

IKEA's Freeze Curtails Medvedev's Goal

By [The Moscow Times](#)

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An IKEA customer taking a break in the department of the store selling chairs in Khimki, just north of Moscow. **Andrey Rudakov**

IKEA, the world's biggest home-furnishings retailer, is just the type of investor Russia needs — and isn't getting — to overcome the lowest foreign investment rate among leading emerging-market economies.

The Swedish company says it won't build more stores outside the Moscow region until local officials stop withholding permission for two outlets in the cities of Samara and Ufa. After investing \$4 billion in Russia over 10 years, IKEA placed a freeze on expansion in June 2009.

The reason the stores aren't opening is that IKEA is refusing to pay bribes to safety inspectors, said Kirill Kabanov, head of the nongovernmental National Anti-Corruption Committee.

"We have a zero tolerance on corruption, and we have a very clear policy, and then things must take the time they take," IKEA Russia managing director Per Wendschlag said in an interview. He said he had no specific complaint on the delay in permits in the two cities.

At stake is President Dmitry Medvedev's goal to match the economic growth rates of other BRIC nations. With barely more than one-tenth the population of China and India, Russia needs to attract non-energy investors to grow and diversify. Corruption has "penetrated all branches of power," Medvedev said in a recent interview.

The president's credibility as a graft-busting former lawyer working to improve the business environment was tarnished in December when a Moscow court handed a new jail sentence to Mikhail Khodorkovsky, the former Yukos billionaire, said James Beadle, a British-based consultant for investors in Russia. Lack of progress risks harming Medvedev's prospects a year ahead of presidential elections.

Foreign companies have repeatedly faced difficulties in Russia. Royal Dutch Shell, Europe's largest oil company, in 2006 ceded control to state-run Gazprom of its biggest project in the country, the \$22 billion Sakhalin-2 oil and gas development, amid threats by regulators to revoke the permits on environmental grounds.

Russian health officials last year warned Nestle, the world's largest food company, that it was violating safety rules at its Russian plants. A spokesman confirmed the warning last month. It was a move to favor local rivals or extort money, according to Kabanov.

He has been on the board of Transparency International's Russia branch since 1995 and was an officer in the anti-corruption and anti-contraband units of the Federal Security Service from 1994 to 1998.

Wal-Mart Stores and Carrefour, the world's two biggest retailers, quit the Russian market in the past 16 months after saying they couldn't repeat the success they had had in other countries. Both companies are expanding in China, India and Brazil. Spokesmen for both companies repeated that reason in recent interviews.

"Russia has the largest consumer market in Europe with a relatively low degree of penetration," said Kingsmill Bond, chief strategist at Troika Dialog. "It's a very attractive market, but companies encounter endemic corruption and that is impacting foreign investment."

Vonnell Martinez, founder and chief executive officer of Vim Resources, a Miami-based investment firm, put a plan on hold in November to set up a \$100 million equity fund in Russia because he decided he couldn't risk investing other people's money in the country.

"All the uncertainty and political threats that are constantly attacking you, it crushes investment," he said. "If you grow too big, you're speculating and then you put yourself under the whim of people who can destroy your business from one day to the next."

Medvedev, who before his election in 2008 pledged to combat "legal nihilism" to win investment to help diversify Russia's economy away from oil and gas, said in a speech to the World Economic Forum in January that "we haven't yet achieved outstanding results" in the fight against corruption and for modernizing law enforcement.

Still, he said, "We are full of determination to act further," and "I am confident that we will manage to combat corruption."

Russia is the world's most corrupt major economy, according to Transparency International's 2010 Corruption Perceptions Index, issued in October. It holds the 154th spot of 178 countries surveyed, tied with Tajikistan and Kenya.

To be sure, Russia's position as the world's largest energy exporter yielded BP's Jan. 14 agreement to swap 5 percent of its shares for a 9.5 percent stake in Rosneft, Russia's biggest oil producer, and jointly explore new Arctic fields.

PepsiCo's accord in December to buy a controlling stake in Wimm-Bill-Dann, one of Russia's leading producers of juice and dairy products, for \$3.8 billion is also a sign that companies want to tap into Russia's fast-growing consumer market.

In addition, the benchmark MICEX Index has risen 28 percent in the past 12 months, while the comparable Chinese index is down 5.2 percent and India's Sensex Index has risen 10 percent.

IKEA's Wendschlag said same-store sales in Russia are growing at more than 20 percent a year. The company, whose holding unit is based in Leiden, Netherlands, currently has 12 stores in Russia and had planned to open the largest commercial center in Europe outside Moscow among other new outlets, Wendschlag said.

"We are one of the top-selling IKEA countries in the world," he said. "The potential with 141 million people who are interested in consuming and furnishing their homes is big."

At the same time, concern about the legal system is one reason Russia got less than a third of the investment fund inflows of China, slightly more than 40 percent that of Brazil and less than did India in the past three years, according to EPFR Global of Cambridge, Massachusetts, a research company that tracks \$13 trillion of assets.

Foreign direct investment in Russia was about \$8 billion in the first nine months of 2010, compared with \$16 billion in 2009, according to Bank of America Merrill Lynch Global Research.

Political risk and corporate governance issues mean that it isn't safe to invest long-term in Russian stocks, said Kaha Kiknavelidze, a managing partner at London-based Rioni Capital Partners that manages \$60 million in emerging markets.

"Politics influences the corporate side, particularly in big sectors, so much that it's very difficult to get comfortable on a company's political stance in the long term," he said by phone. "We like to look at a 12-to-18-month horizon in Russia."

IKEA's founder, 84-year-old Swedish billionaire Ingvar Kamprad, has his own concerns. The company fired two executives in Russia in February 2010 for allowing a contractor to pay a bribe related to a store in St. Petersburg, the company said in a statement at the time.

Kamprad said in a statement in December that he had been "over-optimistic" about his company's ability to navigate the Russian market. "It is shocking and sad that our organization got carried away."

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