall structure, then this will bring only benefits. Of course, this is the matter of a long-term perspective. Today we have a wholistic enterprise and the main task is to avoid losses at least. This the task for this year.

PwC: You have partners abroad, as I understand it?

A.I.K. Russian Post is a member of the Universal Postal Union. And our international co-operation is not limited to this membership. There's also the Regional Communications Union, which includes the other CIS countries, the Baltic States; there are bilateral relations: for example, starting last year this means money transfers can now be done through the post from China and from France to Russia. We're in the final development stages of a project to increase our presence in Germany. There's a great deal going on. Even I am surprised at the breadth of geography and the intensity of all these kinds of measures, the meetings in this area.

PwC: In terms of postal services, it's possible to make a claim for regional competition. What kind of niches could be taken from the point of view of services on the international regional level?

A.I.K. On the regional level, the post is a national operator, and each country has its own. It's only in the European Union countries that changes have been made in the laws, in accordance with which postal services need to go beyond their national borders; by the way, we will also be able to use this. So… well, I'll be careful here, and say that, in general, I see such cross-border opportunities in the market for money transfers, especially in the former Soviet Union, where the volume of transfers is high. Here there's probably an opportunity to strengthen our niche presence.

PwC: Speaking of strategy, and again of competitive advantages, the latest survey shows that the opinion of Russian respondents has shifted a little bit. Whereas previously they used to say that the main advantage for Russian companies was the exclusive access to natural resources, now they talk about the availability of leading technologies. What's your opinion, what really has priority?

A.I.K. It's hard for me to judge about natural resources, other than human resources, if you can call them that. We are experiencing the constant turnover of the personnel, people come and leave And for this reason one of the greatest resource problems is the deficite of the human resources, which will only get worse in the coming years. This is one of the objective factors that can slow down the growth.

PwC: At the same time purchasing power is growing.

A.I.K. I don't think that in the next few years the significance of conversion, the transition to the significance of new technologies will be the determining factor. There's a huge amount of inertia, and the Russian economy's dependence on natural resources is very great. It's even become greater over the past few years: this raw materials inertia will be very high. But despite this, there are definitely achievements on the software market, undoubtedly the growth there is quite rapid. This is probably one of the hopes for the future. If everything is tied in only with raw materials, one could be very pessimistic about this.

PwC: From the viewpoint of personnel, you touched on the issue of resources. Indeed, everyone says that in general the situation is catastrophic. And not only from the viewpoint of a shortage…

A.I.K. 270,000 people started work over the year, and 263,000 left.

PwC: And why is there such high turnover?

A.I.K. Because of the salaries, the working conditions we are forced to use such resource as alternative military service at the post office: nearly 2,000 people did so this year.

PwC: How are you going to deal with this?

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A.I.K. How? Improve finances and raise salaries. There's no other option.

Cutting personnel is also an issue – and a tricky one. Non-core personnel are an enormous social burden. Cafeterias, garages, hairdressing salons, hospitals. As everything was, so it remains.

PwC: With regard to managers, is there the same problem? How difficult is it to select management personnel?

A.I.K. Very difficult.

PwC: Maybe you should have your own corporate universities, of a sort.

A.I.K. There is a corporate system of retraining and professional development for personnel, a qualifications commission, certification, it's all in place. There are a lot of things.

PwC: I think you've already formulated the requirements for yourself. So what are the main skills and qualities that you would demand of managers, young managers who came to help you raise up Russian Post?

A.I.K. An education in economics and the ability to use that education. Creativity would be mandatory. Because, here, the challenges are such that even with all their linearity they are very non-linear. But they are subject to a linear solution. The ability to learn is another necessity. Because this is a very specific kind of sector, nonhomogeneous, here there are a lot of factors where one's economic training can be applied. It is very variegated – a fertile environment for self-education.

PwC: Are logistics your own or are there partners?

A.I.K. Mostly our own.

The post was preserved almost in its entirety, because up to 2004 it was a conglomerate of independent legal entities. All post offices were independent and worked on a contractual basis. They didn't compete, but operated only in their own territories. It was only in 2004 that they were made into a united whole. Each main post office had its own system of salaries, its own economic benchmarks, so to speak. How it all managed to survive is just amazing.

There aren't many postmen, for example; despite the numbers, there aren't in fact that many of them. The bulk of work is in rural areas… it works out to one postman per thousand residents.

PwC: You mentioned financial services – how far along are plans to increase the amount of financial services provided through post-office outlets?

A.I.K. Well, they're still being formulated. There is already a certain practical experience that has been created. The mail now accepts payments in favour of banks, repayment of loans, we already have precedents of accepting deposits under contracts with banks, utility payments of course, money transfers, release of funds on cards, we have all of that already. It's just that quality, the system – that's another question. And in the income structure today, almost 60% comes from financial services rather than postal services. But this is related to tariffs as well: because finances are not regulated, rates are competitive, the post office itself establishes tariffs, and for transfers as well, and they are frequently lower than bank services, lower than the conditions that the banks offer. The prospects here are very good, because the network is enormous, but the capacity of this network, that's another question, as now all the services are delivered at one window, by one person. The Post is supposed to be a universal institution and it can, of course, do primitive banking functions. But to do so you need personnel who, at the very least, don't leave after a year. Otherwise it ends up being nothing but a training factory, and a fairly cheap one at that. And it has the potential to be a very promising line of business, because the banks do not have the money to build branches everywhere. They won't do it, they open up a hundred outlets, maybe two hundred and that's it. And the big cities are the main thing. And that's why for objective reasons they are interested in working with the post office.

PwC: To return to the delivery chain, to logistics: in theory, the market is there; can you choose now, or do you feel a certain restriction from the standpoint of partners?

A.I.K. Here the market follows from the state of infrastructure, from the state of our own assets; if your transportation is worn-out, you lose out. At one time there were post-office boats on the rivers, and now they've all died out, they're gone. The mail was delivered by river, cheaply. Now it can't be delivered. There was a post-office air fleet, and now there isn't. There are cities, populated areas, where there's no way to get through other than by helicopter. So we're faced with the desirable and the possible. I say that the fact that the post office survived the transition period is a huge miracle.

PwC: So in fact there is a shortfall in infrastructure?

A.I.K. No. But it's catastrophically undercapitalised, not depreciated. But I'm simply not going to mention any figures as to how much Russian Post's capital is estimated to be.

The authorized capital, that's 17 million roubles, that's not much It's a situation where you need to make serious state investments right away so that it can get on its feet somehow.

PwC: I'd like to ask now about the brand that we're talking about here. This is, I would think, a competitive advantage, a strong brand? People trust it.

A.I.K. I don't know how strong it is, it depends how you look at it. Yes. But on the other hand there are a colossal number of claims and complaints. So it's kind of a two-edged sword. True, Sberbank did have a similar story. On the one hand there's trust, on the other there's the association with queues and rude service.

PwC: Question about sorting centres. Catalogue shopping is now growing in Russia, and I think that for you it's some kind of special line of business?

A.I.K. Shopping by mail? Just today I was looking at the tariff component, and well, there are serious clients there,. and the sales through the postal system are pretty healthy.

PwC: To talk for a minute about the difference between Sberbank and Russia Post. You've moved to a new company. Two state-owned companies.

A.I.K. Now Sberbank is in fact a non-governmental company. There's a big difference.

It is after all a joint-stock company, and for this reason the operating independence is enormously higher in the bank. The range of goals is different… The bank is after all a more homogenous structure and works with a homogenous product. And the post office is more complicated, I'd say, from the point of view of internal organisation, than the bank. From the point of view of the substance of operations, if we're talking about financial operations, then of course there's no comparison, here they're very simple. Here there probably shouldn't be complex operations. In the end, it's not a bank and shouldn't ever be a bank. The bank may work, using the postal infrastructure, sure, but the post office as a whole is not a bank. It's a transaction system.

PwC: An enterprise like Russia Post, could it perhaps acquire, for example, certain operators? Logistics operators, or some other kind, in order to improve.

A.I.K. In theory, it could, I don't know, I wouldn't rule it out. Here there's also the process of spinning off companies: EMC, express mail, subsidiaries of Russia Post. So for now we're not buying, we're spinning things off.

PwC: In other countries there are other social expenses. What do they survive on there?

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A.I.K. Well over there I doubt that they're carrying leisure resorts on the balance sheet, services, and other sorts of things. In addition, if you look at other countries, state protectionism has been a lot stronger, it's kind of obvious, when they close off certain types of market against foreign operators for a certain period. Here though it was the other way around. They opened up the gates. That is, they gave the sweetest parts of the market to private operators. But the post office still managed to survive somehow… it simply lives with a shortfall, a chronic shortfall of working capital. Accordingly, it lives on due to its low salaries, due to its huge turnover.

PwC: Well, then, if we're to talk about the role of the state, because after all in many countries with fast-growing economies it's state capitalism of one kind or another, and the leading enterprises are seriously supported by the state. From your point of view, what is the state not doing, and what could it do to support enterprises, to realise their international ambitions and even realise their domestic ambitions?

A.I.K. I can't say that we had any kind of conscious policy. In part, we had some kind of sporadic solutions. All of a sudden, there would be some kind of sectoral prohibitive tariffs, or embargos on the delivery of something. And some kind of joint policy in such economic sectors that are also strategically important, despite the fact that there is a list of strategic enterprises. It's not evident that some one, somehow, was seriously protecting the interests of strategic sectors. That means aircraft, shipbuilding, transportation.

PwC: But now we're on the verge of WTO accession as well.

A.I.K. We'll see whether it happens at all. I'll be honest with you, it's not that I have doubts but I just don't see the pluses, especially for Russia.

PwC: Well, a breadth, variety of services, they say, for the public.

A.I.K. Well, the variety of services is not narrow now. It will just be an erosion of the local manufacturer, that's absolutely correct. For the majority of sectors, it's competition that they're not ready for. For specific advanced countries, the WTO is a good tool for expanding their own markets: they have the technologies, they have the companies. For those that are not in such a great position, well I think it's more of a headache. I don't know why we're so eager to join. It's not a matter of retrogression, but simply one of pragmatic interest. I don't see it. Maybe for a certain range of metals, maybe someone will come out a winner, but in general, I think, that's about it. All equipment manufacturers will lose out; the textile industry is completely on its knees as it is; agriculture is dying out.

PwC: In other words, right now at the government level there's no programme to develop the post office, no development strategy for the post office, no idea of supporting the post office?

A.I.K. We have to present a project, then maybe it will appear. In any case, it's on the agenda of the government commission. After all, the understanding is growing there that something has to be done.

PwC. That is, it will be developed deep inside the post office itself?

A.I.K. Well naturally with the involvement of the ministry.

A projection of 200 billion roubles has been calculated, based on the most obvious needs. That is the amount of investment required to raise the quality of services minimally, the financial position itself. But mainly it's the modernisation of the Post's infrastructure. Because, and I repeat, emergency measures are needed.

It's a medium-term development programme, let's say, for about three years.

Right now two automated centres are being created, and there should be 27, we need hundreds of mail cars, we need thousands of new vehicles – with regular replacement, and not how they use them now for 10 years or more.

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PwC: Yes, the volumes are enormous, and the volumes of investment should be enormous.

A.I.K. In some article it was written that the amount in general is fairly modest. If you look at the US Postal Service, it receives up to $4.5bn each year in tax return for providing a certain range of services.

PwC: What can the state do to increase the competitiveness of all of Russia, since after all right now there's a competition for capital among countries with rapidly-developing economies, there's a fight for markets, and many sectors are feeling this competition?

A.I.K. There are many things the state could do, but for now it somehow has not discovered them. At the very least, the tax system that we have in this country does absolutely nothing to stimulate investment. For example, you have to pay tax on imported equipment right away, despite the fact it will be put into operation only in five years' time. Payroll taxes, there again, there's something that should be thought about. Why have shadowy arrangements that have still not died out, to put it mildly?

PwC: Investments in infrastructure?

A.I.K. Investments in infrastructure. Take this idea that all free cash from oil-and-gas exports should be invested abroad; in my view, it's acceptable only for countries such as Switzerland. It is already difficult to find such scope for investments.

As a result, we risk losing time that we've been given by the favourable situation.

The state could use these funds in a more productive way, and not simply hold on to them at a low interest rate in dollar assets that are losing value. During this time jobs could have been created, demand, and so on.

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