1. Introduction

Many economies in the world are undergoing some form of transition. However in some countries the degree of change has been unprecedented as they are changing from a centrally planned economy to a market-based system. These 'transition economies' include countries of the Former Soviet Union (FSU), Central and Eastern Europe (CEE), China, Mongolia and Vietnam. Most of these countries adapted some form of 'shock therapy' that included rapid price liberalisation, opening up to international trade, and mass privatisation. Organisations, faced with such radical institutional upheaval, frequently struggled to adapt, leading to sharp drops in countries' industrial output and dramatic economic decline. Nowhere was this more apparent than in Russia where, in the first decade of transition, industrial production dropped more than 50 per cent and the economy contracted by around 60 per cent.

In Russia privatisation proceeded rapidly – it took only three years to transfer most state enterprises into private hands. However, two key factors inhibited change inside the organisations at the time: first most companies ended up in the hands of 'insiders', mainly existing managers, who had no experience in a market economy. Second a relative absence of legal, regulatory and financial institutions allowed many managers to pursue their own interests with impunity. In the planned economy, firms were largely state-owned and had excess employment and inventories, dated physical resources, extensive social services and a non-competitive product portfolio.

Managers faced cognitive barriers to understanding the radically changed environment and existing resources lost their value, while firms lacked resources normally considered standard in mature market economies, such as marketing and finance functions, and a portfolio of products in demand on the market. The new market conditions and the collapse of the old supply relationships required organisations to radically reappraise their operations, change their approach to business, and thus transform their organisations in order to survive.

RUSSIAN OIL INDUSTRY RESEARCH SETTING

The process of organisational transformation was particularly rapid in certain of the Russian oil companies (Khartukov, 2001; Dixon, 2004; Grace, 2005), to the extent that some of the integrated oil companies were beginning to compare themselves with the Western oil majors (Khartukov, 2001). The Russian oil industry thus provided an opportunity to analyse, at a company level, a rapid process of organisational transformation over a short period of time. Organisational transformation has been defined by Newman as: 'intra-organizational change that leaves the organization better able to compete effectively in its competitive milieu' (2000: 603). The purpose of this book is to explain this process of organisational transformation in the Russian oil industry in the critical ten-year transition period from 1995, when the Russian oil companies were privatised, up to 2005.

The main theoretical perspective adopted for the company-level analysis was the resource-based view, which highlights how the deployment of unique and idiosyncratic organisational resources and capabilities generates competitive advantage (Wernerfelt, 1984; Barney, 1991). The Russian oil companies provided a particularly interesting quasi-experimental setting, in that four firms started from similar positions in the mid-1990s, but followed different paths over the next decade. Two of these companies – Yukos and TNK/BP – demonstrated, *prima facie*, a high degree and rapid pace of organisational transformation towards Western business models (I call them 'Western-style' companies). This permitted literal replication between the two cases (where similar results are predicted) (Yin, 2003). The other two companies – Lukoil and Surgutneftegaz – were changing more slowly (I call them 'Soviet-style' companies). This permitted theoretical replication where different results are obtained but for predictable reasons. Table 1.1 provides basic data on the four oil companies and illustrates that Yukos was the leading company in 2002 in terms of growth in oil production, production costs and market capitalisation. The production and financial indicators for the other Western-style company – TNK – lagged the other companies, partly due to the later privatisation of this company and its inheriting the rump assets. As I shall argue below, however, organisational learning within this company and its organisational transformation clearly distinguished it from its Soviet-style counterparts. Indeed, by the end of 2004, it had gained the leading position in the industry in terms of oil production growth.

Table 1.1 Basic data on four Russian integrated oil majors

	Yukos	TNK	Lukoil	Surgutneftegaz
CEO¹	Mikhail Khodorkovsky	• Simon Kukes (German Khan Viktor Vekselberg) ⁷	Vagit Alekperov	Vladimir Bogdanov
CEO background¹	<ul style="list-style-type: none"> • 1963 – born Moscow • Mendeleev Institute of Chemical Technology • Deputy Head • Komsomol • 1986 – first business/private café • 1988 – import/export business \$10 mn. • 1989 – Bank Menatep • 1996 – First VP Yukos 	<ul style="list-style-type: none"> • 1946 – born Moscow • Moscow Chemical Institute • 1977 – Emigrated to USA • US citizenship • To 1995 – Work for US oil firms Phillips and Amoco • 1995 – Return to Russia 1995 as head Yukos refining • 1998 – President TNK 	<ul style="list-style-type: none"> • 1950 – born Azerbaijan • Azerbaijan Institute of Oil and Chemistry • To 1979 – Caspian oil fields • To 1984 – Siberian oil fields • 1984 – General Director, Kogalymneftegaz • 1990 – Deputy/Acting Minister of Fuel and Energy • 1991 – President Lukoil 	<ul style="list-style-type: none"> • 1951 – born Siberia • Tyumen Industrial Institute • 1973 – started as technician in Siberian oil fields • Rose to deputy general director and general director Surgutneftegaz
Ownership/control²	<ul style="list-style-type: none"> • ‘Western-style’ Mikhail Khodorkovsky	<ul style="list-style-type: none"> • Western-style’ Viktor Vekselberg Peter Aven Mikhail Friedman German Khan	<ul style="list-style-type: none"> • ‘Soviet-style’ Vagit Alekperov	<ul style="list-style-type: none"> • ‘Soviet-style’ Vladimir Bogdanov

Table 1.1 (continued)

	Yukos	TNK	Lukoil	Surgutneftegaz
	<ul style="list-style-type: none"> • Oligarch • Entrepreneur • Major shareholder 	<ul style="list-style-type: none"> • Oligarchs • Entrepreneurs • Major shareholders 	<ul style="list-style-type: none"> • Oligarch • Industry bureaucrat • Major shareholder 	<ul style="list-style-type: none"> • Oligarch • Industry bureaucrat • Significant control of shares
Head office¹	Moscow	Moscow	Moscow	Surgut
Oil production kb/day 2002 ³	1,392	753	1,515	987
Oil production growth 2002 ⁴	20.3%	9.1%	1.5%	11.7% ⁹
Refinery throughput, kb/day 2002 ³	623	284	681	298
Production cost 2001 ⁵	\$1.76/bbl	\$3.63/bbl ⁸	\$2.50/bbl	\$2.50/bbl
Market value 31 December 2002 (World ranking – PFC 500) ⁶	\$ 21 billion (no. 15)	n/a	\$13.1 billion (no. 33)	\$13.2 billion (no. 31)

Notes and sources: ¹ Company data. ² Grace 2005. ³ (Petromarket Research, 2003) ⁴ (IEA, 2004). ⁵ (Landes et al., 2004) Compare ExxonMobil \$3.38/bbl (2001). ⁶ (PFC Energy, 2004) Compare ExxonMobil, \$235.1 billion (No. 1). ⁷ Although Kukes was CEO, Khan and Vekselberg were the key decision makers. ⁸ TNK came late to the privatisation process and inherited the rump assets. ⁹ Surgutneftegaz increased production by excessive and inefficient drilling.

OVERVIEW OF RESEARCH

Research interest in the transition economies of Central and Eastern Europe is expanding rapidly and is not only influenced by existing organisation theory, but also attempts to influence it. Thus Meyer and Peng (2005) postulate that research into the resource-based view in transition economies makes a contribution to general theory development in strategic management and international business beyond the context of the CEE. Furthermore, the context of organisational transformation in transition economies provides an interesting setting for the empirical testing of the resource-based view, providing a societal quasi-experiment for testing and developing theories by engaging them in an unusual and changing context.

The objectives of this research were thus twofold: to investigate the process of organisational transformation in the Russian oil industry and to contribute to resource-based theory in the context of the Russian oil industry. In pursuing these objectives I sought to understand how and why the process of organisational transformation differed between Russian oil companies and to what extent the resource-based view helped to explain this.

The study is based on longitudinal and cross-sectional case studies of four Russian oil companies covering a ten-year period from full privatisation of the oil industry in 1995 to 2005. Interviews were conducted from 2001 to 2005 and respondents were asked to talk about organisational change since privatisation. A longitudinal and qualitative approach is one most often used for research into organisational change (Pettigrew et al., 2001; Dawson, 2003). Choosing a period of rapid change allowed me to conduct a processual analysis of change over a relatively short period of time. The novelty and complexity of processes in a transition economy suggested the use of an interpretive approach, which is appropriate where the phenomena to be investigated are complex and not well understood.

Semi-structured interviews were conducted as it was essential to gain an in-depth knowledge and understanding of the organisations and their processes (Rouse and Daellenbach, 1999). Respondents included managers at different levels (top, senior and middle managers), representing different functions (e.g. strategy, PR, HR, finance, manufacturing and production) at two types of location (head office and regional subsidiaries). External experts with knowledge and experience of the case companies were also interviewed to gain a triangulated view of the general context of the industry. This triangulation of source data avoided over-reliance on perspectives of senior managers who might present events in a favourable light. Seventy-one interviews were conducted in which seventy-four respondents were involved. Eight of the respondents had worked in two of the companies. In 2003, while the research was still being conducted, two important events

happened: TNK merged with BP to form a fifty/fifty international joint venture (JV); and the CEO of Yukos, Mikhail Khodorkovsky, was jailed for alleged tax crimes. The subsequent partial dismantling of Yukos meant that several employees transferred from Yukos to the new TNK-BP JV providing a good source of comparative data.

The interviews were conducted in Russian or English, according to respondent wishes, and lasted around one hour. They took place mainly in Moscow but also in the regions (for example Siberia for oil production and European Russia for oil refining). Respondents were encouraged to talk freely about organisational change and were assured of anonymity in writing up the results. The interviews were taped and transcribed. Representative quotations are given in the text, with anonymised references to the respondents provided in brackets, as well as an indication as to whether the text was translated or not (trans) and whether the interview took place in the regions or not. More information on the research methodology and data analysis is provided in the Appendix.

A THEORY OF ORGANISATIONAL TRANSFORMATION

On the basis of the above research I developed an integrative theoretical framework of organisational transformation, that captures the complexity of organisational transformation processes in transition economies. The framework demonstrates the influence of the institutional context and the administrative heritage, illustrates the varying roles of management practices, and explains how their impact changes over time, in a three stage process. I contribute to organisational learning and dynamic capabilities theory by explaining the linkages first between exploitation learning and the deployment function of dynamic capabilities, generating the operational capabilities required for short-term survival in a market economy, and second between exploration learning and the search and selection function of dynamic capabilities, generating the strategic flexibility required for sustainable competitive advantage in an unstable institutional environment. A top-down management style may provide the initial impetus for short term survival, but at later stages of transformation an empowering approach appears more likely to secure sustainable competitive advantage.

The main theoretical perspective is the resource-based view, however it is supplemented with key insights from organisational learning, dynamic capability, organisational change, top management team (TMT), leadership and institutional theory to form an integrative framework for organisational

transformation. Key concepts in the theoretical framework thus are the TMT, administrative heritage, institutional embeddedness, absorptive capacity, organisational learning, operational and dynamic capabilities and strategic flexibility. Their role and relationships evolve over the stages of organisational transformation.

This integrative framework addresses one of the current challenges of strategic management research: how to develop a theory of strategic management that reduces fragmentation and synthesises different views (Elfring and Volberda, 2001; Schoemaker, 2001; Hambrick, 2004). It integrates a range of theories to gain a fuller appreciation of the complexity of the processes. Furthermore three stages of transformation are identified, each with distinct change dynamics, thereby contributing to the organisational change literature by adopting a processual theory of change (Pettigrew, 1997) and explaining the temporal and organisational processes by which change unfolds (Greenwood and Hinings, 2006).

STRUCTURE OF THE BOOK

Chapter 2 describes the external (macro-environmental and industry) and internal (administrative and cultural heritage) context for the Russian oil companies. Primary and secondary data are interwoven with the literature to provide a rich description.

Chapter 3 presents an integrative theoretical framework to explain a three-stage process of organisational transformation in firms in transition economies. This framework was developed as a result of iteration between the literature and the empirical research.

Chapters 4–6 present stories of organisational transformation as individual case studies for the Western-style companies Yukos and TNK-BP and as a combined case study for the Soviet-style companies Lukoil and Surgutneftegaz.

Chapters 7–9 split the integrative framework for organisational transformation into three sections and demonstrate the empirical underpinning for the model. Chapter 7 explains the relationship between leadership, administrative heritage and absorptive capacity. Chapter 8 focuses on the links between different types of organisational learning and the development of operational capabilities and strategic flexibility. Chapter 9 explains the interrelationship of organisational learning and dynamic capabilities. Each chapter includes detailed time-ordered and conceptually ordered cross-case data displays to explain the process of organisational transformation and to draw out the key similarities and differences between the four companies.

Chapter 10 provides the overall conclusions and explains the implications for theory and practice. A postscript is added to put the study into the context of developments in the Russian oil industry since the research was completed in 2005.