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## **Governments and Companies in the Post-Soviet World: Power, Intentions, and Institutional Consistency**

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### **1. Introduction**

The role of private and semi-private business groups as a driving force for the transformation of economic and political institutions is a topic long debated in economics and political science in general, but also in case of the post-Soviet transitions. On the one hand, private business is (at least, potentially) a significant interest group able to shape the political decisions and to determine how the institutions of a country evolve. The importance of business interests as a factor of political and economic transition is not natural: the difference between business power and political power could be negligible in terms of economic outcomes if there are no costs of corruption and subsidies (Shleifer and Vishny 1994) or, more generally, one can assume a “political Coase theorem” stating independence between political institutions and economic performance (Acemoglu 2003; Parisi 2003). However, in a world where corruption is costly and transaction costs are present, allocation of power is likely to matter.

On the other hand, the interests of the private business are not entirely clear and often subject to debate. It is also possible that the impact of business interests is not determined by the intentional and conscious planning, but it rather, following the ideas of Hayekian economics, a collection of “unintended consequences of intended action”. Finally, the government-business relations models are based on a system of institutions of their own, which therefore should be considered from the point of view of its interrelation with other institutions governing the interactions in a particular society, and thus fall in the domain of the debate on “institutional consistency” or “institutional complementarities”. Therefore, although the importance of the factor of the government-business relations is hardly in dispute, the multitude of potential influence factors and forces makes it a difficult field of the analysis.

This paper aims to provide a systematic overview of the possible channels of influence of the government-business relations models on the emergence of economic and political institutions in the post-Soviet countries, using this framework as the basis for the comparative analysis of the countries of the Former Soviet Union (FSU). I will specifically consider three potential channels of influence: asymmetry of power, unintended consequences of conflicts and institutional (in)congruence and derive a set of hypotheses from each of them (although the latter will be treated in less detail).

Then I will proceed by discussing the evolution of the government-business relations in the FSU countries. The paper looks at four countries of the region. Three of them (Russia, Ukraine and

Kazakhstan) seem to be a relatively standard choice for this sort of empirical analysis given their size and importance in the region, as well availability of data. It should also be noted that these countries often serve as “best practice” cases for other governments of the FSU: it is particularly clear for Russia (given the structure of the traditional ties), but also recently for Kazakhstan (for example, due to the liberal reforms implemented by this country in the early 2000s, which were enthusiastically perceived even in Russia) and Ukraine (for example, given the experience of the “orange revolution” of 2004, which constituted a major shift of power in the FSU regimes). In addition, I look at Uzbekistan as an example of a country without consequent market reforms (similar to Belarus and Turkmenistan) to understand the role of government-business relations in this particular case.

## 2. Government-business Relations and Institutions: Three Channels of Influence

As already noticed, this paper proceeds from the assumption that there are three aspects of the government-business relations to be worth considering in the context of the FSU. Basically, the models of government-business relations include two main components: first, the *formal rules* governing the degree of public intervention in the economic decisions of enterprises (both privatized and state-owned), and second, the *informal interdependence* between political, bureaucratic and business groups. Hence, there are two distinct analytical perspectives, which could be applied.

First, one can focus on the *content* of the government-business relations, considering both formal and informal components “as a whole”. From this point of view formal and informal aspects of government-business relations models can be more or less important, and hence, deserve more or less consideration in the analysis. This perspective, however, includes two distinct analytical approaches. On the one hand, there is the ability of powerful actors to shift policies (and also, given the still instable legal order of post-Soviet countries, formal norms) in their favor.<sup>1</sup> However, institutions and policies often originate not only from intended design by the government, but also as a by-product of power struggles. The original concept of institutions as “unintended results of intended action” can be traced back to Scottish moral philosophy and was extensively developed by the Hayekian school in economics.<sup>2</sup>

Second, however, one can specifically look at the *contradictions* between formal and informal institutions as a source of incentives of public officials and businesses. This approach can also cover the contradictions between the institutional framework of the government-business relation models and other domains of social, economic and political interaction. In this case the more general problem of institutional complementarities between the government-business relations models and other aspects of formal and informal regulation becomes relevant. Actually, in the second case one applies a conceptual framework similar to that of the Varieties of Capitalism (Hall and Soskice 2001), although one should not necessarily accept the perspective of equally good performance of all combinations of institutions characterized by complementarity.<sup>3</sup>

### 2.1. Relative Power: Business as the Dominant Actor

The first (and the most intuitive) perspective suggests that the design of political and economic institutions depends upon the will of the incumbent actor. The direction of influence is

<sup>1</sup> This is for example the core of what one may call “neorealist” approach to institutional change (Amable and Palombarini 2009).

<sup>2</sup> This problem also is discussed by Knight (1992): he considers societies, where shifts in technology or resources lead to conflicts of social actors over power, and shows, that the institutions appear unintentionally as a consequence of these distributional conflicts.

<sup>3</sup> For the FSU countries similar attempts are sometimes made by the opponents of liberal market reforms (Кирдина 2004), although the empirical justification of this claim is weak. However, an alternative point of view suggests that the set of stable institutional equilibria also includes more and less efficient ones (North, Wallis and Weingast 2006). The approach of this paper allows me to differentiate between the costs and benefits of the specifics of interaction in a particular equilibrium and the costs of being “out of equilibrium” by looking at the perspectives of the content and the consistency of institutions outlined above.

determined by the motivation of the actors. Hence, in this case the main objective is to find out the relatively more powerful agent (the government or the business) and then consider their objectives in the negotiations. It is clear that using the words “government” and “business” in this contexts is sloppy: it is possible the “business” side is represented just by a small group of powerful business groups (and, in fact, concentration of power by this actors could imply a limited ability of other businesses to access the political decision making) or by an organized lobby with well-structured business associations. For the FSU the more realistic option is the former one, which I will also use as the benchmark in the argumentation in this subsection. The “government” side is also associated with interests and positions of particular bureaucrats and politicians engaged in negotiations.<sup>4</sup>

As a starting point for the analysis, assume that the power is concentrated on the side of the private business groups. However, here one immediately faces the first large problem of the transition debate: the interests of the (large) business groups are not entirely clear. The dawn of the transition of the FSU was characterized by the discussions of the “spontaneous” emergence of the demand for property rights once the private companies achieve a certain level of maturity, following the prescriptions of the New Institutional Economics (North and Thomas 1973); therefore creating a large group of private owners was treated a main objective of economic transition. However, already in the mid-1990s it was clear that large business (with Russia being the most notable example) did not live up to the expectations. Similarly, the demand for “good” institutions was also limited on the side of the small and medium business. From the theoretical point of view the response to this situation was to show that under certain conditions (present in the FSU during the period) private companies are interested in *maintaining inefficient institutions* rather than supporting advancements of institutional reforms.<sup>5</sup>

Libman (2007) surveys three arguments in favor for demand for bad institutions: redistribution, deficit of vertical trust and learning costs. First, the use of inefficient rules can be relatively profitable for groups benefiting from redistribution, if the rents are higher, than the losses from transaction costs. Since normally these groups possess a lot of political power, they can effectively block any improvements of the quality of institutions. Specifically, the result can be related to the gains from partial reforms (Hellman 1998; Полтерович 1999; Hoff and Stiglitz 2008), benefits from private protection of property rights under strong concentration of assets as opposed to the public property rights protection (Sonin 2003; Polishchuk and Savvateev 2004) or adverse selection among successful businesses in presence of the lobbying option (Gaddy and Ickes 1999). Second, absence of trust prevents societies from finding out efficient institutions (including informal institutional alternatives to public institutions): Russia is among the societies with the lowest level of trust in the world. Specifically, if individuals have always suspected their government, any change of institutional environment is considered to be for the worse than the existing state, and the actors support present, and not better institutions, or consciously organize their activity through informal channels (to avoid government’s attention). Third, it is possible, that the sunk cost (i.e., learning costs, which can pay off only under a specific institutional environment) are higher, than the gains from better institutional environment, and individuals decide not to change the status quo, or, at least, not to invest in political activity to improve the situation.<sup>6</sup> For example, the result can follow from the experience of the institutional chaos of the early 1990s; the informal bargaining in the Soviet “administrative market” (Кордонский 2001), which formed the basis for the existing interest groups; misperceptions and misinterpretations can also play a role.<sup>7</sup>

<sup>4</sup> There is also a difficult question of the management of state-owned companies, where the clear border between a public agency (say, a ministry) and a business group is absent or sloppy; this issue will be of great relevance for the discussion to follow.

<sup>5</sup> It should be noted that the issue is not just the formal design of rules of the game in economies; there is a parallel problem of the “under-usage” of law, which can be caused by misinterpretations, alternative institutions and wrong expectations of market participants; this aspect is formulated in the market design literature and debated by Krug and Hendrichske (2010) with respect to China.

<sup>6</sup> In addition, it is possible to observe the effects of the cognitive dissonance: choices once made influence the preferences in their favor (e.g. Mullainathan and Washington 2009).

<sup>7</sup> For example, Furman (Фурман 1995) argues that the actions of companies and individuals in the 1990s were heavily influenced by the “cartoons” of the market economy created by the Soviet propaganda: the latter created a very consistent

The simple existence of demand for bad institutions in the early 1990s is hardly debated in the modern literature. Nevertheless, the account of possible changes of business preferences remains one of the key issues for transition studies. Havrylyshin (2007:17) refers to this discussion as “transition inevitable” and “transition frozen” school of thoughts and claims, that “the debate ... will certainly go on for some time to come”. Specifically, the transition to the demand for good institutions from the demand for bad institutions can be driven by a number of factors. Polishchuk (2002) and Runov (Пунов 2003) mention the adverse effects of redistribution struggles in case when “nothing is left to steal”, the need for investments in order to replace the amortisation of assets created in Soviet times, demand for transparent standards for corporate governance and concern over reputation on global markets. Internationalisation increases the business legitimacy, its independence from the government and its bargaining power in government-business relations, and makes transparency, better protection of property rights and clear rules of the game more attractive for business groups. In addition, the CIS countries start experiencing a “change of generations” in business management, when “founders” of corporations move to the pure shareholder position and delegate their authorities to managers, and are therefore interested in the protection of their property rights – a process, which, according to several reports, was reversed by the crisis of 2008-2009 (when the companies start cutting hired management and replacing them by shareholders in order to optimize the cost structure). Finally, demand for good institutions can follow from the learning effects, when the misperceptions and mistakes of the past gradually “wear off”.

Anyway, depending upon the choice of the “transition inevitable” or “transition frozen” approaches, two alternative hypotheses could be deduced. For the inevitable transition case, *improving the quality of institutions* is possible if business groups are powerful. Similar results, by the way, could be expected if the driving force of institutional transition is the powerful multinationals, which may be free from the demand for bad institutions bias. According to the second approach, since business still prefers bad institutions, *the main source of institutional innovations is the state* (i.e., political actors), which forces private businesses to accept new rules (if it is able to do so). In this case, however, political economics considerations should be taken into account, as it will be discussed in what follows. Finally, one should notice that the instability of the inefficient institutional equilibrium (either from the actions of the government or of the private business) does not automatically imply a transition to a better equilibrium. Kapelyushnikov (Капелюшников 2001) offers a perspective of the “steady state” transition when countries permanently shift from one instable and inefficient equilibrium to another: probably, the cycles of redistribution resulting into the economic decline of Argentina in turn of the last century could be interpreted as an example of this sequence.

## 2.2. Relative Power: Government as the Dominant Actor

Assuming that the government has the upper hand in negotiations, however, leads just to another dilemma, once again related to the preferences of the politicians and bureaucrats. In this case the problem is, however, more intuitive from the point of view of the standard economic analysis: Weingast (1993) describes it as a “fundamental political dilemma of an economic system”. On the one hand, the government should be strong enough to be able to implement economic reforms and sustain the dynamics of transformation, even if there is demand for inefficient institutions from private business (the “grabbing-hand” government, as in Frye and Shleifer 1997). On the other hand, the strong government is likely to exploit its position for redistribution and rent-seeking, thus preventing any institutional progress. In terms of the economic reforms the strong government can be also conceptualized as an “autonomous” government (although the strength is also related to its ability for enforcement and not just independence from potential interest groups with rent-seeking goals). The particular definition of autonomy is subject to debate: the older view focuses on the *independence* of government from the redistributive desires of interest groups, which makes it able to implement economic reforms (cf. the paper of Afontsev (Афонцев 2000) for the critique of this approach), while

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picture of the “capitalist” economies and “oligarchic” political systems, which has in fact been unconsciously copied by the post-Soviet entrepreneurs and politicians.

the more recent ideas focus on *impartiality* of the government in the long run (Rothstein and Teorell 2008).

Depending upon the assumptions on the preferences of bureaucrats and politicians, the absence of autonomy can lead to substantially different results. First, deficit of autonomy (specifically, understood as independence) makes further reforms very costly and dependent upon the coalition-formation, which can be expensive; thus it is possible that this government should end up in a reform blockade, for example, similar to that predicted by Fernandez and Rodrik (1991). Second, absence of autonomy influences the behavior of politicians. In the simplest possible situation they will just increase redistribution to get support of individual interest groups, what is most certainly likely to have a negative influence on the political transition. Things can, however, be more complicated: Radaev (Радаев 1998) and Darden (2008) describe a government which consciously designs the institutions in a way which makes business dependent upon the political support; McMann (2006) claims that this loss of “economic autonomy” through the “hostage taking” by the government can form a solid foundation of its power.<sup>8</sup> Thus, a non-autonomous government is also interested in maintaining inefficient institutions – as a tool of its power making it possible to control private actors.

In addition, even if the autonomous government acts as a rent-seeking Leviathan, increasing its independence can make it more forward-looking, and therefore support the “stationary bandit” logic described by McGuire and Olson (1996), i.e. existence of higher benefits from economic growth, than from more intensive redistribution. In this case the government rather reduces its “share of the pie” if the “size of the pie” goes up. However, as it has been shown by Shen (2007) and Chaturvedi and Muenster (2009), if the government is unsure of the future survival, this logic cannot work, since the “fruits” of the current pro-growth policies will be captured by other governments. There seems to be a clear analogy to the private business behavior: if it is unsure of the long-term stability of its claims on assets, asset stripping becomes the only viable option (see Braguinsky and Myerson (2007) for a related model).

So, once again, as in case of the business interests, we face a contradiction between two hypotheses based on the preferences of the government: it makes sense to restrict the ability of the “grabbing hand” government for the rent-seeking, but encourage autonomy of the “enlightened bureaucrats” willing to promote economic growth. A general problem, however, is as with case of business, that the preferences of agents are per definition not observable: one can attempt to deduce them from choices and claims made by actors, which, however, are not necessarily consistent or can be designed strategically for the purpose of misinformation. That is why an alternative approach described in what follows can be more interesting and requires serious consideration.

### 2.3. By-products of Power Struggles

The idea that the property rights can spontaneously emerge from anarchic environment has been one of the main subjects of the modern economics of conflict (e.g. Grossman 2001 or Hafer 2006) and, as already mentioned, could be traced back to the Hayekian ideas of spontaneous evolution (Beaulier and Prychitko 2006). As mentioned, from the empirical point of view it has one particular advantage: in order to explain institutional changes as by-products of power and distributional conflicts there is no need to introduce strong assumptions on the motivation of actors, like in the discussion above. In fact, one can even assume that both political and business actors are unwilling to support economic reforms, which, however, still take place as an “unintended result of intended action”. Since the preferences are never directly observable (and even revealed preferences based on observations of choices are difficult to deduce in intransparent political settings), the analysis of by-

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<sup>8</sup> Of course, creating inefficient institutions can also be a source of rents and be caused by the internal logic of the bureaucratic hierarchies. In the book of Paneyakh (Панеях 2008), which discusses the operation of small enterprises in Russia, the following example is debated: currently Russian small business specifically submits tax reporting including a limited number of mistakes, which they in fact (informally) indicate to the inspectors, so that the tax authorities can correct them. The benefit is for both parts: tax authorities report their successful fight against the tax evasion, and taxpayers are free from possible detailed monitoring of all accounts.

products of power struggles has clear benefits for research. Nevertheless, some conclusions can be made regarding the potential structure of government-business relations models.

The most evident factor able to influence the outcomes of state-business conflicts is the instruments of conflict used by different actors. Instruments used in state-business conflicts can be divided into two groups. First, actors apply “traditional” problem-solving instruments like internal negotiations, administrative measures and bargaining, borrowing them from the old Soviet “administrative market”. Second, “alternative” instruments include use of courts and legal procedures. The first group of instruments supports inefficient institutions, even if actors are trying to change it. The alternative instruments also provide no guarantee of changes, but at least open a window of opportunities for transition. The two major positive by-products of alternative instruments include: (1) actors get used to “new” instruments (thus their application reduces learning costs for better institutions and “demand for bad institutions”, and therefore creates new behavioral routines) and (2) permanent application increases the quality of “new” instruments through knowledge accumulation (e.g. legal procedures or parliamentary elections). “Alternative” instruments are risky (or, at least, are perceived as risky), and that is why it is possible to assume that only a powerful actor is ready to use alternative methods instead of traditional “hidden bargaining” instruments (see also Libman 2006). On the other hand, Schattenschneider (1960) argues, that the weaker party in political conflicts is more interested in attracting additional participants (or socializing the conflict), which is exactly the case when alternative instruments are applied.

However, involving new instruments can be costly from the point of view of the third perspective of the analysis, which is focusing on the consistency of institutions and will be discussed in what follows.

## 2.4. Consistency of Institutions

From the point of view of the consistency of formal and informal institutions, the government-business relations models can be described in terms similar to the concept *institutional complementarity*. The original notion of institutional complementarity in the comparative political economy, however, mostly refers to the combinations of different formal institutions governing different social arenas (say, labor market, firm hierarchy, educational system etc.). In case of informal institutions the situation is more difficult, because they usually “share” the arena with formal rules. Hence, consistency of institutions may imply that (1) institutions mutually reinforce each other in terms of incentives set for agents and informal institutions increase the strength of formal rules (defined in terms of enforcement and stability, cf. Levitsky and Murillo 2009), (2) formal and informal rules divide the domain of application in a form of a “division of labor among institutions” (Leipold 2006) in a way, which leads to their mutual survival (though it may, actually, imply incentives for *different* choices in similar situations on different arenas – Helmke and Levitsky (2004) refer to “accommodating” informal institutions); (3) there exists a division of labor among institutions over time: for example, in the period of weakening formal institutions informal rules ensure the “survival” of the conditions, resulting in the replication of old formal structures (Либман 2008) and (4) finally, the meaning of institutions is consistent with the “labels” used to describe them – otherwise institutions emerge, which resemble the “efficient” rules for markets and policies, but in fact rather undermine the institutional transformation than support it (Евстигнеев 1997; Гельман 2010).

One should notice that I define consistency of institutions not in terms of efficiency, but in terms of survival of (combinations of) institutions. However, it is reasonable to claim that the inconsistency of institutions, i.e. if formal and informal institutions directly contradict each other, so that the formal institutions cannot be fully enforced (Gruževaja 2005) or are misused (Polishchuk 2008, Полищук 2008) per se generates additional costs for actors. It is easily possible to imagine a trade-off between a stable combination of inefficient institutions and institutional reform, creating better institutions but causing additional costs through inconsistency. The concept of “second-best” institutions (Rodrik 2008) targets exactly this trade-off; the problem is of course that the trade-off may

easily imply corner solutions. The costs of inconsistency may also be related to instability of institutional combinations, as it has also been debated with respect to Russia (Перегудов 2008).

The problem of consistency is obviously important for government-business relations. Basically, both formal and informal rules may set a certain balance of power between politics, administration and business, as well as specifically restrict the parties from using certain forms of intervention and instruments of influence. However, the rules set by formal and informal institutions may differ substantially. For example, while formal institutions may specify clear restrictions on interventions of government in economic affairs, informal institutions may as well construct a de-facto hierarchical structure, where businesses are forced to seek support of specific groups in politics and bureaucracy. Alternatively, even in the case the government has de-jure complete authority over business decisions, de-facto this formal hierarchy may co-exist with a sophisticated system of informal bargaining, as it was present in the Soviet administrative market – a concept powerful enough to be applied to at least several post-Soviet countries, as I will show in what follows.

### 3. Government-business Relations in the Post-Soviet Countries

#### 3.1. General Overview

Before proceeding to the specific analysis of government-business relations in selected FSU countries, which will utilize the whole complexity of the framework presented above, it may be prudent to start by giving a short overview of the government-business relations in the whole set of post-Soviet states, which will then serve as a point of departure for the further analysis. While this approach necessarily simplifies the specifics of government-business relations and economic models (partly because of limited data availability and partly due to the need to keep the “eagle’s eye” perspective to stay within the framework of this paper), it still could form the basis for the more detailed investigation in what follows.

To start with, consider different strategies of economic transformation used by the post-Soviet states. From the point of view of economic institutions and reforms, two key elements of marketization include price and trade liberalization and privatization. These two issues (specifically, their relation to the gradualism vs. shock therapy debate) have been probably the key elements allowing to provide a typology of the FSU countries in the 1990s. Specifically, while some countries (most prominently, Russia, Kazakhstan, Armenia and Kyrgyz Republic, and at a later stage also Georgia) followed the “fast track” to the creation of market institutions, other countries (Uzbekistan, Turkmenistan and Belarus, and initially also Azerbaijan) rather preferred a slower path of transformation with significant involvement of the government. Ukraine originally demonstrated a somewhat delayed path of privatization, but later caught up with Russia (as it will be discussed in what follows). The probably most obvious example of the contradictions between these two paths of transition is that between Kazakhstan and Uzbekistan, resulting in substantially different economic performance at different periods of time (Alam and Banerji 2000).

During the 2000s the contradictions between gradualists and shock therapy countries became less apparent. On the one hand, the very concept of transition (as a teleological process resulting into establishment of market economies) for the states like Uzbekistan or particularly Turkmenistan seemed to be less unambiguous: it is questionable whether these countries aspire any form of marketization at all (or rather the current status will survive in the long run). On the other hand, other aspects may turn to be more important for the analysis of the FSU states. Specifically, in the recent paper (Григорьев и Салихов 2006) four key types of development models for the FSU states based on the industrial structure surviving after the transition recession have been introduced. While one of these types refers to three Baltic states (which are of smaller importance for my analysis), three other types explicitly focus on what is perceived as the “former Soviet Union” space in this paper. The *resource* model is associated with an increasing share of natural resources (mostly oil and gas and mining and metals) in the industrial structure and greater dependence on the international commodities markets, and includes Kazakhstan, Turkmenistan and Azerbaijan. The *industrial model* in Belarus is still based on significant industrial assets, partly maintaining their competitiveness in the

FSU through the privileged trade agreements between the countries of the region. The *migration model* of Armenia, Georgia, Moldova, Uzbekistan, Kyrgyzstan and Tajikistan was observed in the countries experiencing the strongest de-industrialization in the FSU, for which in many cases labor migration to other post-Soviet (and partly European) states became the key competitive advantage. For some of these countries (like Tajikistan) migrant remittances form a substantial portion of its GDP.

Once again, this typology is in many aspects simplified. For instance, Russia is attributed simultaneously to the resource and industrial models; Ukraine – to the industrial and the migration models. However, for Belarus reliance on natural resources is significant, although in a different form, than, say, for Kazakhstan: the country depends upon its position at the transportation route of Russian oil and gas to the European consumers. Georgia, while originally a good example of the migration model, seems to move away from this original type of economic organization, partly because of the worsening economic relations with Russia. Nevertheless, for the development of government-business relations this type of reliance on industry or on export of resources may be even more important than the original distinction between gradualism and shock therapy, as it will be discussed in what follows.

On the side of the transformation of political institutions, the story is somewhat more homogenous. Basically, one can differentiate among two groups of the countries of the former Soviet Union, though the borders between them are not entirely unambiguous. On the one hand, the majority of the post-Soviet states in different forms can be attributed to the group of semi-autocracies, i.e. political regimes where the non-democratic government stays in power by imitating (to a certain degree) the democratic decision-making and is somewhat constrained in the application of coercion. Versions of these semi-autocracies vary from more rigorous ones (Uzbekistan or Tajikistan) to somewhat more liberal ones (Kazakhstan and Russia), but the distinction is never straightforward. On the other hand, several other post-Soviet countries have less consolidated political systems, however, usually without clear “rules of the game” characterizing advanced democracies. Whether one should contribute these countries (specifically, Ukraine and Moldova) to “competitive oligarchies” or “unconsolidated democracies” may be an issue of further discussions: both countries mentioned had several experiences of democratic transit of power. Georgia is a more difficult case: after the “rose revolution” it was usually considered part of this “unconsolidated democracies” group, yet recently its political system shows serious features of semi-autocracies. Finally, some post-Soviet countries (currently it is only Kyrgyzstan) experience an extreme weakness of the central government, in many cases unable to exercise effective control over its territory. This typology, certainly, simplifies a lot the further varieties of the elite organization in the FSU, but at least provides describes the key features of the post-Soviet political systems (see Фурман 2004; Макаренко 2005; Gel'man 2008).

To conclude, the development of the government-business relations in the FSU is likely to emerge at the intersection of political (competitive oligarchies / non-consolidated democracies and semi-autocratic regimes) and economic systems (slow reformers vs. fast reformers, relative role of resources, industry and migration as driving forces for the economic growth). From this point of view, the probably most generalistic approach to the study of government-business relations in the FSU can be derived from Iwasaki (2003), who introduces three main models: order state, rescue state and punish state. An order state is characterized by the dominance of well-organized bureaucracy with strong roots in the central planning system, vertical integration of business groups and highly centralized industrial organization. Rescue state is based on much higher decentralization, which, however, involves a significant level of state interventions to prevent chains of corporate bankruptcies, so it still relies on strong presence of the government. Finally, the punish state the government avoids direct participation in the business activities, restricting itself to limited interventions (based on the legal requirements). The group of punish starts, however, includes just Estonia, Latvia and Lithuania. The ordered states in 1992 included Azerbaijan, Belarus, Tajikistan, Turkmenistan and Uzbekistan; Tajikistan and Azerbaijan moved into the group of rescue states as early as 1996. All other FSU economies are attributed to the rescue state group.

While it is obvious that during the economic crisis of the 1990s (the period researched by Iwasaki) the key element of the rescue state machinery has been the ability of the government to support the enterprises in the harsh external environment, during the 2000s three types of government-business relations described in the paper do not lose their validity as such, but rather should be analyzed from the point of view of somewhat different aspects. The key element of the rescue state

under the conditions of the economic growth seems to be rather the ability of the bureaucrats to use their strong position to extract rents. Thus one can actually observe a slow shift of many of the members of the rescue state group towards the conditions of an order state with increasing centralization and stronger control of the government over business. On the other hand, in all three order states of the 1990s certain elements of liberalization seem to have been introduced (with probably the exception of Turkmenistan, which is a country we know very little about at the moment). So, one could describe the 2000s as a period of slow convergence between the rescue states and the order state, if one uses the Iwasaki (2004) classification. The punish states still remain a minority and basically are limited to the Baltic countries.

Nevertheless, while the “eagle’s view” approach can be helpful to obtain the general “map” of the political and economic institutions and the government-business relations in the FSU, this “map” is likely to be somewhat simplistic and in many cases face problems by taking into account the dynamics of the interaction of companies and governments, which often (at least in the post-Soviet economies with a high speed of changes) poses questions and challenges not accounted for by the existing typologies. Hence, in what follows I will provide a more detailed discussion and assessment of the government-business relation models, as they have emerged in four FSU countries: Russia, Ukraine, Kazakhstan and Uzbekistan.

### 3.2. Russia: From “Oligarchs” to “Bureaucrats”<sup>9</sup>

To start with, consider the Russian case, which is most certainly the best studied. The origins of the Russian government-business relations model as it was formed at the turn of the century can be traced back to the privatization of the first half of the 1990s, which served as the foundation for the establishment of a number of large business groups. As it is often argued today, the governmental decisions during this period are likely to have been strongly influenced by the interests of regime stability and political survival (Mau 1999), which makes the emergence of large business groups as a tool of support for the existing regime even more likely. Originally the dominant business groups were bank-centered representing the ability of commercial banks to accumulate financial resources necessary for successful privatization endeavors (though probably smaller than the fair value of the assets).

The crisis of 1998 put an end to the dominance of banks in the Russian industrial system; however, most of the business groups of the early 1990s survived, transforming themselves into industrial holding companies now with main focus in particular industries (Эскиндаров 1999). Pappe (Панпэ 2000) provides a detailed survey of the evolution of this large business groups, and, according to Guriev and Rachinsky (2005), in the early 2000s the lion’s share of the Russian economy was controlled by a small group of asset owners. Foreign investors had a subordinate role in the Russian economy (Грязнов 2000) and were rarely allowed to access the most attractive assets. In addition, many state-owned companies (probably, including even *Gazprom*) went through the informal “quasi-privatization” process, i.e. were controlled by the management rather than by the government as the main shareholder and surrounded by a network of smaller companies used to “absorb” revenues. Although the number of dominant players was very small, the degree of coordination between them was usually limited (with the exception of the most pronounced political decisions, like Yeltsin’s re-elections in 1996), and there was most certainly almost no institutionalized lobbying mechanism present.

The results of this model have been debated in the literature in greater detail. On the one hand, this is the period when “asset-stripping” and “demand for bad institutions” models emerged and were empirically confirmed from the behavior of the large Russian business groups. On the other hand, it would be somewhat simplistic to describe the period as an era of unambiguous weakness of

<sup>9</sup> Since this is a survey paper, I give only a limited discussion of the empirical results from the literature. However, for each country I will provide detailed references to the empirical studies. For Russia, for instance, see Braguinsky (2009) and Guriev and Rachinsky (2005) for the Yeltsin period; Orttung (2004) for the region-center dynamics in government-business relations; and Yakovlev (2005, 2010) and Volkov (Волков 2010) for the Putin period. Yakov Pappe (Панпэ 2000, Панпэ, Галухина 2009) summarizes the development of key Russian companies during the last 20 years.

the state and dominance of private interests. Rather it is possible to describe the period of the Yeltsin's presidency (at least if relations between the federal government and the largest business groups are to be considered) as "strategic business capture with a tactical state capture". The ability of private business to influence the decisions related to individual policies or to successfully negotiate with individual public agencies during this period is hardly in dispute. However, on the other hand, business seemed to be strongly influenced by what one could call a "double lack of legitimacy": unclear legal status of ownership and of control (partly because of the intransparent legal system, but partly because of the attempts of the business groups to hide their control from outside observers through complex schemes of indirect and circular holdings) and still predominant disapproval by the public (which seemed to be relatively stable given the extreme scope of the transition recession in Russia during the period). Therefore, in case of an "outright" conflict between the consolidated government and any business group the latter was doomed to lose, as in fact the following Putin period clearly demonstrated.

Anyway, the majority of powerful business tycoons maintained strong ties with the government, although many of them seem to come outside of the old Soviet *nomenklatura* cadre (Braguinsky 2009). It should be noticed, however, that it would be too simplistic to reduce the complexity of the government-business relations in Russia during the period studied just to the interaction between the federal government and the business groups. Russia of the 1990s also experienced a strong trend towards decentralization accompanied by the emergence of multiple regional political regimes, often able to significantly influence the turn and the shape of economic and political reforms. The relations between business and regional administrations, however, gave rise to a variety of government-business relations models (Перегудов, Лапина и Семенов 1999; Yakovlev 2005). In many cases regional regimes established close ties to the local business effectively protecting it from the federal administration and from the "newcomers" from Moscow and from other regions, thus supporting the system of what Ericson (2000) described as the "industrial feudalism".

This system experienced dramatic changes during the 2000s, which started almost immediately (or, actually, even before) the Putin rule. The first years of the Putin's administration were characterized by significant advancements of economic reforms, when the government was able to break a number of previously existing reform blockades. To give just a few examples, the issue of the property on agricultural land was finally resolved; several codifications of the legal acts were passed by the parliament; taxation system was simplified and the tax level was reduced. There is evidence that the private business actively cooperated with the government while implementing these reforms, as it has been the case, for example, in the area of taxation (Jones Luong and Weinthal 2004). Private business seem to have cooperated with the central government in its attempts to remove the barriers between regional markets created by the protectionist governors of the "industrial feudalism" era, which also prevented the business groups from advancing their expansion in the regions – so, the private business groups in fact strengthened their position in terms of the geographic spread of their presence (Orttung 2004). Hence, there is some evidence of the emergence of "demand for good institutions", which is supported by the increasing internationalization of Russian business effectively enforcing higher transparency standards (Heinrich 2003)<sup>10</sup> and the spread of business associations demonstrating support for the market development (Pyle 2006).

Vladimir Putin was relatively successful in terms of mobilizing resources and consolidating the power basis of the central government, which also implied a shift in the "tactical state capture" system, which was in fact perceived as "state capture" in general by a large fraction of population and by many observers. The original claim of the Putin's government was to maintain what he called an "equidistant" scheme of relations with all potential business groups. Most certainly, already the first years of the Putin's administration witnessed a number of government-business conflicts (Gusinskiy and Berezovskiy deals), which, however, were probably unavoidable in any scenario of the political development of Russia: both businessmen controlled significant media assets and actively intervened in the political processes (with Berezovskiy being probably rather a politician than a businessmen at this stage of his carrier) and at least originally not indicating a direct threat to other business groups.

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<sup>10</sup> Although this period also witnessed an increase of the Russian FDI in the former Soviet Union, where the impact of internationalization on the "demand for good institutions" was not so unambiguous (Либман и Хейфец 2006).

At the same time “equidistant” politics supported the emergence of business associations, making the lobbying process more organized with the advancement of the Russian Union of the Industrialists and Entrepreneurs as the key player (Перегудов 2003).

In addition, Yakovlev (Яковлев 2003) shows that during this period government also increases its “demand for law”, probably to provide a countervailing power to the strong business groups. In fact, it is possible to show that in Russia, contrary to the intuition of the dominant theory, public ownership increased the quality of corporate governance (Yakovlev 2008), what can be explained by the governmental attempts to defend its property rights. Hence, one can immediately observe how (even weak) conflicts between private and public agents can lead to the emergence of the better institutions, even without strong preference assumptions.

The situation seems to have changed significantly (at least from the external observer’s point of view) with the *Yukos* deal in 2003. *Yukos* at that moment belonged to relatively advanced and transparent Russian companies; the attack clearly showed that the double lack of legitimacy was still there and could be used to remove even the “blue chips” from the Russian business community. The development demonstrated that business groups still preferred hidden bargaining and individual patronage schemes to the collective action supporting “one of their own”. Even more, the transparency and the openness of *Yukos* made the attack actually easier, thus suggesting that further opening up was likely to slow down (Панеях 2008). What started with *Yukos* and sporadically surfaced in the Russian economy during the 2000s (like the banking crisis in 2004, with the *Guta Bank* case), became a systematic trend in 2005-2006: the re-nationalization of the leading private companies accompanied by regaining public control over the “quasi-privatized” public businesses and stronger pressure on the remaining large private business groups.

At the end of the second turn of Putin’s presidency the government-business relations model in Russia have changed dramatically. While originally it was influenced by a number of large business groups, now in the key industries (like oil and gas) the control was transferred to the state-owned companies.<sup>11</sup> In a similar way, regional control over important local enterprises was weakened, particularly if the latter were of strategic importance (like the diamond producer *ALROSA* in Sakha, see Bahry 2005). Several sectors of the economy are protected from foreign investors by the new FDI regulation; while already in the 1990s Russian companies were able to gain control over important assets through informal channels, in the 2000s it was strengthened by the legal framework and the pressure of the state-owned business, with the key example of the Sakhalin-2: a gas field where foreign investors were forced to let *Gazprom* enter the exploration project. As a culmination of the increasing public control over the Russian economy, the new legal form of “state corporations” (*gosudarstvennye korporatsii*) provides a number of large public companies (often with development objective, but partly – like *Rostekhnologii* – rather more general collections of assets in individual industries) a special status with relatively limited control.

What is equally important is that the private sector remains linked to the government; in fact, these linkages seem to be growing over time. In the Yeltsin era the problem of “soft budget constraints” of privileged enterprises on the regional and federal level, most certainly, also represented a clear symbiotic relationship between a large fraction of private companies and the governments. In the state-led economy under Putin these relations seem to flourish; on the other hand, private business faces a significant pressure of informal requirements from the government which it has to comply to. For instance, the corruption, according to the existing (but not unambiguous) estimates seemed to be increasing during the period of economic growth between after 1999 (ИНДЕМ 2005),<sup>12</sup> but also during the crisis of 2008-2010 (Маслов 2010). Already during the Yeltsin’s periods many regional governors used the source of quasi-mandatory contributions of business to semi-private funds controlled by the regional elites and to the implementation of regionally important tasks. Under Putin the private companies still in many cases have to act as

<sup>11</sup> Although one should notice that for as early as 2001 Chernykh (2008) reports that a substantial fraction of Russian listed companies were controlled by the state through an extensive use of pyramids.

<sup>12</sup> This study indicates an enormous increase of corruption, yet is criticized in the literature from the methodological point of view (Гурьев 2007). It is also the case that even large corruption probably does not bother business as much, in spite of its high level (ВИЭ 2010); this, however, may just indicate a good level of adjustment to the existing inefficiencies and even “demand for bad institutions”.

substitutes for the provision of public goods by the governments: Polishchuk (2009) looks at the Russian corporate social responsibility from this perspective.<sup>13</sup> In a representative survey of Russian companies, less than 23% of the firms have never provided any assistance to their regional governments (БЛИЭ 2010).

The results of the evolution of this centralized economy and power concentration on the side of the government should not, however, be over-simplified. It is indeed the case that the influence of private “oligarchs” went down dramatically over the last decade: yet it is important not to over-estimate it in the first place and, on the other hand, to notice that the emerging state corporations and largest state-owned companies themselves seem to fill the gap and turn into strong political actors, especially at the regional level. It is particularly noticeable for the state corporations with their “personified” (Волков 2008, 2010) public property structures. Hence, the same problem of influential “business” actors seems to return in disguise: strong owners of private corporations are replaced by the leading bureaucrats of state-owned companies (Петров 2007). On the other hand, it is important not to under-estimate a number of positive trends, both from the point of view of the organization of private business (Паппэ и Галухина 2009) and the government-business relations – however, at the regional level. Frye, Yakovlev and Yasin (2009) and Yakovlev (2010) indicate that one can be observing the formation of the new “alliances” between businesses and regional governments aiming rather to increase competitiveness of the regions and promote investments and development than to act as tools of the regional protectionism. In the same way, the problem of the double illegitimacy is going down, at least, from the point of view of one of its dimensions: the public acceptance of the entrepreneurship, private property (ИКСИ 2005:7) and even big business is increasing – although, as Frye (2006) indicates, the “original sin” of the questionable privatization remains a significant problem for the perception of business in Russia.

### 3.3. Ukraine: Business Groups and Political Conflicts<sup>14</sup>

The Ukrainian mass privatization was delayed as opposed to the Russian one (ИНИОН 2003); however, it does not seem to have prevented the formation of large business groups in this country – rather shifted the channel of their development, which mostly went through the informal “asset grabbing” and “spontaneous privatization” during the 1990s. Since the Ukrainian economy is more decentralized than the Russian one in terms of economic activity, and there is no equivalent of oil and gas as the key appropriable resources, Ukrainian business landscape seems to be rather dominated by regional business groups, which often have close linkages to particular regional administrations and interests (see Kowall and Zimmer 2002). In addition, since the early 2000s Ukrainian economy experienced a strong expansion of the Russian business groups, which, in spite of the existing restrictions, were able to gain dominant positions in a number of sectors, like oil refinery (Либман и Хейфец 2006). Nevertheless, in spite of these differences, as in Russia (and, as it will be shown in what follows, in Kazakhstan) Ukraine still provides an example of the emergence of strong business groups with political ambitions. And, similarly to Russia, during the 1990s these groups seem to have been able to develop a set of informal ties to the politicians and bureaucrats.

Considering the power asymmetry in the Ukrainian model of government-business relations, as it existed prior to the “Orange revolution” in 2004, one could probably once again characterize it as an example of the “strategic business capture combined with tactical state capture”; however, the balance was most certainly shifted towards the business interests, and therefore the area of their “tactical influence” was larger. Probably, the main reason for that is a more pluralistic political system of Ukraine, which allowed greater opportunities for lobbying and interest groups participation.

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<sup>13</sup> A somewhat more difficult area for the analysis of the government-business linkages and interrelations is the international economic activity of the largest corporations. While the claims that Russian business is under strong political control in its international decisions have been numerous, there are also abundantly many observers considering internationalization virtually independent of the political pressure, looking at the internationalization as an escape route from the political pressure or interpreting Russian foreign politics as a tool of private business interests associated with the leading groups of the Russian elite. See also Libman (2009).

<sup>14</sup> A detailed survey of the landscape of dominant business groups and the government-business relations in Ukraine is offered by Kowall and Zimmer (2002) and Aslund (2005).

However, another feature shifting the balance to the business side is the described linkages between partisan, regional and business interests; geography plays a major role in Ukrainian politics, and many political forces have clear regional background, with regional business groups therefore able to make close alliances with politicians representing these forces (Aslund 2005). Nevertheless, the position of the president and the central government during this period should also be not underestimated: Kuchma's regime was able to extract substantial rents and to exercise a clear influence on the business groups (unsurprisingly, Kuchma's family members were able to turn into influential "oligarchs" in Ukraine).

However, the Orange revolution constituted a major political shift, changing the structure of the government-business relations in the country. The role of the business interest for the Orange revolution remains an issue not yet resolved from the empirical point of view. On the one hand, there is evidence suggesting a "business-driven" revolution and based on changes in preferences of the business groups – in line with the "transition inevitable" approach (Gould and Hetman 2008). On the other hand, Aslund (2004) labels the Orange revolution as a "revolt of the millionaires against the billionaires": unsatisfied business community attempting to remove the special privileges of a small group of business leaders strongly connected to the existing government. It is indeed the case that certain business interests can be linked to almost all sides of the conflict. The positions of business groups are often not intuitive and are difficult to trace: there are claims, for instance, that Russian businessmen partly supported the "Orange" opposition. Finally, the Orange revolution can also be interpreted in the framework of this paper as a case of "unintended consequences" of what probably started as a business conflict (Timoshenko deal), but then changed its shape because of the application of alternative instruments different from the traditional "hidden bargaining" (Libman 2006).

While the role of the business factors as part of the Orange revolution is not unambiguous, so are the consequences of the revolution for the development of the government-business relations. On the one hand, during 2004-2005 there was a certain move to transparency in the public policies: for example, the re-privatization of *Kryvorozhstal'*, one of the largest Ukrainian metallurgical plants, can be considered as exemplarily in terms of transparency and openness. However, at the same time the first post-revolutionary government of Yuliya Timoshenko increased its pressure on the private business, initiating a large number of revisions of privatization. Both movement to the higher transparency and increasing public interventions, however, did not last for long given an extremely high level of instability characterizing the Ukrainian economic policy-making during 2005-2010. Business interest involvement in the politics is claimed to remain sufficiently high, and they will certainly remain important under the presidency of Viktor Yanukovich with his regional and economic links; on the other hand, at least in the Timoshenko's policy several traces of the more "government-centered" view of modernization can be detected (Libman 2010b). Hence, Ukraine seems to turn into an experimental field where "transition inevitable" hypothesis can be directly evaluated: did the business interests change in a way consistent with a modernization agenda? There seems to be some indirect evidence for that: largest Ukrainian companies are, for example, interested in maintaining economic ties to the important European markets, what implies a certain level of transparency. The next years of the Ukrainian political development can be of great interest from that point of view.

### 3.4. Kazakhstan: Getting Rid of the Multinationals<sup>15</sup>

The development of Kazakhstan closely resembles that of Russia, but there is also a number of significant differences. At least from the formal point of view, Kazakhstan belongs to the countries implementing consequent liberal reforms and abolishing most forms of public control over economy. In fact, the privatization and deregulation in Kazakhstan was even broader than in other countries of the CIS, for example, with respect to banking system, power utilities and housing sector (where the country's advancement in the more difficult "second generation" reforms seems extremely interesting). The share of private sector in banking was in Kazakhstan in fact larger than in other FSU

<sup>15</sup> For details of the evolution of domestic companies see Junisbai (2010) and for foreign companies Libman and Ushkalova (2009).

countries. So, from the point of view of *formal institutions* Kazakhstan achieved a significant progress in the development from the Soviet-type hierarchical relations to the restricted role of the government in the economy (Либман 2003). Moreover, Kazakhstan seems to be unique in the post-Soviet space (at least, among larger countries) from the point of view of establishing favorable conditions for foreign investors, with huge success in terms of attracting FDI (cf. Libman and Ushkalova 2009).

However, while the formal government-business relations model differed substantially from that existing in Russia or in Ukraine, the situation in terms of informal power distribution was quite different. Kazakhstan actually established a regime with two separate models of government-business relations. On the one hand, in spite of privatization and liberalization effort, Kazakhstan developed a large segment of privileged domestic business groups (mostly controlled by large banks) with strong ties to government (even more specifically, to the president Nursultan Nazarbaev and his family, see Olcott 2002). The dependence of large business from the governmental support was even stronger than in, say, Russia or Ukraine, due to greater power concentration in the office of Nazarbaev.<sup>16</sup> As in Russia, the model was based on mostly centralized business groups (although in the 1990s the country also experienced the informal decentralization, see Libman 2010). However, at the same time the government had to interact with large multinationals from developed countries, which received privileged treatment. Foreign companies, unlike in Russia and Ukraine, were able to acquire the most attractive assets in the country's mining and energy resources sectors. The history of Kazakhstan was full with attempts to "re-write" the rules of the game by individual bureaucrats and politicians on central and regional level; however, until early 2000s foreign corporations still enjoyed significant influence on the governmental politics.

Both models should be considered separately in terms of their influence on institutional development in the country. The relations of political elite with privileged domestic business groups were hardly different than those existing in other countries of the post-Soviet world in terms of demand for bad institutions at the early stage of transition and unclear shifts at the latter stage when business groups from Kazakhstan matured in terms of wealth accumulation and international expansion. Like Russia or Ukraine, Kazakhstan experienced a number of conflicts between the government and the wealthy businessmen, which were lost by the business groups (in particular, the Mukhtar Abliazov deal and the Galymzhan Zhakianov deal in the 2000s). However, there is no evidence that business resolved to "alternative" channels of influence (like it happened in Ukraine), on the contrary, the Abliazov conflict was resolved through a typical undercover agreement (with Abliazov appointed president of one of the largest banks in Kazakhstan, TuranAlem).<sup>17</sup> The impact of multinationals on reforms is not unambiguous, combining elements of transferring better practices with negative convergence and active use of rent-seeking (cf. Libman and Ushkalova 2009), as well as indirect support of semi-authoritarian regimes (Bayulgen 2005) and increasing volatility of institutions (Weinthal and Jones Luong 2001).

However, in the recent years both models started to change dramatically. On the one hand, the government started a slow *re-nationalization process*, which was may be less obvious than in Russia, but still significant. It was accompanied by a change in policy-making: from rather liberal economic reforms towards greater attention to the industrial policy (the well-known "Cluster Initiative" and the further emergence of the *Kazyna* investment fund). Second, the government clearly changed its attitude towards foreign investors: instead of privileged treatment the new aim was to reinstate the control over attractive assets. Though the first successful re-nationalization act was implemented already in 1997, when the government regained control over the nuclear industry (*Kazatomprom*), it was not until mid-2000s when the re-nationalization affected the most attractive oil and gas industry.

Similar to the Russian case, where Sakhalin 2 conflict marked the expansion of the public business towards the assets controlled by foreign multinationals, in Kazakhstan the benchmark was set by the *Kashagan* conflict in 2007, when the government successfully partially re-nationalized this

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<sup>16</sup> However, as Junisbai (2010) points out, the competition between financial-industrial coalitions in Kazakhstan should not be over-estimated, even under current conditions of even stronger power accumulation by the government (to be discussed later)

<sup>17</sup> Interestingly, he lost this position during the re-nationalization of the bank during the crisis of 2008/09, to a certain extent, setting a mark of final transition between models of government-business relations, which shall be discussed in what follows

oil field. It was followed by a number of further examples in oil and gas, as well as in metals and mining and power utilities industries (*AES, Kazakhmys*). In spite of the obvious similarities, the importance of these attacks in the case of Kazakhstan is higher: in Russia the presence of foreign companies was from the very beginning only marginal, while in Kazakhstan the very core of one of the government-business relations models was re-defined (see Libman and Ushkalova 2009).<sup>18</sup> At the same time the country becomes somewhat more open to Russian and Chinese investors, which sometimes are used in the re-nationalization schemes and often seem to be more convenient bargaining partners for the government (Либман 2006).

The shifts of the power balance in the government-business relations obviously affects not only foreign investors, but also domestic companies (as the example with *Mangistaumunaigaz* shows), however, since the politics and bureaucracy has already had a significant impact on domestic business, the changes in relations with multinationals are more pronounced. One could probably claim, claim that the re-nationalization trend is still relatively inconsistent: the attacks clearly focus on individual investors and let others (in spite of possible violations of regulation potentially usable for re-nationalization purposes) out of sight (Смирнов 2008). Generally speaking, the processes in Kazakhstan resemble very much the re-nationalization wave in Russia in mid-2000s, although the scope of public control in Kazakhstan seems to be smaller than that achieved in Russia (on the other hand, Russia was less liberalized in the first place). What is, however, specific for Kazakhstan (as opposed to Russia), is the new infrastructure for public control over assets. The state owned shares in all sectors were consolidated within the *Samruk* holding group under direct control of the president (in Russia there is a number of state-owned enterprises with normal legal status, as well as so-called public corporations controlled by the president) created in 2006. *Samruk* received the public stake in telecom, oil and gas, power utilities, postal services and railroads. The holding officially does not intervene in the operating decisions of companies, however, does make strategic decisions (Смирнов 2007). In 2008 *Samruk* was merged with the state-owned development fund *Казына*, creating an even more centralized system of public control (very dissimilar to the multitude of Russian state-owned corporations).<sup>19</sup>

To conclude, presence of multinationals does not significantly alter the path of the evolution at the re-nationalization stage (but may have been important in the stage of initial reforms, which, as mentioned were relatively successful). One can even claim that the current changes at least to a certain extent are an *outcome* of government-business relations of the 2000s. In fact, the re-nationalization wave is certainly a good example of commitment problem often present in government-business relations. By investing in Kazakhstan multinationals at the same time support and strengthen the existing regime (at least, indirectly through improving economic situation, but also directly through participating in corruption networks and contributing to the formation of international legitimacy). In a phase of high commodity prices even significant expropriation threat still allows profitable investments; hence, businesses cannot credibly commit to “punish” government in case of expropriation. On the other hand, given increasing political power of the regime, the political elite have an increasing incentive to appropriate the investments. Kazakhstan is a very good example supporting this claim, because, unlike other countries where similar re-nationalization waves were observed, the policy shift happened without any leadership changes. However, it implies that given the demand for good institutions in the early model (with relative power on the side of multinationals) was not high enough, the political-economic system was not “pushed out” the old inefficient equilibrium, and hence, multinationals created the basis for their own demise.

<sup>18</sup> The economic crisis 2008 obviously supports the nationalization trend: the banking system of Kazakhstan (relatively more developed and also better integrated in the world economy) was hit by the crisis, and the government had to partly re-nationalize several large banks, including *People's Bank, TuranAlem, Kazkommerzbank* and *Allianz Bank*. Of course, the question remains whether this increase of public control at the turbulent times will ever be withdrawn? Russian experience from the banking crisis 2004 shows that economic turbulences can be used to support the re-nationalization process.

<sup>19</sup> The trend towards centralization of state-owned assets can be traced back to the 2000s, when *KazMunaiGaz*, a state-owned holding for oil and gas assets was set up. It is interesting though that in Russia similar attempts of combining public assets in this area were unsuccessful, probably because of the strong lobbying potential of individual public companies and their “allies” in the politics and public administration.

### 3.5. Uzbekistan: Hidden Business Interests

Unlike three largest countries of the FSU, Uzbekistan basically maintained the old hierarchical structure of economy. Although the beginning of the 1990s witnesses a rapid small-scale privatization, which at least partly implied legitimization of previously underground activities and administrative market (Spoor 1993), the government still maintained control over the largest enterprises and the most attractive assets (which, in fact, constitute the nature of government-business relations). Moreover, in 1996 Uzbekistan introduced severe exchange controls restricting private economic activity across the borders, thus even going back in terms of economic liberalization (cf. Pomfret 2006). Government holds direct or indirect stakes in almost all medium and large enterprises, which operate within the framework of numerous public holding companies, which often have de jure or at least de facto veto power in the corporate decisions. State and business are “fused at almost all levels” (Melvin 2004), and the degree of state capture by the business is extremely low as opposed to other transition economies (Hellman and Schankerman 2000). Uzbekistan has also extremely low acceptance of privatization among population even among other post-Soviet countries with their (although, as discussed above, diminishing, but still important) legitimacy problems for property rights, especially those of large business (Капелюшников 2008).

Of course, even in Uzbekistan there seem to exist fields where foreign investors had a substantial influence on economic decisions. Troschke and Zeitler (2006) claim, that the companies with foreign shareholders are less dependent from governmental support in Uzbekistan. Even more, Gilmore, Collin and Townsend (2006, 2007) provide an example of British American Tobacco, which controls the privatized tobacco industry of the republic and is one of the largest (if not the largest) foreign investors. According to their study, BAT was successful in influencing the tobacco excise policy, in particular, reducing the excise and creating a system benefiting its brands and putting the competitors at a disadvantage. Hence, even in this centralized system there is some place for private rent-seeking. However, it is certainly restricted to non-critical industries. A business elite able to counteract or to challenge the authority of the government (even in extremely limited forms and finally unsuccessfully, like in Kazakhstan), did not appear in Uzbekistan (Serra i Puig 2007). The few wealthy entrepreneurs in Uzbekistan are closely related to the president (for example, president's daughter Gulnara Karimova, is claimed to have business interests in telecom, gold-mining (Collins 2006:271), as well as retail, beverages, construction material, media and tourism. There is a number of influential businessmen listed as potentially controlling certain sectors of the economy, but usually they not have formal claims on assets (which are state-owned), but rather “control financial flows” (as the Russian oligarchs in the very early stage of transition used to do).

The positions of the local business elite are highly unstable, as opposed to other countries of the former Soviet Union. For instance, in 2010 the Prosecutor General of the country started an attack on the key representatives of the business elite, including the owners of banks and retail markets, as well as those controlling the bazaars. The accusations were followed by arrests and significant governmental pressure on the business at all levels. While there have also been some cases of government-business conflicts in the country (Sanjar Umarov's case in 2005), their impact – as opposed to the Russian Yukos deal or Ukrainian scenario – has been very limited if not minuscule.

However, Uzbekistan, as well as almost all Central Asian states, seems to be strongly affected by the presence of regional interest groups, which are able to have a significant impact on the political decision making and even to restrict the enforcement of the centralized policies (Libman 2010). Traditional and regional clans become important political-economic players establishing their clientele networks and creating the “tacit division of major industries and sectors” (Gaman-Golutvina 2007). Even limited openness and introduction of quasi-market institutions increase enormously the potential for rent-seeking. For example, in spite of formal centralization, individual managers of enterprises seem to have extremely large opportunities for asset-stripping (Repegather and Troschke 2006): the de-facto devolution of power is, probably, similar to that in the Russian state-owned sector under Yeltsin. Therefore it seems to make sense to use the concept of the administrative market developed originally to describe the informal bargaining in the Soviet state-owned economy as a

framework to accurately describe the complex bargaining and negotiations in the public sector of Uzbekistan – and, as in case of the Soviet economy, it is important not to over-estimate the formal centralization, which is the top of the iceberg open for external observers.<sup>20</sup>

## 4. Conclusion

### 4.1. Commonalities and Differences of Government-business Relations

To conclude, it is possible to provide a brief overview of the key features of government-business relations in all four countries studied in this paper. Basically, four common aspects seem to be present in all economies (see also Libman 2006a).

1. In most countries one observes an encompassing rent-seeking on the government size. While the reasons for this rent-seeking behavior may be different (for example, political ambitions of the Ukrainian politicians after the “orange revolution” versus hidden contests of clans in Russia or Kazakhstan), in all countries political involvement in the business activity is rather a routine event than an extra-ordinary situation, and usually is focused on controlling and fighting for rents available in the business sector. Therefore all countries also show very high level of corruption.

2. Most countries still exhibit certain elements of what can be called a “power-property” system (Нуреев, Рунов 2002; Плисевич 2008). Hence, the political power and the business structures in all countries form stable coalitions operating on both political and economic markets. Even the most democratic country of the group – Ukraine – seems to be subject to this problem; it is rather the fragmentation of political-business coalitions than their absence, what is explaining its political and economic dynamics.

3. The extent of economic concentration in all four countries is relatively high. While the shape of this concentration is different (from mostly regional business groups in Ukraine to state-controlled Russian and Kazakhstani companies and informal relations with oligarchs in Uzbekistan), there are almost always significant entry barriers on the economic market and a small number of dominant companies present shaping the government-business relations. However, this concentration should not be mistaken by the presence of unidirectional hierarchical control of the government over business: in most cases these selected business groups form very sophisticated power relations with the government, often based on mutual interdependence and permanent re-allocation of political and economic property rights.

4. In all four states discussed in this paper the informal relations and networks have been dominating the government-business interaction models. This factor, probably inherited from the Soviet past and the turbulences of the transition period, and combined with the high concentration, may explain the relative weakness of the institutionalized lobbying of the European and US type in the former Soviet Union. Certainly, institutionalization of lobbying is difficult in the non-democratic countries, and in many cases requires considerable amount of time – so, Russia, Ukraine, Kazakhstan and Uzbekistan are not unique in this matter (see also Kennedy 2005 for the evidence concerning China), but the failure of attempts to create organized business representation (particularly in Russia) is striking.

These four aspects seem to remain stable over time and thus could constitute the fundamental features of the post-Soviet economies. On the other hand, the specific balance of power between the business and the government, as well as the domination of different private and public coalitions is much less robust and exhibits significant changes (as it has been demonstrated above). However, while the FSU countries discussed in this paper share a number of common features, there is also a significant number of differences to be mentioned. *Table 1* provides a brief overview over the key distinctions between the government-business relations in these four countries.

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<sup>20</sup> One should notice that the analysis so far concentrated mostly on large-scale industries and companies in Kazakhstan and Uzbekistan and ignored the flourishing informal sector in these countries, mostly comprised by small entrepreneurs. Empirical evidence has been reported, for example, by Ozcan (2010).

**Table 1:** Government-business relations in Russia, Ukraine, Kazakhstan and Uzbekistan – key differences

Characteristic	Russia	Ukraine	Kazakhstan	Uzbekistan
Dominant form of private business groups	Industrial business groups	Regional industrial business groups	Industrial and banking business groups	Informal holdings of individual oligarchs
Role of state-owned companies	Currently significant	Limited to specific areas	Significant (but lower, than in Russia)	Highly significant (main industries under state control)
Concentration of state-owned companies	Low (multiple competing centers)	Not applicable	High (SamrukKasyna)	Mixed (given the dominance of state-owned companies in the economy)
Role of regional business groups	Declining	Significant	Declining	Mixed (based on informal power relations)
Role of foreign investors	Low	High (Russian companies)	Declining (weakening of multinationals)	Mostly low (with some exceptions)
Degree of informality of property rights of domestic business groups	Low (with the exception of state-owned companies)	Low	Low (with the exception of state-owned companies)	High
Relative concentration of power	Currently on the side of the government, but with exceptions (“personalized” property in state-owned corporations)	Mixed, depending upon particular political coalition (and may shift on the side of the business)	On the side of the government	On the side of the government
Government-business conflicts	Strong in the early 2000s, resolved through hidden bargaining	Very strong, resolved through partial institutional change	Significant (but weaker than in Russia) in the early 2000s, resolved through hidden bargaining	Relatively weak (but present), no significant impact on the business elite

Once again, these differences seem to be much less stable than the commonalities. It should also be mentioned that in most cases they just reflect the *relative* extent of certain features in my sample, rather than their *absolute* levels. So, although formalization of property rights is somewhat higher in Russia than in Uzbekistan, both countries suffer from the predominance of informal institutions; although the power balance in Ukraine is rather shifted to the business than to the political side, the “strategic business capture with a tactical state capture” could be observed in both countries.

## 4.2. Empirical Validity of Theoretical Predictions

The discussion so far focused on a number of possible hypotheses describing the influence of the government-business relations on the emergence and development of political and economic institutions in the FSU, as well as provided a brief and unavoidably somewhat simplified overview of the evolution of the government-business relations in four countries of the region. Therefore it is now possible to link the hypotheses with the stylized evidence.

To start with, Table 2 summarizes the key arguments for all hypotheses I have obtained from different countries. It should be pointed out that, for example, the “transition inevitable” vs. “transition frozen” theses refer rather to the *theoretical conjectures* for which individual countries could provide empirical evidence than to an attempt of a *typology* of post-Soviet economies – although some differences may be present. However, in different countries the predictive power of different hypotheses was different. On the one hand, one can claim that in all FSU countries the impartiality of the government is low; its level of autonomy differs though between semi-autocracies and more competitive systems. The evidence regarding the demand for good institutions from the business and from the government, as well as the conjectures regarding the consistency of institutions are, however, somewhat mixed.

**Table 2:** Government-business relations in Russia, Ukraine, Kazakhstan and Uzbekistan – evidence for the hypotheses

Characteristic	Russia	Ukraine	Kazakhstan	Uzbekistan
Autonomy of the government	High	Low	High	High
Impartiality of government	Low	Low	Low	Low
Demand for good institutions by business	Mixed	Mixed	Mixed	Absent
Demand for good institutions by the government	Mixed	Absent	Mixed	Absent
Consistency of institutions	Increasing	Low	Increasing	High (but restricted because of the administrative market)

In what follows I will consider the problem in greater detail. The results for the “transition inevitable” versus “transition frozen” contradiction are rather inconclusive in case of Russia and Kazakhstan. On the one hand, in the early 2000s both countries did demonstrate some movement of its corporations to higher transparency and international best practices, which is unavoidably

associated with the changes in the demand for institutions, and therefore an “inevitable transition”. But these changes seem to have affected only a fraction of the business groups, while many other still remained in the realm of the old intransparent bargaining and “demand for bad institutions”; even more, for the “advanced” business groups it is not clear whether the change was “deep” or rather “shallow” and related rather to image than to the real transformation of the business practices. Anyway, the subsequent increase of public interventions in both countries makes the analysis very difficult: the chances of business communities to have an influence on politics went down and, on the other hand, increasing activity of bureaucrats had a certain distortionary effect on the economic behavior (for example, an Alpha Bank stock market report (Уифер и ДеПой 2006) describes state-owned companies as the most attractive from the stock market investor’s point of view). The situation in Ukraine seems to be more promising, but will become evident only in turn of the Yanukovich’s presidency. For Uzbekistan, where business community is less developed, the “transition inevitable” arguments are unlikely to be present in the first place.<sup>21</sup>

For the autonomous versus rent-seeking government, on the other hand, we find confirmation for both of these conflicting points of view. Russia during the 1990s demonstrated almost all negative features related to a limited autonomy of the government – from inability to construct the reform coalitions to the design of inefficient institutions in order to control potential challengers to the incumbents. In the same way, evidence of inability of a non-autonomous government to support a rigorous reform program can be found in Ukraine. On the other hand, Russia of the 2000s seems to provide evidence for the costs of the rent-seeking government, which uses its advantage rather to extract rents than to promote economic reforms. Libman (2010a) shows that in Russia increase of the (relatively small, according to the international comparison) bureaucracy is associated with the reduction of economic growth. Similar considerations are applicable to Kazakhstan. Even more, an extremely cautious political elite like that of Kazakhstan with strong interest for the international reputation, which originally seems to have contributed a lot to the liberal reforms in the country (Либман 2004), is unable to resist the temptation if the rents become sufficiently high and the power balance is shifting towards the political actors (as it happened during the 2000s). Even the Ukrainian mass re-privatization attempts of the post-revolutionary government of Timoshenko could be considered within this logic, although in this case political and ego-rents have most certainly been more important than the economic ones and the autonomy of the government is much lower (given the generally more competitive political system).

Anyway, it looks like governments, whether weak or strong, are unable to promote economic reforms – either because they lack resources to do it, or they are not interested in it. Business, which during the 1990s rather supported inefficient equilibria, could turn into a strong proponent for economic reforms; however, the evidence is not entirely clear and, more importantly, in many cases the influence of the big business began to diminish exactly when the possible demand for good institutions was able to surface. However, the results are more promising if one looks at the unintended outcomes of the government-business conflicts. The Ukrainian case suggests that applying “alternative” instruments of these conflicts (i.e. moving away from the hidden bargaining approach) can at least support the political democratization; the consequences for the economic reforms are not clear. In the same way, in Russia government’s demand for institutions can be attributed to the attempt to balance the power of business groups. However, in Russia and in Kazakhstan open conflicts between influential business leaders and governments did not involve “alternative” instruments and simply supported the spread of the hidden bargaining practices and vertical mistrust, making existing inefficient equilibria more stable.

The final aspect of the analysis, as mentioned, looks at the institutional congruence. From this point of view the strong deviation between formal and informal institutions, which has been widely accepted as a general problem for transition economies (Gruževaja 2005), is present also in the government-business relations models. One could even go that far and claim that the country with smallest deviation in the 1990s – Uzbekistan – seems to demonstrate very good economic

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<sup>21</sup> If the business controls resources through informal channels and claims on revenue rather than on assets, it is unlikely it is willing to undermine its own control. Of course, there may be some demand for the “first-generation” reforms like privatization, but, to my knowledge, no empirical evidence is present in this respect.

performance (the so-called “Uzbek paradox”, see Spechler, Bektemirov, Chepel’ and Suvankulov 2004); hence increasing dominance of the government in the state-business relations is likely to increase institutional consistency and to promote higher performance (Кирдина 2009). This analysis of course disregards the content of the government-business relations models: it is very likely that the convergence is happening towards a generally inefficient equilibrium, and in this case the benefits from institutional consistency are much lower than the costs of being caught in an institutional trap (Libman 2007a). However, besides this need to take into account alternative analytical perspectives, the idea that increasing governmental presence increases institutional consistency is also not natural: it is possible that it simply increases the domain of the hidden bargaining and competition within the political machine and bureaucracy and between the public agencies and the privileged business groups – once again, restoring the Soviet administrative market; therefore the inconsistencies actually are preserved, just have a different shape now.

The discussion so far should acknowledge a number of limitations. First, the representation of individual government-business relations models and their evolution is highly stylized: it probably makes more sense to look specifically at the interaction between individual governmental agencies and companies, which can exhibit very different patterns of interdependence. It is also the case that quite often the shifts between individual government-business models have been less clear and unambiguous as it has been presented so far. For example, Yakovlev and Zhuravskaya (2006) claim that the level of state capture *in Russian regions* under Yeltsin and under Putin remained virtually the same; firms and regional officials were quite successful in avoiding the consequences of partial reforms.

The paper also ignores the changes caused by the global financial crisis, which hit the economies of the FSU relatively hard (Николаев, Марченко и Титова 2009). For example, the crisis can turn back the positive developments relevant for the “transition inevitable” theory (for example, generational change seems to be delayed and foreign management staff involvement weakened). Anyway, observing future changes in the state-business relations in the post-Soviet space remains an interesting challenge for the research.

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## ABSTRACT

The paper surveys the existing evidence regarding the influence of the government-business relations on the development of economic and political institutions in a number of countries of the former Soviet Union. By doing that, it uses three different analytical perspectives: asymmetry of power between the public agents and the private business; unintended consequences of the government-business conflicts; and the institutional consistency in the organization of the government-business relations models. It discussed the main theoretical predictions generated by these three perspectives and looks at a number of competing hypotheses, which explain the impact of particular models of government-business relations on the institutional performance: for example, demand for bad institutions vs. demand for good institutions, and autonomous vs. rent-seeking government. In the empirical part the paper looks particularly at four countries: Russia, Kazakhstan, Ukraine and Uzbekistan.

► KEY WORDS: government-business relations, demand for institutions, autonomous government, rent-seeking

► КЛЮЧЕВЫЕ СЛОВА: government-business relations, demand for institutions, autonomous government, rent-seeking