Interview with Frank Schauff, Chief Executive Officer, Association of European Businesses (AEB)

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Tags: Association of European Businesses (AEB)

The AEB works through a number of channels to promote the interests of European corporations with operations in Russia. It has a long history in this country, dating back to 1995. Why is a group like the AEB necessary, and what are the main targets on its agenda this year?

I will begin with a few words about the AEB in general. It is quite a unique organization. First, it is the only body that represents the business interests of multiple countries: of course, we represent pan-European interests; but additionally, we represent the interests of some very notable American and Japanese companies, as well as companies from a number of other countries.

We have a specific structure at the AEB that differs from that of other associations: we have about 40 committees working inside the organization. These are partially industry committees, and partially horizontal committees dealing with questions like taxation and customs. Quite a few of our industry committees are very strong—for example, we represent close to 100% foreign automobile makers in Russia. We have an excellent banking group and a strong energy group. Our pharmaceutical committee is quite influential as well, counting amongst its membership the main European players and also some major American companies.

As stated in our charter, we believe that our mission is to help the integration between Russia and the E.U. For this, the economic side is obviously essential but the political side is very important for us as well. We are interested in facilitating a friendly relationship between these regions. About

50% of Russian trade is with E.U. countries, and more than 70% of investment in this region comes from European sources. The European relationship is hence very important for Russia, and the converse is true as well: Russia is the third-most important trading partner for the E.U. We now have approximately 640 members—mostly larger European corporations. Currently we are the main representation for foreign investors here in Russia. The Russian government does not ignore us when we make a statement. Perhaps they will not agree with our position, but they will certainly communicate with us.

The core of our business is lobbying. We try to influence, in a friendly and accountable manner, the environment here in a way that will help our members to conduct business and invest. Success in the lobbying business is not easily measurable, but through a continuous effort matters are likely to move forward.

This year the main targets on our agenda include: localization schemes, customs and taxation issues, the question of a national payment system being instituted in Russia, and the issue of WTO accession.

However, from our point of view, the question of a national payment system being instituted in Russia is not entirely in line with the idea of making Moscow an international financial center.

The AEB represents several thousand European persons residing in Russia, and therefore immigration and legislation issues are always high on our agenda. This may be a bit unusual, but it plays a role for us because it has to do with the practical implications of working here.

The AEB represents companies from the entire scope of the E.U., and, as you mentioned, it also represents American companies, Japanese companies, and some other foreign nationals. How realistic is it to forge a common agenda for these diverse parties?

It is not so much a matter of nationality. It is more a matter of consolidating the opinion of a given industry and delivering this consolidated message to the Russian government. This does not differ very much from what other associations are doing all around the world.

The AEB has an important role here because we can give the Russian government advice or indications on the basis of thorough discussions with united groups of foreign players—be it in industry-specific areas, or be it on a broader level when it comes to legislation on taxation, for instance.

In late April, you met with the Vice-President of the European Parliament, Rainer Wieland, and briefed him on the major issues at stake for European investors in Russia. What did you tell him?

When you are doing business in Russia and you come from, for example, the E.U. or the U.S. the big difference is that the environment is more fluid here than it is in the West. Certainly, in the U.S. or in Western Europe, we see a more established legal framework. Russia as a country exists independently for less than 20 years now, and coming from a Western model, you become aware that many pieces of legislation that you are used to in your home market do not exist here. Many pieces of legislation that do exist could perhaps be improved in order to enhance functionality. These are issues that are of general interest not only for AEB members, but also for the Russian public.

The AEB represents many industrial sectors. As European companies are the market leaders in pharmaceuticals in Russia, and this industry is currently on the discussed at the highest levels of government up to and including the president and prime minister, what do you believe is the significance of the pharmaceutical industry amongst the AEB’s diverse priorities?

It is a very high priority for us. First, as you mentioned, we have quite a few pharmaceutical market leaders within our membership. It is also true that this industry is a political priority here and rightly so. When you consider the demographic situation in Russia, the statistics with regard to healthcare, and the pharmaceutical environment, the situation is quite disconcerting. In a country where life expectancy is rather low in comparison to European neighbors and where we are still battling communicable disease on a wide scale, things have to be done!

For example, there is something in place now that is called the Partnership for Modernization between the E.U. and Russia. We, as an association, already last year defined some priorities that differ a bit from what the Russian government considers priorities.

Certainly, when it comes to the question of localization, the pharmaceutical industry is quite different than, say, the automobile industry—which the government is similarly pushing to localize. The localization of the pharma industry seems to be far more complex. The needs are more diverse, and much more complicated. There are issues with clinical research and IPR; there are questions regarding technology, packaging, and so forth. This seems to be a very demanding exercise. We see that there is a tendency now to localize production, but I believe that it will still take some years until we see a substantial increase of real full-cycle manufacturing in the Russian territory.

The Russian government is certainly very interested in this kind of commitment, but while Russia is becoming more and more open, issues such as red tape and lack of transparency remain. For example, pharmaceutical companies looking to set up manufacturing facilities here still have no

official word about the definition of ‘local status.’ What is your understanding of the Russian bureaucratic environment?

I think that in many cases, it would do the Russian government good to reduce inhibitive administrative procedures. I am from Germany, and began my work here four years ago. I came to learn that quite a few documents that do not exist in Germany—or in America, or in France. This certainly creates a problem, because companies must expend more resources to overcome such barriers. It costs money, and effort, and time. This is an obstacle to development!

If we consider the pharmaceutical sector, there are quite a few problems that we are consistently discussing together with our members and the Russian government. Certainly, things could be simplified. I understand that the authorities must regulate the sector and that the government must have clear guidelines, but in many respects there are too many guidelines here in Russia which often go in different directions. This can be more confusing than helpful.

With extensive bureaucracy—and especially contradictory bureaucracy—corruption and poor ethical practices tend to increase. A reduction of bureaucratic procedures would certainly be helpful.

You mentioned that one issue on your agenda is Russia’s ascension to the WTO. As Russia looks to join this organization, it must resolve issues like defining an international standard of intellectual property protection. After 20 years of talking, do you believe that Russia will finally take the necessary steps to work out issues like this, and finally become a part of the WTO?

Let us be very clear. We at the AEB are certainly in favor of WTO accession, because this may help provide general guidelines for the overall development of the Russian economy and Russian society, in harmony with international standards. We assume that the modernization agenda that has been announced by the Russian government may be simplified in the end.

We understand, however, that there is resistance on the part of certain stakeholders of Russian industry against WTO ascension. However, this is not the case in the pharmaceutical area because there is not a particularly robust local pharmaceutical industry.

We are indeed approaching close to 20 years of negotiation to enter the WTO. In certain sectors, Western industries have been very successful in coming to the Russian market. This does not arouse joy amongst their Russian competitors who believe that WTO ascension will further jeopardize their business. Therefore, I must say that I am always a bit skeptical about the announcements that Russia will become a member country soon, because we have heard these

announcements for many years.

In many ways, the West may be beginning to view Russia in a new light. How do you think the relationship between the E.U. and Russia has evolved?

The E.U., in general, unless there is a crisis on the horizon like the one in 2008 with Georgia, has an objective interest in fostering stable development on the European continent, and this means having a stable relationship with Russia—like it or not! Russia is, again, one of the E.U.'s top trading partners, and in a very vital area: energy. Certainly, the relationship must be stable not only politically, but also in economic terms.

Russia and the E.U. have a highly institutionalized connection. It rarely comes up in the press, but there are very many dialogues going on between the E.U. and Russia on a governmental level. This is not as much the case on the American side. I am not sure if the Americans have the same interest, but the Europeans, being close neighbors, are perhaps in a different situation.

In general, what do you see as the future development path for Russia, and how will its development affect your member companies?

From the point of view of European companies, and international companies in general, Russia is certainly a strategic market. With 140 million inhabitants and with high GDP growth, it is too big to ignore!

Even if you might complain about certain problems that you encounter here, the opportunities are nonetheless lucrative. From my point of view—and I came here for the first time in 1987—Russia has changed very much. Foreign investments have helped to modernize and build up certain sectors, for example pharmaceutical or automobile. This development will continue. Perhaps it will not proceed as quickly as the Russian government would like, but it will continue nonetheless and I think that foreign investors will play an important role.

There is an interesting situation in Russia, because from a business standpoint, it continues to be chiefly headed by oligarchs, and oil and gas remains the foundation of its economy. Do you believe that the middle class can take over, and that other industries can play a more central role?

Certainly, the economic structure that we have here in Russia, founded on oil and gas and with large players controlling the greater share of GDP, is very specific. Therefore, I also think that foreign investors play a different role here than foreign investors in the U.S. or Germany or France, because their role in Russia is to increase competition. Increased competition helps also to develop certain sectors, decrease prices, and etc. I think it is a long-term process.

Under the current conditions of this economic structure, and considering the fact that interest rates are above 10% with short mandatory payback periods, it is very hard for small and medium-sized businesses to really develop and grow. There are very tough conditions here. In all, I must say that I am a bit skeptical about the idea that in the foreseeable future there will be a flourishing middle class heading innovative small companies, as we see in the U.S. or France or Germany. I think that the conditions are not very favorable.

What is then your advice to foreign investors regarding Russia?

The short version of the advice is that you should come here because it is an interesting market and very dynamic. Secondly, you should not ignore the risk that you are taking on. And third, you should not be naïve! Russia is not a European Union country; it does not have European Union legislation in place; and Russians play by different rules.

There are also large differences in mentality. In Russia, people mostly look European and see themselves as European because they live on the European continent. Nonetheless, there are quite a few cases where, say, you have a joint venture or some other form of agreement between a European partner and a Russian partner, and conflicts arise—because, for example, the expectation on the Russian side for attaining high profits is much more pronounced than on the Western side. In the West, we are used to stable growth, low profit margins, etc. In Russia, the expectations are different—and this may lead to disagreements.

The time horizon is also generally shorter than Westerners. A long-term lease contract in Russia may be for three years; whereas in Germany a long-term lease may be for 25-30 years—this is an illustration of what long-term is in a Russian understanding, versus a Western understanding.

Despite lingering difficulties, you seem to have a very personal interest in this country, dating back to your days as a student. What is that you feel so draws people to this nation?

It is simply intellectually interesting. It is very dynamic and very complex.

It is demanding! It is demanding to work here, and it is demanding to live here. But it is extremely interesting.

What is your final message to the international readers of Pharmaceutical Executive?

You should take the Russian market very seriously! As I have said, it is too large to be ignored.

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