

A father and son with big ambitions around one of the world's largest rail networks are finding there is 'no fast track to heaven'

BY DOUGLAS BUSVINE AND
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To get an idea of how parts of the Russian economy still resemble the Soviet Union, take a look at Russian Railways. With 85,000 km of track, 1 million employees and turnover of \$40 billion a year, the state run company remains a heavyweight symbol of the old command economy.

Now President Vladimir Putin's government has ordered the privatisation of a one-quarter stake in the company by the end of 2013. That's starting to open up Russian Railways' management and strategy to closer scrutiny – some of it unwelcome.

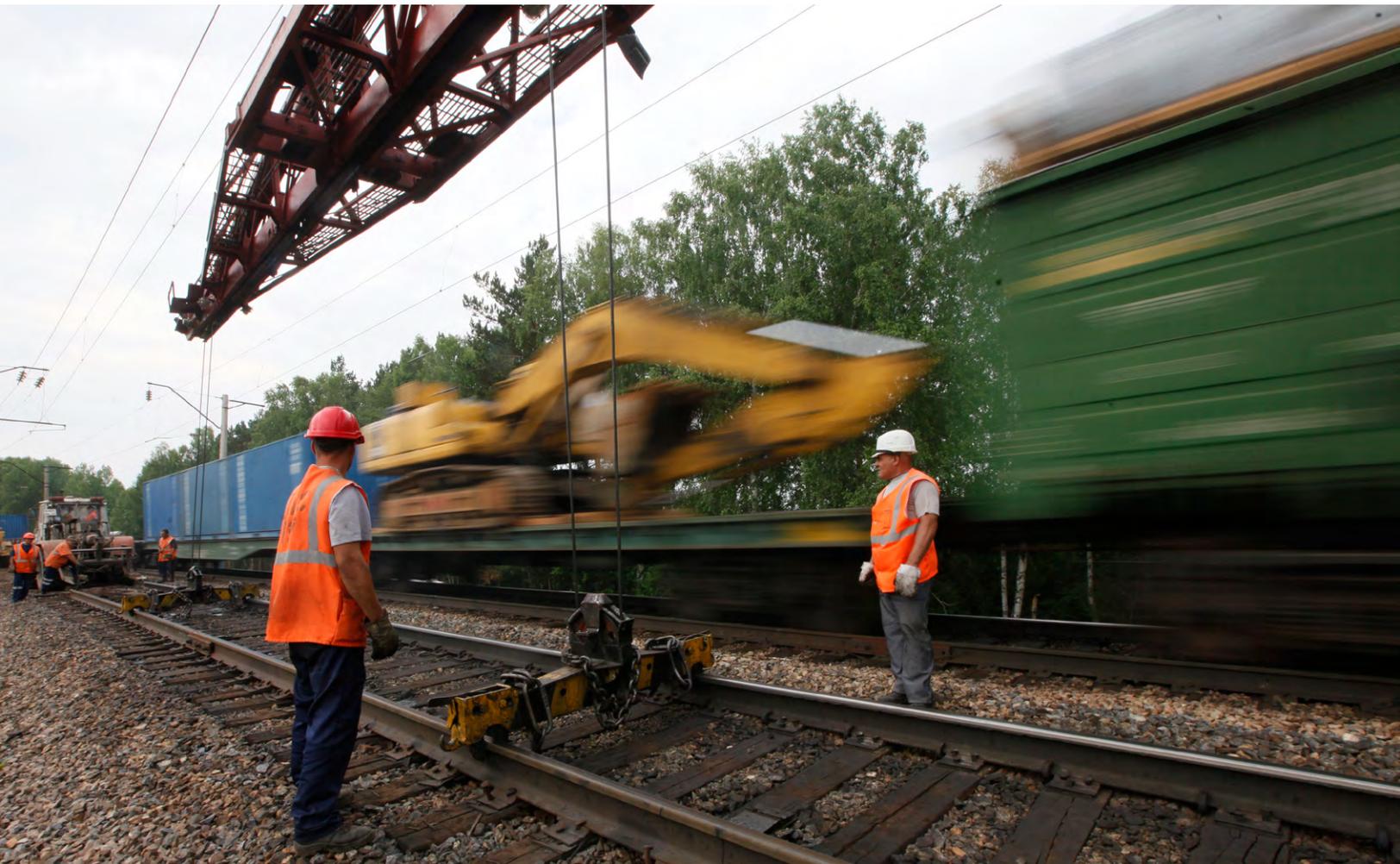
A Reuters investigation has identified business ties between the son of Russian Railways president Vladimir Yakunin and firms and businessmen linked to the railways giant. Andrey Yakunin, 37, a London-based investor, is pursuing a \$500 million plan to build hotels across Russia, partly with the help of a subsidiary of the company run by his father. He also shared offices until recently with a private venture aiming to ship millions of tonnes of freight between Asia and Europe by Russian rail, rather than traditional sea routes.

Russian Railways' family connections

PRIVATIZATION ON TRACK: a quarter of the state-owned Russian rail network is to be sold off by the end of next year.

REUTERS/ILYA NAYMUSHIN

RUSSIAN RAILWAYS AMBITIONS OF A FATHER AND SON



LINE MANAGEMENT: Workers replace track in the Taiga district of the Trans-Siberian Railway, which some envisage as an alternative route for transporting goods from China to Europe. **REUTERS/ILYA NAYMUSHIN**

While Andrey Yakunin is open about his business ties to Russian Railways - and there is no suggestion of any illegality in those links - the state rail monopoly has made only scant disclosures in filings to investors. In a statement to Reuters, Vladimir Yakunin denied any ties at all.

"It's a huge cultural problem," said Elena Panfilova, head of the Russian chapter of anti-corruption watchdog Transparency International. "The core management of Russian Railways comes from a past where it was not the norm to disclose any information, even if it's public and even if it doesn't hurt their operations. It would be much better to explain

and show how these connections go."

Andrey Yakunin denies that any conflicts arise through his dealings with companies linked to the state railways. But, in an interview with Reuters, he said he understood concerns over whether he might have gained an advantage from his father's position.

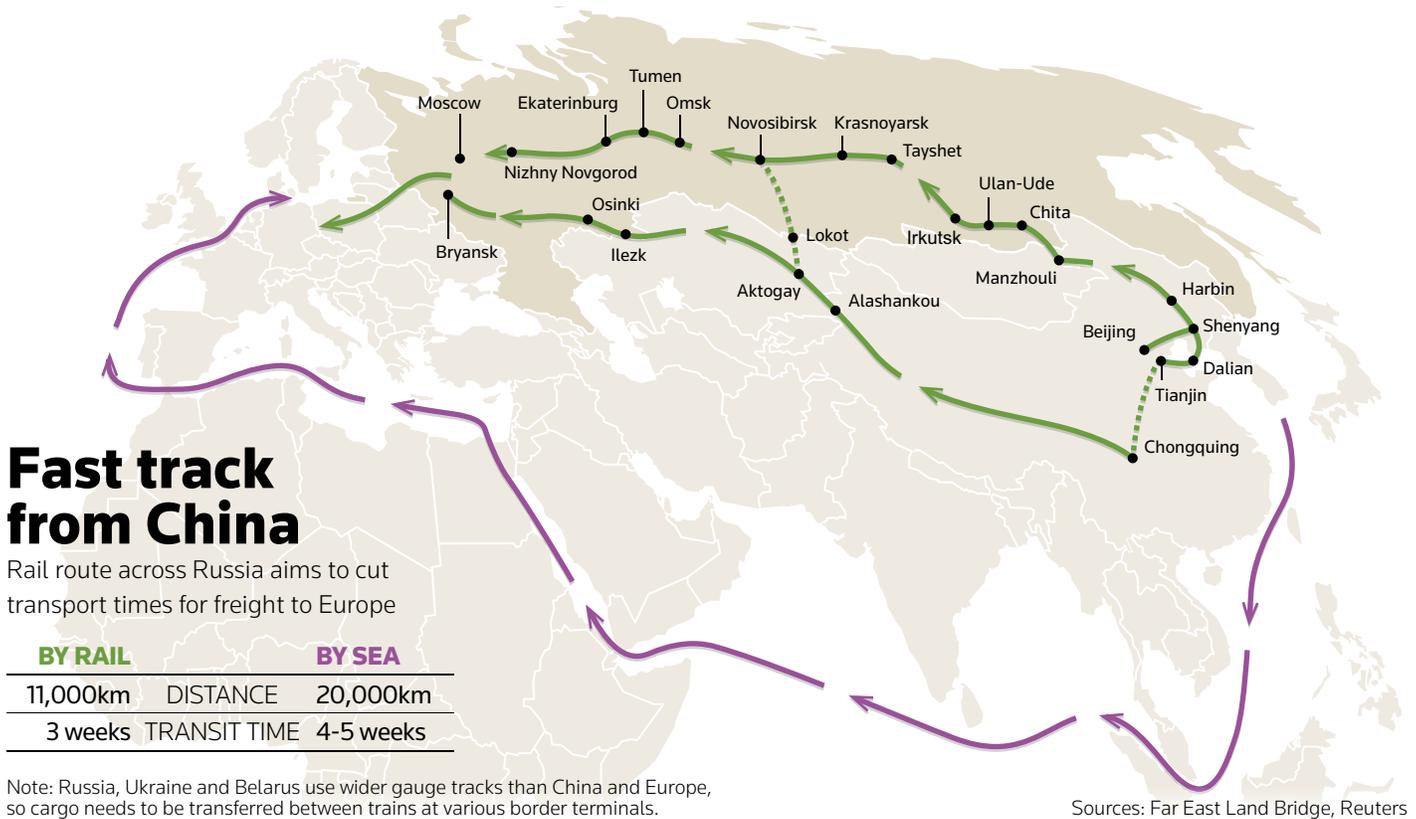
Asked whether his partnership with the real estate arm of Russian Railways might raise questions of disclosure for the state rail monopoly, he said: "I agree, but I'm not getting money from them - I'm paying them."

Nor was buying land from a subsidiary of Russian Railways any goldmine because of his father's position, he said.

Though he had originally thought he had "direct access to the second-largest landowner in the country", Andrey Yakunin said that, thanks to the complexities of land ownership in Russia, his connections were "no fast track to heaven".

The elder Yakunin, 64, declined to be interviewed for this article. In a statement issued to Reuters, the firm said that there were no business links between Russian Railways, which is also known as RZhD, and Andrey.

"Concerning any financial interests on the part of RZhD and its president in the companies you name - they do not exist," the statement said.



Fast track from China

Rail route across Russia aims to cut transport times for freight to Europe

The statement declined to comment on individuals in business with Andrey Yakunin while also having roles at companies either controlled by or linked to Russian Railways.

In the system of Kremlin capitalism built by Putin since he first became president 12 years ago, Vladimir Yakunin is a quintessential insider. The son of a military pilot, he was brought up in Estonia, studied in St Petersburg and later flourished thanks to relationships he built both before and after the Soviet collapse in 1991.

Around the same time that Putin returned from his posting overseas as a KGB agent to start a political career in his native St Petersburg, Yakunin also arrived there, having left the Soviet mission to the United Nations in Vienna to go into business in Russia's second city. The two men soon got to know each other.

On Putin's rise to the presidency in

2000, Yakunin entered federal government and emerged in 2005, after a power struggle, as head of Russian Railways, which in many ways is the blood supply of the world's largest country.

"Mr Putin once said that if you want to know the status of the Russian economy, you should look at the papers of the president of Russian Railways with the daily reports of the amount of cargo, the directions of delivery and amount of passengers."

20

Number of business traveller hotels across Russia planned by Andrey Yakunin

Source: Regional Hotel Chain

Yakunin told the Daily Telegraph on a visit to London this year to market a bond offering by the railways.

The year after Yakunin became Russia's train-driver-in-chief, his son founded a real-estate investment fund, based in London, with an Israeli-born investor called Yair Ziv. The firm began to develop plans for a chain of hotels aimed at business customers travelling across Russia, concentrating on major regional centres from Krasnodar to Khabarovsk.

In 2009 Andrey Yakunin struck a landmark deal with Rezidor, a company listed on the Stockholm stock exchange that has long experience operating hotels. Andrey's company Regional Hotel Chain (RHC) would acquire and develop the sites and Rezidor would manage the hotels. Together they set about planning 20 hotels with, as Andrey said in an email to Reuters, a "fast and massive nationwide roll-out" in mind.

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Andrey said the first three hotels in operation – in the provincial cities of Kazan, Astrakhan and Izhevsk – have nothing to do with RZhD. But plans for at least five other sites are next to or very near key rail stations, according to Rezidor.

To acquire suitable plots, Andrey Yakunin said his firm conducted a “rigorous selection process” to find a property consultant in Russia. It settled on Zheldoripoteka, a subsidiary of Russian Railways. Zheldoripoteka has since helped RHC to secure hotel sites, Andrey Yakunin said.

“We were able to locate a few land plots, which we did eventually acquire through Zheldoripoteka,” he said. They are next to or close to stations in key cities.

But he added that the relationship has not made it any easier for him to acquire land in a country where red tape and corruption make completing deals a challenge. “Without disrespect, the way they have built the process in the company for selling off something from the company’s assets is painful.”

WHAT’S IN A NAME?

Andrey Yakunin is not averse to playing up family associations as he seeks investors for his ambitious hotel plan.

“Yakunin is a brand of a sort,” he told Reuters in an interview over lunch in May at the trendy Blackberry Café in downtown Moscow.

The eagle-eyed might notice that the initials of his private equity and real-estate fund, Venture Investment & Yield Management are strikingly similar to those of his father Vladimir I. Yakunin. They might notice, too, that VIYM’s St Petersburg office is headed by Andrey’s younger brother, Viktor, who has worked for Gunvor, an oil trading firm run by billionaire Gennady Timchenko who also got to know Putin well in the St Petersburg of the 1990s.

But Andrey, a fluent English speaker whose string of qualifications includes an executive MBA from London Business School, said he avoids potential conflicts of interest. “I have to be very careful about



NETWORK PRESIDENT: Vladimir Yakunin, president of Russian Railways, and, right, his son Andrey, who is developing hotels near rail stations. **REUTERS/(ABOVE) ALEXANDER NATRUSKIN AND REUTERS/(RIGHT) IVAN BURNYASHEV**

“They assured us that there is a firewall between the investment company that is owning the Regional Hotel Chain and Russian Railways

Arild Hovland

Russia country manager of Rezidor, the hotel operator partnering with Andrey Yakunin

industries that maybe I find interesting, but I just stay away from ... because I don’t want to create any trouble,” he said.

He said he had turned down an opportunity to tender for fast-food concessions at Russian train stations, adding with a laugh: “I’m still crying over it.”

His father, a champion of conservative moral and religious causes, flatly denies any personal link to his son’s company VIYM, saying in a statement that its initials “bear no meaning besides the creation of an abbreviation.”

“All attempts to extrapolate from this coincidence any kind of affiliation with the head of Russian Railways amount to fiction,” added the statement issued by his office in response to questions submitted by Reuters.

Arild Hovland, Rezidor’s Russia country manager, told Reuters that the Swedish hotel operator had a relationship with Andrey



Yakunin before partnering with RHC and had accepted assurances that he had no business link with his father or Russian Railways.

“Of course we looked at the background of Andrey Yakunin and, sure, we are aware of his father as the top official in Russian Railways,” Hovland said. “However, they assured us that there is a firewall between the investment company that is owning the Regional Hotel Chain and Russian Railways.”

Russian Railways has felt no need to detail Andrey’s relationship with a subsidiary of the company headed by his father. RHC’s partnership with Zheldoripoteka, the real estate arm of Russian Railways, was not made clear in any of the prospectuses for billions of dollars in bonds recently issued by the state rail company.

Hotels are not the only connection between the RZhD and the London office of

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Andrey Yakunin's VIYM. The premises on the 16th floor of the Marble Arch Tower, at 55 Bryanston Street in London's West End were also home, until early July, to another occupant looking to ride the footplate of Russia's rail opportunities: a firm called Far East Land Bridge.

FELB is a freight-forwarding company that joined with a subsidiary of Russian Railways called Transcontainer to offer rail freight transport between Europe and Asia – a potentially lucrative market. While the overland route from China to Europe through Russia is relatively direct, freight sent by ship must travel via the Indian Ocean and Suez Canal. At 18 to 24 days the land bridge takes roughly half the time of seaborne shipments. Among the other advantages FELB claims are lower costs per tonne and more flexibility in changing final destinations during transport.

The company, which this month moved its headquarters to Vienna, is controlled through a nominee-based structure originating in Cyprus. There it uses the same company secretary and the same office address in Nicosia as a number of VIYM-related entities, documents show. Cyprus is a popular offshore venue for Russian businesses because it does not require companies to disclose their beneficial owners.

One of FELB's web sites is registered in the name of Yair Ziv, Andrey Yakunin's partner at the real estate investment fund VIYM, according to a web registry. Ziv declined to comment in response to e-mailed questions regarding VIYM and FELB. And Andrey Yakunin, who set up VIYM with Ziv in 2006, said he was "not involved at all" in FELB.

"Yair does a lot of things in his own right, and if I know about 5 percent of what he's doing, maybe I'm flattering myself," he said.

But Vladimir Yakunin's statement that neither he nor Russian Railways had a financial interest in FELB is contradicted by statements



INVESTMENT NEEDED: Russian Railways is seeking billions to upgrade its infrastructure and rolling stock. REUTERS/SERGEI KARPUKHIN

and filings made by a subsidiary of Russian Railways called Transcontainer. London-listed Transcontainer recently sold its stake in FELB to a firm called RZhD Logistika that was set up in 2010 and is 100 percent owned by Russian Railways. RZhD Logistika announced on June 29 that it had completed the purchase of a 10 percent stake in FELB and intended to raise it to 25 percent.

Andrey Zhemchugov, a spokesman for Transcontainer, described the FELB equity and debt transfer as an "intra-holding optimisation" within the Russian Railways group. In a recent filing, Transcontainer said that FELB was "in fact controlled by the RZhD group".

How such joint ventures between RZhD and private firms will be affected by the privatisation of the state company has yet to become clear. The potential risks and rewards on all sides are high. Vladimir Yakunin estimates a 25 percent holding in RZhD to be worth \$8 billion, but government officials reckon it nearly three times higher.

Yakunin argues that it makes "no sense" to sell a stake in Russian Railways as a whole, and it would be better to continue his strategy of spinning off and selling operating units. But Prime Minister Dmitry Medvedev recently accelerated the privatisation plans - with the stake in Russian Railways to be sold by the end of next year.

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