

Return, Solvency and Capital Structure of Russian Public and Nonpublic Companies



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Abstract: *An analysis of differences in the capital structure and yield of public and nonpublic Russian companies is presented in the article, along with an analysis of the effect of corporate finance concepts – namely, of the capital structure and the relationship between risk and yield in the Russian reality. The concept of the interrelation of risk and yield is widely used in the Russian practice of valuation of business and investment decisions by using CAPM (Capital Assets Pricing Model) to find the value of the discount rate. How customary for the Russian reality is the understanding of the need to account for additional risks for nonpublic companies compared to public ones, common in the theory of corporate finance? This and some other questions are answered in this article. The results of the study have practical significance for investors interested in acquiring Russian assets.*

Index Terms: *business value, capital structure, corporate finance, organizational and legal forms of organization, public and nonpublic companies, return on assets, return on equity, return on sales, risk, solvency, yield.*

I. INTRODUCTION

Analysis of the effect of such corporate finance concepts as the capital structure concept and the relationship between risk and yield is widely described in the literature [1]-[3].

The problem of forming premiums for risk in determining the cost of capital is described in the literature in detail [4], [5], but only Shannon P. Pratt [4] explored the problem of the difference between unsystematic risk for public and nonpublic companies in the CAPM model. At the same time, studies of the valuation of the cost of capital for equity and risk premiums formation are actively conducted [6], [7].

These have been attempts to analyze the capital structure not only for public companies [8], but no such studies have been conducted for Russian companies in the context of various organizational and legal forms.

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A comparative analysis of indicators of return on equity, assets and sales, as well as the current liquidity and autonomy ratio (share of equity in the grand total) for 2009 – 2017 is provided in the article in the context of the three most common organizational and legal forms of companies in Russia: public and nonpublic joint-stock companies and limited liability companies. The analysis covers three sectors: processing industry, construction, and transport and communications (storage). The peculiarities of the sector-specific mechanism of company financing are also noted by other authors [9], but no such analysis has been conducted in the context of organizational and legal forms.

The relationship between risk and yield of Russian companies in the context of organizational and legal forms for several sectors has been confirmed as a result of the study, and the possibility of applying premiums for the risk of investing in nonpublic companies compared to public ones has been revealed.

II. METHODS

Theoretical and methodological basis of the article. The authors relied on academic papers and applied developments of Russian and foreign scientists and practitioners on the problems in the field of corporate finance in terms of the analysis of yield and risk and capital structure of public and nonpublic companies. The dialectical method of knowledge and the systematic approach to the problem are used in the article; general scientific and special research methods are applied: analysis (in particular, economic analysis and comparative analysis), synthesis, analogy, classification, as well as tabular and graphic methods. Papers of Russian and foreign scientists in the field of corporate finance are the information base of the work. Data from the official websites of research agencies and other organizations are used in the article. The study was carried out based on the data from the comprehensive information disclosure system NAUFOR on issuers SKRIN [10] for several thousand Russian public and nonpublic companies for 2009 – 2017, using Excel application tools.

III. RESULTS

A. Analysis of return on equity, assets and sales of public and nonpublic companies by sectors

Two types of cash flow are known in the formation of business value using the discounted cash flow method:



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free cash flow to equity (FCFE) and free cash flows to firm (FCFF) [5]. At the same time, the discount rate for the corresponding cash flow is found in different ways, since the result of the rate calculation should correspond to the level of the owner's yield in case of choosing the FCFE or to the level of yield for all investors in case of opting for the FCFF [11].

The actual value of the owners' yield indirectly indicates the rate of return on equity, and the value of the investors' yield indicates the rate of return on assets.

The authors found the return on equity, return on assets and return on sales for 2009 – 2017 for three sectors in this study: processing industry, construction, and transport and communications (storage), in the context of such

organizational and legal forms of companies as public and nonpublic joint stock companies and limited liability companies.

The results of analyzing the indicators of return on equity, assets and sales for 2009 – 2011 were published earlier [12]. They revealed that the use of the premium for a risk of investing in nonpublic companies compared to public ones was justified for Russian organizations in those periods (Table I). Has this trend been preserved in the current situation?

Table I. Comparative analysis of indicators of return for various organizational and legal forms by sectors for 2009 – 2011

Sector	Form	Number of companies	Return on assets			Return on equity			Return on sales		
			2009	2010	2011	2009	2010	2011	2009	2010	2011
Processing industry	JSC	4,498	0.029	0.024	0.007	0.105	0.094	0.071	0.011	0.003	0.020
	CJSC	905	0.045	0.038	0.018	0.164	0.092	0.242	0.018	0.009	-0.031
	LLC	564	0.047	0.066	0.064	0.282	0.277	0.255	0.012	0.036	0.025
Construction	JSC	5,602	0.021	0.012	-0.008	0.093	0.083	0.085	-0.040	-0.059	-0.083
	CJSC	9,537	0.023	0.042	0.022	0.215	0.206	0.173	-0.006	-0.013	-0.026
	LLC	10,000	0.010	0.057	0.046	0.230	0.157	0.173	0.015	0.013	0.008
Transport and communications	JSC	70,40	0.015	0.010	-0.007	0.079	0.073	0.070	-0.052	-0.063	-0.082
	CJSC	9,415	0.028	0.048	0.030	0.216	0.199	0.185	-0.010	-0.007	-0.023
	LLC	10,000	0.039	0.054	0.042	0.334	0.302	0.280	0.011	0.011	-0.002

The calculations of the authors made at a later date confirm this conclusion (Table II).

All types of return had increased in all periods in 2009 – 2011 and in all sectors for limited liability companies (hereinafter LLC) better than the return for closed joint-stock

companies (hereinafter CJSC), while CJSC companies, in turn, had seen a better growth in all types of return than open joint-stock companies (hereinafter JSC) (Tables II and III), but the situation changed in 2012 – 2017.

Table II. Comparative analysis of indicators of return on assets and equity for various organizational and legal forms by sectors in 2012 – 2017

Sector	Form ¹	Return on assets						Return on equity					
		2012	2013	2014	2015	2016	2017	2012	2013	2014	2015	2016	2017
Processing industry	JSC/PJSC	0.06	0.03	0.02	0.06	0.06	0.06	0.10	0.03	0.05	0.12	0.15	0.12
	CJSC/JSC	0.12	0.04	0.05	0.09	0.09	0.07	0.23	0.15	0.20	0.20	0.16	0.13
	LLC	0.01	-0.01	0.01	0.05	0.09	0.08	0.19	0.33	0.37	0.35	0.34	0.24
Construction	JSC/PJSC	0.01	0.02	-0.01	-0.03	-0.01	-0.01	0.11	0.11	0.11	0.08	0.10	0.10
	CJSC/JSC	0.04	0.03	0.02	-0.03	0.01	0.01	0.24	0.25	0.22	0.18	0.15	0.17
	LLC	0.02	-0.01	-0.01	0.02	0.03	0.03	0.24	0.46	0.49	0.21	0.33	0.34
Transport and communications	JSC/PJSC	0.03	0.03	0.05	0.06	0.08	0.04	0.14	0.14	0.13	0.12	0.20	0.14
	CJSC/JSC	0.14	0.09	0.06	0.10	0.18	0.14	0.21	0.14	0.18	0.22	0.26	0.22
	LLC	0.05	0.05	0.04	0.07	0.08	0.08	0.29	0.51	0.55	0.51	0.37	0.32

Table III. Comparative analysis of return on equity for various organizational and legal forms by sectors in 2012 – 2017.

Sector	Form	Return on sales					
		2012	2013	2014	2015	2016	2017
Processing industry	JSC/PJSC	0.11	0.05	0.06	0.08	0.09	0.10
	CJSC/JSC	0.14	0.12	0.13	0.16	0.12	0.11

Sector	Form	Return on sales					
		2012	2013	2014	2015	2016	2017
Construction	LLC	-0.04	0.02	0.04	0.03	0.05	0.07
	JSC/PJSC	0.02	0.04	0.01	-0.01	0.01	0.03
	CJSC/JSC	0.07	0.06	0.06	0.07	0.06	0.05
	LLC	0.01	0.01	-0.01	0.06	0.05	0.01
Transport and communications	JSC/PJSC	0.05	0.05	0.05	0.09	0.08	0.08
	CJSC/JSC	0.14	0.14	0.13	0.20	0.21	0.18
	LLC	0.01	0.01	0.04	0.05	0.03	0.09

All types of return in all analyzed periods and sectors were still higher for nonpublic JSCs than for PJSCs (Tables II-V, Figs. 1-6), but LLCs saw better return than nonpublic JSCs in

all sectors only for return on equity, while this trend was not observed for the other two indicators of return.

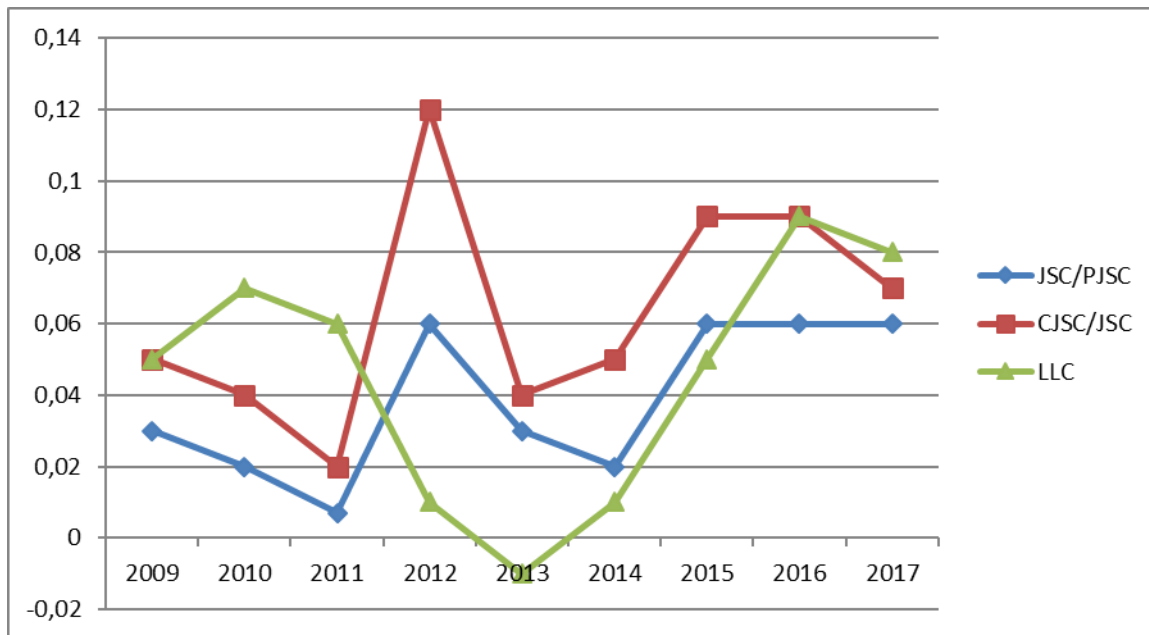


Fig. 1. Dynamics of return on assets for various organizational and legal forms for Processing industry



Fig. 2. Dynamics of return on assets for various organizational and legal forms for Construction

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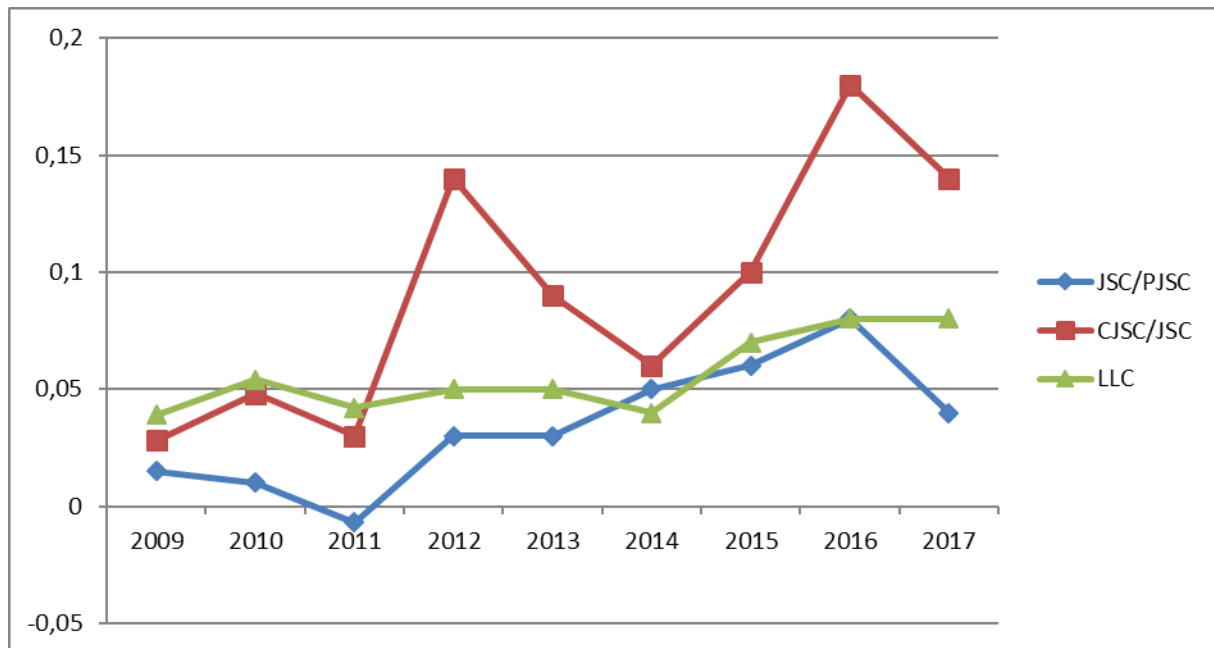


Fig. 3. Dynamics of return on assets for various organizational and legal forms for Transport and communications (storage)

In most cases, return on assets for LLCs is higher than this indicator of return for PJSCs but not for nonpublic JSCs. As for return on sales, LLCs have the lowest indicators in all periods and sectors in comparison with other organizational and legal forms.

It is shown on Figs. 1-3 that the return on assets for nonpublic JSCs in all sectors is higher than that of PJSCs. The

return on assets for LLCs in Processing industry and Construction for the majority of the analyzed periods is higher than that of public and nonpublic JSCs. At the same time, the dynamics of return on assets of public and nonpublic JSCs are unidirectional, and their trends coincide, but the dynamics of LLCs differ significantly and are described by significant volatility.

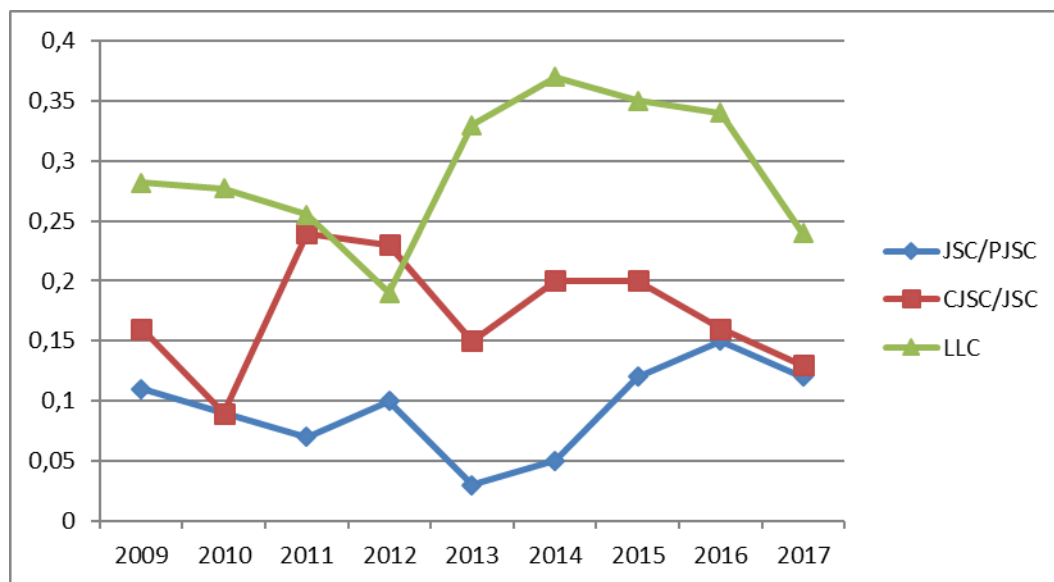


Fig. 4. Dynamics of return on equity for various organizational and legal forms for Processing industry

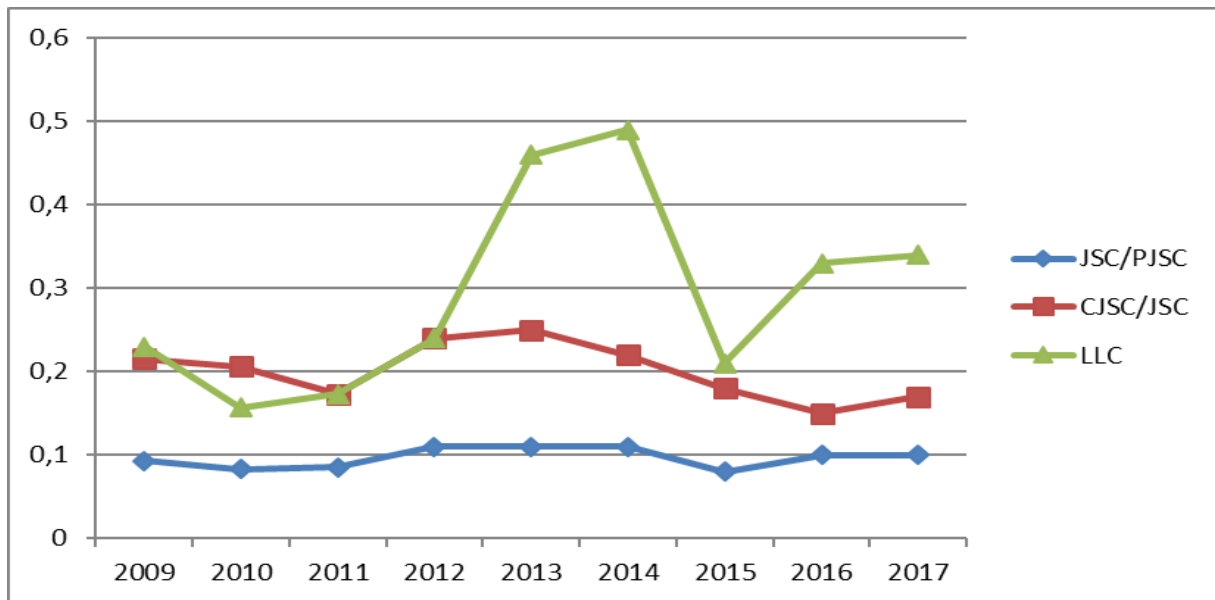


Fig. 5. Dynamics of return on equity for various organizational and legal forms for Construction

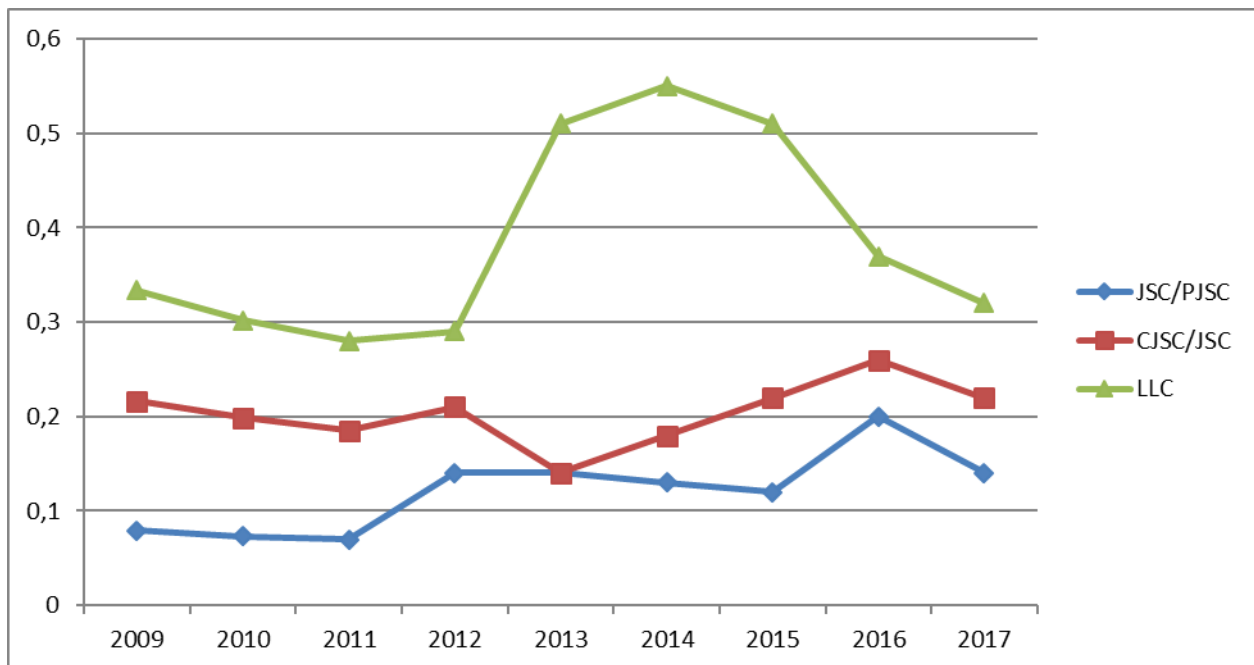


Fig. 6. Dynamics of return on equity for various organizational and legal forms for Transport and communications (storage)

The indicators of return on equity are "calmer" in all sectors and are quite stable for public and nonpublic JSCs (Figs. 4-6), while return on equity for LLCs is more volatile than that for JSCs. At the same time, it is clearly seen that return on equity for nonpublic companies is higher than for public ones in all periods and for all analyzed sectors.

The average deviation of return on assets in 2009 – 2011 by sectors was 1.4 % to 2.9 % between JSCs and CJSCs depending on the sector, 1 % to 2.5 % between LLCs and CJSCs, and 3.9 % to 5 % between LLCs and JSCs. The average deviation of the return on equity had more significant value and variation: 7.6 % to 12.6 % between JSCs and

CJSCs, 1.1 % to 10.5 % between LLCs and CJSCs, and 18.1 % to 23.1 % between LLCs and JSCs.

The average deviation of return on assets in 2012 – 2017 by sectors (Tables IV and V) between PJSCs and JSCs was 3 % to 7 %, while the deviation of return on equity for the same legal forms was 6 % to 10 %. The average deviation of return on assets was from minus 6 % to 0 % between LLCs and JSCs, and from minus 1 % to 2 % between LLC and PJSC. The average deviation of return on equity was 13 % to 22 % between LLCs and JSCs, and 21 % to 28 % between LLC and PJSC.

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Table IV. Analysis of deviations of return on assets and equity for various organizational and legal forms by sectors in 2012 – 2017

Sector	Form	Return on assets							Return on equity						
		2012	2013	2014	2015	2016	2017	average	2012	2013	2014	2015	2016	2017	average
Processing industry	PJSC	0.06	0.03	0.02	0.06	0.06	0.06	0.05	0.1	0.03	0.05	0.12	0.15	0.12	0.10
	JSC	0.12	0.04	0.05	0.09	0.09	0.07	0.08	0.23	0.15	0.2	0.2	0.16	0.13	0.18
	deviation	0.06	0.01	0.03	0.03	0.03	0.01	0.03	0.13	0.12	0.15	0.08	0.01	0.01	0.08
	LLC	0.01	-0.01	0.01	0.05	0.09	0.08	0.04	0.19	0.33	0.37	0.35	0.34	0.24	0.30
	deviation between LLCs and JSCs	-0.11	-0.05	-0.04	-0.04	0	0.01	-0.04	-0.04	0.18	0.17	0.15	0.18	0.11	0.13
	deviation between LLCs and PJSCs	-0.05	-0.04	-0.01	-0.01	0.03	0.02	-0.01	0.09	0.3	0.32	0.23	0.19	0.12	0.21
Construction	PJSC	0.01	0.02	-0.01	-0.03	-0.01	-0.01	-0.01	0.11	0.11	0.11	0.08	0.1	0.1	0.10
	JSC	0.04	0.03	0.02	-0.03	0.01	0.01	0.01	0.24	0.25	0.22	0.18	0.15	0.17	0.20
	deviation	0.03	0.01	0.03	0	0.02	0.02	0.02	0.13	0.14	0.11	0.1	0.05	0.07	0.10
	LLC	0.02	-0.01	-0.01	0.02	0.03	0.03	0.01	0.24	0.46	0.49	0.21	0.33	0.34	0.35
	deviation between LLCs and JSCs	-0.02	-0.04	-0.03	0.05	0.02	0.02	0.00	0	0.21	0.27	0.03	0.18	0.17	0.14
	deviation between LLCs and PJSCs	0.01	-0.03	0	0.05	0.04	0.04	0.02	0.13	0.35	0.38	0.13	0.23	0.24	0.24
Transport and communications	PJSC	0.03	0.03	0.05	0.06	0.08	0.04	0.05	0.14	0.14	0.13	0.12	0.2	0.14	0.15
	JSC	0.14	0.09	0.06	0.1	0.18	0.14	0.12	0.21	0.14	0.18	0.22	0.26	0.22	0.21
	deviation	0.11	0.06	0.01	0.04	0.1	0.1	0.07	0.07	0	0.05	0.1	0.06	0.08	0.06
	LLC	0.05	0.05	0.04	0.07	0.08	0.08	0.06	0.29	0.51	0.55	0.51	0.37	0.32	0.43
	deviation between LLCs and JSCs	-0.09	-0.04	-0.02	-0.03	-0.1	-0.06	-0.06	0.08	0.37	0.37	0.29	0.11	0.1	0.22
	deviation between LLCs and PJSCs	0.02	0.02	-0.01	0.01	0	0.04	0.01	0.15	0.37	0.42	0.39	0.17	0.18	0.28

Table V. Analysis of deviations in return on sales for various legal forms by sectors in 2012 – 2017

Sector	Form	Return on sales						
		2012	2013	2014	2015	2016	2017	average
Processing industry	PJSC	0.11	0.05	0.06	0.08	0.09	0.1	0.08
	JSC	0.14	0.12	0.13	0.16	0.12	0.11	0.13
	deviation	0.03	0.07	0.07	0.08	0.03	0.01	0.05
	LLC	-0.04	0.02	0.04	0.03	0.05	0.07	0.03
	deviation between LLCs and JSCs	-0.18	-0.1	-0.09	-0.13	-0.07	-0.04	-0.10
	deviation between LLCs and PJSCs	-0.15	-0.03	-0.02	-0.05	-0.04	-0.03	-0.05
Construction	PJSC	0.02	0.04	0.01	-0.01	0.01	0.03	0.02
	JSC	0.07	0.06	0.06	0.07	0.06	0.05	0.06
	deviation	0.05	0.02	0.05	0.08	0.05	0.02	0.05
	LLC	0.01	0.01	-0.01	0.06	0.05	0.01	0.02
	deviation between LLCs and JSCs	-0.06	-0.05	-0.07	-0.01	-0.01	-0.04	-0.04
	deviation between LLCs and PJSCs	-0.01	-0.03	-0.02	0.07	0.04	-0.02	0.01
Transport and communications	PJSC	0.05	0.05	0.05	0.09	0.08	0.08	0.07
	JSC	0.14	0.14	0.13	0.2	0.21	0.18	0.17
	deviation	0.09	0.09	0.08	0.11	0.13	0.1	0.10
	LLC	0.01	0.01	0.04	0.05	0.03	0.09	0.04
	deviation between LLCs and JSCs	-0.13	-0.13	-0.09	-0.15	-0.18	-0.09	-0.13
	deviation between LLCs and PJSCs	-0.04	-0.04	-0.01	-0.04	-0.05	0.01	-0.03

The average deviation of return on sales by sectors is 5 % to 10 % between PJSCs and JSCs, from minus 4 % to minus 13 % between LLCs and JSCs, and from minus 5 % to 1 % between LLCs and PJSCs.

In other words, the magnitude of deviations in 2012 – 2017 became more significant than in 2009 – 2011, which indicates an increase in the size of risk premiums for nonpublic companies in recent years in comparison with public ones, as well as their high volatility. Negative risk premiums were observed in some cases.

At the same time, the presented deviation values can be used as additional risk premiums when the discount rate for nonpublic companies is formed.

B. References

The indicator describing the capital structure in this study is the autonomy ratio (ratio of equity to the grand total). The results of the analysis of this indicator are presented in Tables VI and VII.

Table VI. Comparative analysis of current liquidity and autonomy ratios for various organizational and legal forms by sectors in 2009 – 2011

Sector	Form	Number of companies	Current liquidity ratio				Autonomy ratio			
			2009	2010	2011	average	2009	2010	2011	average
Processing industry	JSC	4,498	2.46	2.43	2.33	2.40	0.407	0.377	0.330	0.37
	CJSC	905	2.65	2.79	2.98	2.81	0.327	0.328	0.219	0.29
	LLC	564	2.60	2.73	2.71	2.68	0.365	0.342	0.350	0.35
Construction	JSC	5,602	2.27	2.34	2.14	2.25	0.376	0.485	0.451	0.44

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Sector	Form	Number of companies	Current liquidity ratio				Autonomy ratio			
			2009	2010	2011	average	2009	2010	2011	average
	CJSC	9,537	2.01	2.21	2.21	2.14	0.252	0.250	0.247	0.25
	LLC	10,000	1.81	1.80	1.78	1.80	0.353	0.397	0.394	0.38
Transport and communications	JSC	7,040	2.42	2.69	2.40	2.50	0.441	0.553	0.517	0.50
	CJSC	9,415	3.23	3.02	2.99	3.08	0.265	0.269	0.259	0.26
	LLC	10,000	3.15	3.13	3.06	3.12	0.239	0.273	0.255	0.26

The share of equity for public and nonpublic JSCs for Processing industry did not change significantly throughout the analyzed period, but such stability is not observed for other sectors and organizational and legal forms (Figs. 7-9).

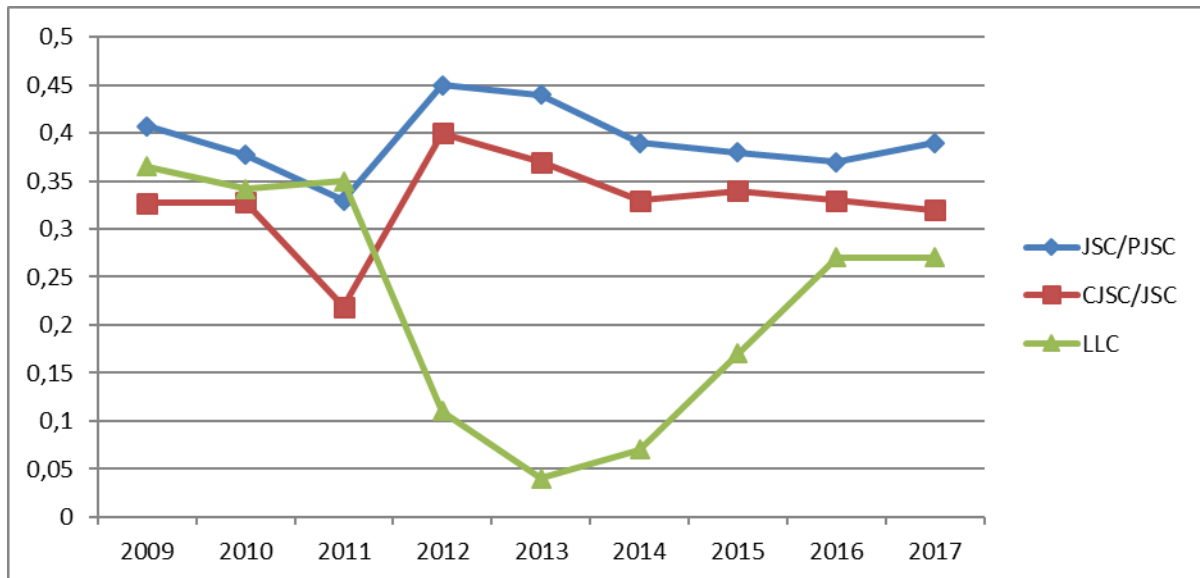


Fig. 7. Dynamics of autonomy ratio for various organizational and legal forms for Processing industry

Table VII. Comparative analysis of current liquidity and autonomy ratios for various organizational and legal forms by sectors in 2012 – 2017

Sector	Form	Current liquidity ratio							Autonomy ratio						
		2012	2013	2014	2015	2016	2017	average	2012	2013	2014	2015	2016	2017	average
Processing industry	JSC/PJSC	2.05	2.09	2.35	2.03	1.99	2.00	2.09	0.45	0.44	0.39	0.38	0.37	0.39	0.40
	CJSC/JSC	2.22	2.6	2.13	2.54	2.01	2.04	2.26	0.40	0.37	0.33	0.34	0.33	0.32	0.35
	LLC	2.04	1.42	1.32	1.57	1.72	2.02	1.68	0.11	0.04	0.07	0.17	0.27	0.27	0.16
Construction	JSC/PJSC	1.62	1.68	1.65	1.63	1.79	2.06	1.74	0.23	0.23	0.19	0.21	0.28	0.25	0.23
	CJSC/JSC	1.56	1.43	1.88	2.01	1.66	1.52	1.68	0.16	0.16	0.16	0.04	0.15	0.14	0.14
	LLC	1.43	1.09	1.17	1.25	1.64	1.27	1.31	0.14	0.02	0.03	0.07	0.12	0.14	0.09
Transport and communications	JSC/PJSC	2.19	1.72	2.02	2.07	2.00	2.37	2.06	0.37	0.34	0.37	0.37	0.43	0.49	0.40
	CJSC/JSC	2.46	2.21	2.46	2.29	2.37	2.41	2.37	0.49	0.49	0.44	0.43	0.44	0.46	0.46
	LLC	1.71	1.61	1.25	1.26	1.61	1.77	1.54	0.28	0.14	0.13	0.14	0.22	0.25	0.19

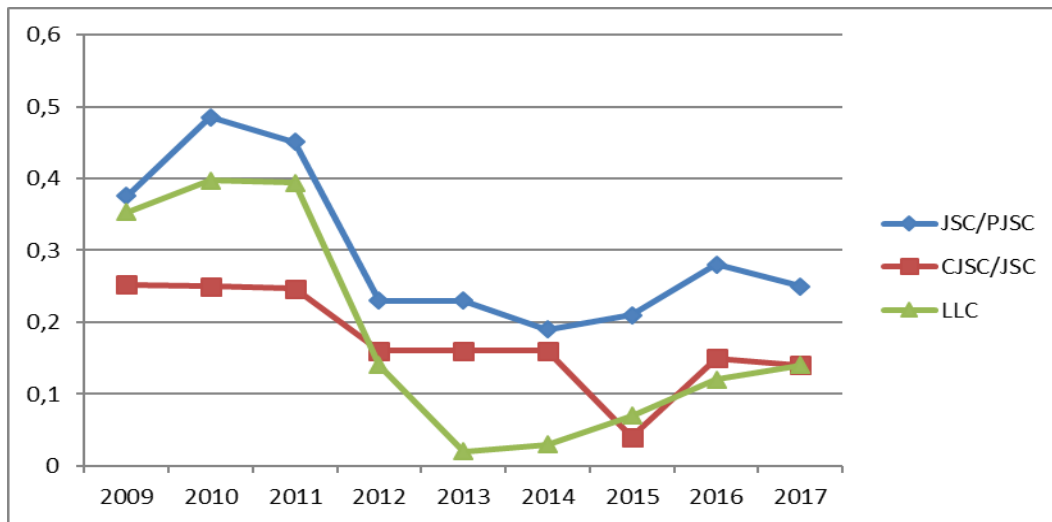


Fig. 8. Dynamics of autonomy ratio for various organizational and legal forms for Construction

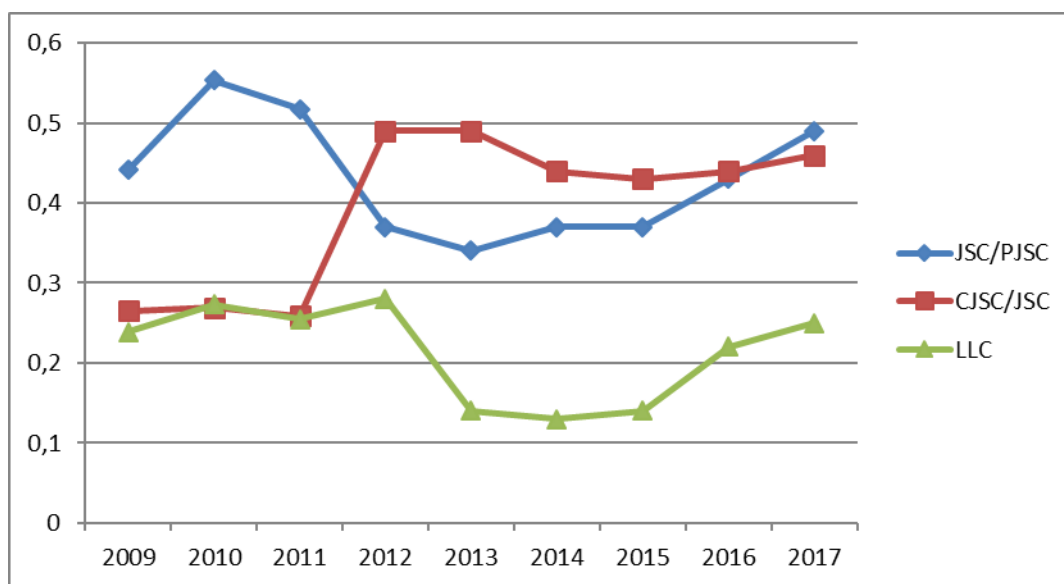


Fig. 9. Dynamics of autonomy ratio for various organizational and legal forms for Transport and communications (storage)

The indicators from Tables IV and V describing the autonomy ratio and Figs. 7-9 indicate the presence of the highest equity ratio for PJSCs compared to nonpublic JSCs and LLCs for almost all analyzed sectors (the only surge in the equity ratio for nonpublic JSCs compared to PJSCs is observed in certain periods in Transport and communications (storage) (Fig. 9)), while the equity ratio for LLCs for most periods and all sectors is lower than that of public and nonpublic JSCs.

At this stage, it becomes clear that return on equity for LLCs is higher than return on equity for public and nonpublic JSCs. However, this conclusion is not so obvious for 2009 – 2011, because the equity ratio in this period for all sectors is higher for LLCs than for nonpublic JSCs, although the return is higher for LLCs.

Besides, following the results of the analysis of Figs. 7-9, it can be argued that the equity ratio in Processing industry throughout the analyzed period is quite stable for public and nonpublic JSCs. This ratio for LLCs had declined significantly in 2012 – 2015 but returned to the level of 2009 – 2011 in 2016 and 2017.

A downward trend in the equity ratio with a slight increase in 2016 is observed in Construction throughout the entire analyzed period. The equity ratio in Transport and communications (storage) decreased for PJSCs and LLCs in 2012 – 2014 but grew for nonpublic JSCs in these periods. The equity share then grew in 2015 – 2017 and returned to the positions of 2009 – 2011.

The above trends indicate an obvious relationship between the capital structure and the return on equity for companies of various organizational and legal forms in various sectors.

C. Comparative analysis of return and solvency of public and nonpublic companies by sectors

The current liquidity ratio (ratio of current assets to current liabilities) is used in this study as an indicator describing solvency of organizations.

The data from Tables VI and VII indicate a downward trend in the solvency of organizations of various organizational and legal forms in all analyzed sectors. An increase is observed for some indicators in 2017.

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It is known that liquidity and profitability are also inversely related to each other (Kovalev, 2000), which the results of this study actually confirm.

The dynamics of the current liquidity ratio indicate that its value depends on the organizational and legal form of the company and the sector it belongs to. Its value was lower for LLCs in comparison with public and nonpublic JSCs in 2012 – 2017. At the same time, there was a higher ratio value for nonpublic JSCs compared to PJSCs for Processing industry and Transport and communications (storage).

IV. DISCUSSION

It can be summarized that the provisions of the theory of corporate finance are quite acceptable for the Russian economy in terms of the concepts of the relationship between risk, return, and capital structure. The multidirectional movement of liquidity and return indicators is confirmed.

It can also be noted that almost the entire analysis indicates a significant instability in the performance of LLCs throughout the analyzed period, which indicates the high riskiness of investing in such companies and also their higher return. From the standpoint of the ratio of return to riskiness of investing funds, as well as solvency, nonpublic JSCs are more attractive in Processing industry and Transport and communications (storage).

V. CONCLUSION

As such, it can be stated that this study confirms the possibility of implementing individual theories and models of corporate finance in the context of the modern Russian economy. A connection between the capital structure of Russian companies and their return is observed, which confirms the higher risk and return for nonpublic companies compared to public ones.

The results of the calculations of the return indicators and capital structure conducted in 2009 – 2017 for samples of organizations in various sectors and organizational and legal forms prove the differences in the level of risk and return.

The use of risk premiums for investing in nonpublic companies compared to public ones is fully justified for the Russian economy. The premium size depends on the organizational and legal form of the company and its sector.

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