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Inna Melnykovska: Colour Revolution or Soft Authoritarianism? Institutional Change in Ukraine and Russia

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Abstract

Transition in the countries of the former Soviet Union (FSU) has tended to follow the same trajectory, resulting in “soft authoritarianism” and “clan capitalism”. But recent upheavals — the so-called “colour revolutions” — in Georgia, Ukraine, and the Kyrgyz Republic have challenged the existing regimes. The aim of this paper is to explain why colour revolutions occurred in some countries of the FSU while the political regimes in others have remained intact. Ukraine and Russia, respectively, were chosen as case studies.

According to the theory of institutional change put forward by Douglass North, change is taking place in every country. Arguing that colour revolutions and soft authoritarianism involve institutional change — discontinuous in Ukraine and incremental in Russia, the paper addresses the logic and driving forces behind this change.

The main actors in Ukraine and Russia were oligarchic clans, which benefited from the reform gridlock in the early years of transition. In addition, their individual economic privileges allowed them to extract rents. Surprisingly, most oligarchic clans directly or indirectly supported Putin’s reforms in Russia and the Orange Revolution in Ukraine. Therefore, the paper focuses on the changes in the sources of income and economic rents and analyses how these changes influenced the preferences of the oligarchic clans.

The paper identifies the following results:

(i) In the 1990s, Soviet legacies shaped the actors and their preferences. However, as the clans became more and more integrated into the global economy, they were forced to follow international standards of doing business. Additionally, the demands of international markets changed over time. After the 1998 crisis in Russia, transparency and good corporate governance gained importance.

(ii) The behaviour of elites also reflects learning from the transition experiences. Initially, elite groups preferred to avail themselves of informal practices and individual economic privileges. However, having accumulated properties and capital, they became owners, and therefore became interested in the security and sustainable growth of their empires. The existing patronage relationships were highly unstable and could not fulfil these new preferences properly.

(iii) The oligarchic clans in both countries are evolving from “roving” to “stationary” bandits (Mancur Olson). Under the pressure of globalisation, which constrains their rent-seeking possibilities, and due to the instability of the informal networks, they have changed their preferences. Now, they are striving for good and secure state governance. However, due to differences in the sources of profits and economic rents, rent-seeking for the Ukrainian clans was limited through anti-dumping measures aimed at their metal products. In addition, higher oil and gas prices led to higher production costs and reduced competitiveness. These factors forced the Ukrainian clans to adapt their behaviour faster than their Russian counterparts.

(iv) The state should play the role of an arbiter capable of protecting property rights and guaranteeing stability. While Putin consolidated state authorities and created a system with a “dominating power”, Kuchma pursued a “divide and conquer” policy in circumstances of “feckless pluralism”. The relatively free media and the population’s dissatisfaction with its political ruler as well as the abandonment of punishing “defections” helped the Ukrainian clans to develop a confrontational strategy towards the incumbent regime.

Ukraine and Russia have moved along a transition trajectory common for the post-Soviet republics. Along the way, they have had to cope with the triple task of building a nation state, implementing democracy and moving towards a market economy. Ironically, the relatively peaceful foundation of the Ukrainian and Russian states has led to the preservation of power in the hands of the old elite groups, who were neither experienced nor interested in the radical reforms. Consequently, the lag in the transition of the political and economic spheres resulted in “soft authoritarianism” and “clan capitalism”.

Political and economic scientists searched for mistakes in the liberal reforms, designed according to the Washington Consensus, and defined the forces impeding their implementation.¹ The labels for the new regime outcomes²—“defective democracy”, “imitative democracy”—supported the idea of a continual transition, but whether or not the transition was headed towards democracy was disputable. Those who considered “authoritarian” and “patronal” regimes to be the final outcomes of the transition, as well as those who still hoped for a further democratisation in the former Soviet Union (FSU), were surprised by the “colour revolutions” and absolutely unprepared to respond to the subsequent tensions in the region. The turn of events fuelled speculation over further radical democratic reforms in Ukraine and over the potential for regime change to spread within the FSU; these speculations were not confirmed, however. Insufficient understanding of recent events reawakened old beliefs in enigmatic, inconsequential and chaotic trends in the post-Soviet area. The aim of this paper is to explain why “colour revolutions” occurred in some countries of the FSU while the political regimes in others remained intact. Ukraine and Russia, respectively, were selected as case studies.

Are the “colour revolutions” real revolutions?

To unravel the mystery of why the Orange Revolution occurred in Ukraine while the political regime in Russia remained stable, it is useful to narrowly define terms and dispense with a few common misconceptions.

A serious question remains as to whether the term “revolution” is even appropriate in these cases. The answer depends on the definition itself. Does “revolution” mean an attempt to establish a radical new order and withdraw old privileges, or should the more moderate definition of a springboard for new political activities be taken? Fairbanks identifies many features of a classical revolution in these upheavals, but has proposed treating the “colour revolutions” as a new and largely non-violent subspecies.³ However, the events during and after the Orange Revolution in Ukraine hardly constitute a regime overthrow. By mutual agreement of orange and white-and-blue political forces⁴ during the new round of presidential elections in 2004 and due to constitutional changes to reduce presidential power, Ukraine was transformed into a parliamentary republic. The “Party of Regions”, an opponent of the “orange” coalition political force, won the parliamentary election of 2006, and created a parliamentary majority with the Communist and the Socialist parties. Viktor Yanukovich, Viktor Yushchenko’s rival in the presidential run-off, became the prime minister with the backing of the “Our Ukraine” bloc. All in all, the forces in the Ukrainian political game are still the same, but the distribution of power between them has changed and the possibility of monopolisation of state authorities by any one political force has been diminished. Therefore, it is more appropriate to treat the Orange Revolution as a peaceful but discontinuous – and therefore visible – transformation of the political regime in Ukraine. According to North, such a transformation—when different

1 Hellman, Joel S.: *Winners Take All: The Politics of Partial Reform in Postcommunist Transitions*, in: *World Politics*, 1998 (vol. 50), No. 2, pp. 203–234.

2 Levitsky, Steven / Way, Lucan A.: *The Rise of Competitive Authoritarianism*, in: *Journal of Democracy*, 2002 (vol. 13), No. 2, pp. 51–65; Diamond Larry: *Thinking about Hybrid Regime*, in: *Journal of Democracy*, 2002 (vol. 13), No. 2, pp. 21–34; McFaul, Michael: *The fourth wave of Democracy and Dictatorship: Non-Cooperative Transition in the Post-Communist World*, in: *World Politics*, 2002 (vol. 54), No. 2, pp. 212–224.

3 Fairbanks, Charles H. Jr.: *Revolution Reconsidered*, in: *Journal of Democracy*, 2007 (vol. 18), No. 1, pp. 42–57.

4 Orange is the colour of Yushchenko’s “Our Ukraine” bloc. Blue and white have become symbols of Yanukovich’s “Party of Regions”.

groups build a coalition to resolve reform gridlock—takes place if informal and formal institutions do not provide a “framework for actors to settle disputes, realise the potential gains”.⁵ The institutional change could be continuous, as in Russia, if a state ruler “makes new bargains and compromises between players possible”. Therefore, “change” is the most appropriate term to describe the “colour revolution” and “soft authoritarianism”, because it encompasses both types of transformation.

Most studies on the “colour revolutions” deploy the “method of similarity” and concentrate on the countries in which the revolutions took place. McFaul identifies the similarities of the upheavals and their distinctions to other democratic revolutions.⁶ Fairbanks compares the upheavals in a historical perspective with the French and English Revolutions. The comparison gives rise to a catalogue of the circumstances necessary for a successful revolution. However, the “method of similarity” has its weaknesses. On the one hand, the circumstances are not reliable indicators until their presence or absence is determined in non-revolutionary cases. Thus, countries that have not experienced “colour revolutions” should be included in the analysis. On the other hand, these circumstances are mostly conditional variables, which are guaranteed to have a certain effect on the upheavals. The deeper reasons of why some actors — oppositional or allied — decided to use these circumstances to confront an incumbent regime remain undiscovered.

The change driving forces in a rent-seeking society

Following a “first-level” analysis, institutional change – often called “reform” – is devoted to a new national ruler coming to power by means of either an uprising or election. In the FSU, any state that lost its legitimacy prior to the transition – and therefore became even weaker during the transition process – was unable to encourage or implement reforms. Elite groups, often organised in oligarchic clans, were the only powerful actors there. Moreover, at the beginning of the transition process, the policy recommendations were foreign and alien to national, central and local elites. Elites were only interested in the implementation of those reforms that provided personal benefits. As a result, reforms were implemented only partially.

The enforcement and implementation of reforms in the countries of the FSU depend not only on central state rulers, but also on central and local state actors, as well as non-state actors, especially economic ones. By this logic, the successful implementation of Vladimir Putin’s reforms could be explained by the wide support they enjoy among Russian elite groups; the president’s policy caters to their preferences. Similarly, the dissatisfaction with the reform gridlock under Leonid Kuchma also reveals a shift in the preferences of the Ukrainian elites, which, however, were not incorporated into state policies and ultimately led to the ouster of the president. Having neglected the advantages and opportunities of “defective democracies” and “clan capitalism”, most oligarchic clans directly or indirectly supported Putin’s reforms in Russia as well as the Orange Revolution of 2004 and the subsequent institutional changes in Ukraine’s political and economic system. The members of the oligarchic clans, supporting the “orange camp”, took part in the public protests personally or indirectly by providing financial and media resources. It is evident that the elite groups in Russia and Ukraine have changed their preferences. However, what are the determinants of these changes and what preferences do the elite groups have nowadays?

Arguing that the “colour revolution” and “soft authoritarianism” involve institutional changes, but of a different type—incremental in Russia and discontinuous in Ukraine—the paper addresses the logic and driving forces of these changes. As oligarchic clans play an important role in Russia and Ukraine, the paper focuses on the changes in the sources of income and economic rents after the 1998 crisis in Russia and analyses how these changes influenced the preferences and strategies of the oligarchic clans.

5 North, C. Douglass: *Institutions, Institutional Change and Economic Performance*. Cambridge: Cambridge University Press, 1990, p.90.

6 McFaul, Michael: *Transition from Postcommunism*, in: *Journal of Democracy*, 2005 (vol. 16), No. 3, pp. 5–19.

Clans: major political-economic players

“Clans”, with their hidden social network system, are not a new phenomenon in FSU political systems. They have their origins in the Soviet past. Unsurprisingly, in the early period of transition, the clans’ representatives, possessing administrative resources held over from the Soviet system, had opportunities to shape reforms to their own advantage and accumulate large amounts of capital. Furthermore, being the early winners of the transition period, the clans obstructed the progress of those economic reforms in Ukraine and Russia that were detrimental to their interests and bolstered political and economic institutions that were beneficial to their financial empires.⁷

Although “clan capitalism” is widespread in the post-Soviet area, the Ukrainian and Russian clans differ from traditional clans. They are not groups of relatives or systems of kinship, but business entities.⁸ They are mainly interested in the accumulation of assets, profitable activities and new markets. In terms of power structure and distribution of profits, the Ukrainian and Russian clans are divided into hierarchical levels. The top position is endowed to a “chieftain”, who is surrounded by a “core” of trusted business partners, relatives and friends. The next levels in the clan’s hierarchy are filled by professionals and ordinary members working in the enterprises under the clan’s control. Agents of influence or patrons in politics occupy a special place. Officially, they are not members of the clan, but their mutual support and cooperation are vital for the clan’s fortunes. The patronage relationship between Pavlo Lazarenko, the former prime minister of Ukraine, and Yulia Tymoshenko, the former president of the United Energy Systems of Ukraine, ensured the monopoly of this company on the Ukrainian gas market.

In addition, the symbiosis between politics and the economy involved more than just a simple patronage connection. The assimilation of the clan’s members in politics and visa versa was a common phenomenon. During the Ukrainian and Russian transition periods, the special hybrid of a political-economic actor—often called an “oligarch”—arose. In this sense, an oligarch is a political entrepreneur who uses the strategy of “power-money-power” for capital accumulation and its circulation. Access to the state power structure enables oligarchs to reap profits, which they reinvest to broaden their political power. The personal representation of the clan’s interests by a chieftain or members of the “core” in politics was widespread in Ukraine and Russia.

The establishment of the Ukrainian and Russian clans’ financial empires followed similar historical paths. During the early years of transition and the presidencies of Kravchuk and Yeltsin, the clans started to accumulate their capital. With gains from illegal trade or financial speculation, oligarchs bought profitable enterprises during national privatisation auctions. State officials supplied the oligarchs with information about the financial situation and productive capacities of the enterprises and ensured them a privileged position during the privatisation auction. Consequently, the oligarchs’ fortunes were concentrated in the most profitable sectors, such as the oil, gas, metallurgy, machinery and food industries. Due to the dissemination of the clans’ properties across different branches, the separation between clans is not drawn along industrial lines. For the most part, clans are incorporated according to a regional principle. Additionally, because their business interests are concentrated in the few most profitable spheres of the Ukrainian and Russian economies, clans often compete with each other.

Unlike their Russian counterparts, the Ukrainian clans are characterised not just by inter-clan competition but also by internal rivalry.⁹ In Ukraine’s case, clan members do not interact in the particularly close and mutually supportive way typical among kinsmen. Instead, there is internal rivalry, the consequence of fissions among new business groups in the clans, whereby enriched members of the core went on to create their own clans. The increasing number of clans in both countries complicates the classification of the clans

7 Hellman, Joel S.: *Winners Take All: The Politics of Partial Reform in Postcommunist Transitions*, in: *World Politics*, 1998 (vol. 50), No. 2, p. 204.

8 Relatives could be included in a clan, but familial relationships play a secondary role.

9 Kosals, Leonid: *Interim Outcome of the Russian Transition: Clan Capitalism*. Discussion Paper No. 610, Kyoto Institute of Economic Research. Japan, January 2006.

along regional lines as well. Sharing the same regional origin did not stop the newly created clans from competing with each other. Clan wars were not unusual in Ukraine and Russia.

The political systems in both countries are dominated by the oligarchic clans. Ukraine possesses a multi-clan system in which no one clan wields enough power to monopolise the state; the clans are therefore forced to cooperate and compromise with each other. In Russia's mono-clan system, a single clan is capable of implementing institutional change. However, a wise leader cares about the interests and relative benefits of those clans that provide support to the dominating clan and punishes clans that weaken it.

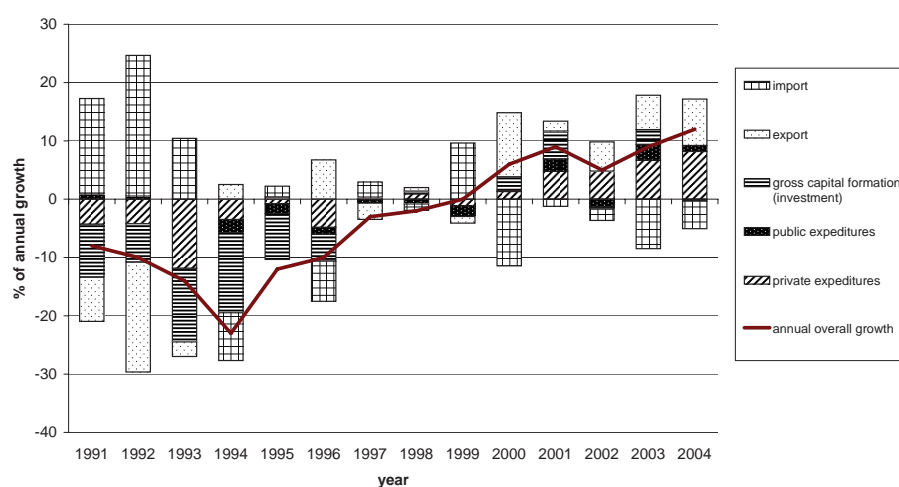
From a national to global player: striving for sustainability

At first glance, the interests of the oligarchic clans vis-à-vis reforms might seem enigmatic. This can be explained by arguing that the oligarchic clans in Ukraine and Russia are abandoning their strategy of pure capital accumulation for one of capital security. As Mancur Olson puts it, the oligarchs are evolving from roving to stationary bandits and widening their time horizon.¹⁰ Their short-term goals include the accumulation of profitable new assets, lobbying in state bodies and eliminating rivalries. The clans' long-term strategy is not only to accumulate but also to secure their assets and foster the sustainable growth of their companies and society in general.

Due to the rapid economic growth since the end of 1990s, the majority of oligarchs have at least doubled their fortunes.¹¹ In the early stages of transition, the security of property rights and rule of law held little interest for the Ukrainian and Russian oligarchic clans. On the contrary, weak property rights allowed them to define the enterprises to be privatised and to acquire new assets in the privatisation auctions. Even after the auctions, the oligarchs neglected the rule of law and refused dividend payments to small shareholders and workers. The subsequent disappointment among small shareholders enabled them to buy up all the shares of the enterprises at artificially low prices. With the enlargement of their own fortunes and business empires, the necessity for protected property rights became imperative. Anatoly Chubais complained that Russian businessmen "stole absolutely everything during raw capitalism", but nevertheless remained optimistic, arguing that as owners, they would become decent administrators of this property.¹²

Whether or not the oligarchs have achieved the limits of capital accumulation and shifted their focus to capital security is difficult to determine. A deeper look at the driving forces of the current economic growth and sources of rents in both countries is therefore necessary.

Figure 1a. GDP growth by demand components in Ukraine, 1990–2004



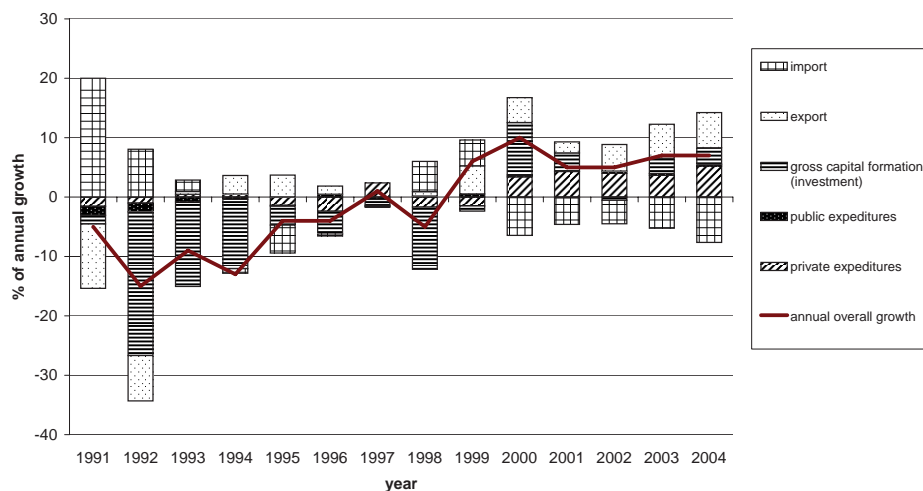
Source: World Development Indicators, World Bank; own calculations.

10 Olson, Mancur: *Power and Prosperity: Outgrowing Communist and Capitalist Dictatorship*. Basic Books, 2000.

11 Lista 100 Najbogatszych Europy, Wprost.

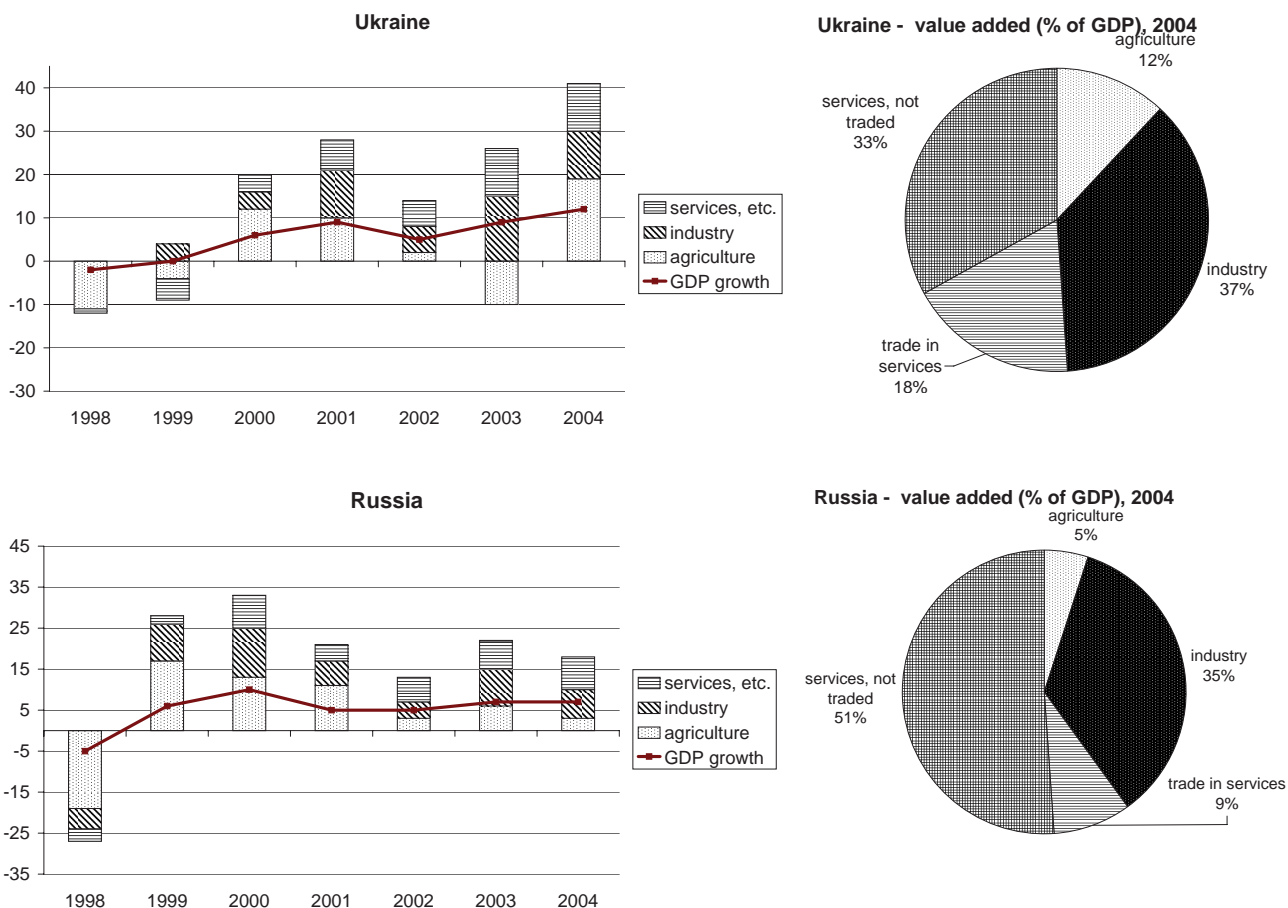
12 Steen, Anton: *Political Elites and the New Russia. The Power Basis of Yeltsin's and Putin's Regimes*. London: Routledge, 2003, p. 93.

Figure 1b. GDP growth by demand components in Russia, 1990–2004



Source: World Development Indicators, World Bank; own calculations.

Figure 2. GDP growth by sectors in Ukraine and Russia, 1998–2004



Source: World Development Indicators, World Bank; own calculations.

Now that Ukraine and Russia have achieved strength via economic growth, the issue of how to sustain this growth has become crucial. Figure 1 reveals in detail the drivers of growth from the demand side, showing contributions of final use components to GDP growth. Figure 2 analyses the value added by economic

sectors.¹³ Because the drivers of growth have changed from year to year, different phases of growth can be distinguished.

Some evidence of output recovery appeared in late 1997 in Ukraine and in early 1998 in Russia, but fell quickly during the financial crisis of 1998. After the crisis, economic performance was mainly driven by the increased competitiveness of the Ukrainian and Russia goods brought about by the devaluation of the hryvnia and the rouble. The resulting reduction of real wages and huge cuts in real social spending led to a significant drop in real household incomes. Rising poverty caused the population to prefer cheaper domestic goods as the prices of imported goods skyrocketed. However, those negative tendencies had a positive effect on the domestic private sector, which, due to huge domestic demand, started to recover and make profits. As shown in Figure 2, industry played the driving role in the recent recovery, followed by the service sector. Industrial production began to recover in 1999, especially in those non-resource sectors that were oriented towards domestic markets. The fall in real wages and cheap domestic resource prices decreased input costs and made Russian and Ukrainian industries competitive on world markets. Additionally, liberalisation and privatisation reforms allowed private enterprises to seize the opportunities provided by currency devaluation. Therefore, in the initial period of 1999 to 2001, economic recovery was not solely resource-dependent in either country.

Since 2000, inflation in both countries has gradually declined. Russia experienced an oil extraction boom and Ukraine benefited from the strong international demand for metal products. Additionally, export prices for energy resources and metal products were extremely high. Thus, while the positive effects of the devaluation gradually faded, the oil and gas industries in Russia and the metallurgy sector in Ukraine became the main drivers of growth in 2000–2004.

Since energy and metal production started to decline in 2004, growth in Ukraine and Russia has been buoyed by a domestic consumption boom. At the same time, the role of domestic production in satisfying domestic demand has largely decreased, making room for imported goods. Although rapid import growth gives the impression that the role of resources and metal product exports has diminished, economic growth in 2002–2004 would have been very small in the absence of strong export trends in the natural resource sectors in Russia and the metallurgy industry in Ukraine. The other positive effects were brought about by simplified tax schemes that boosted small firms from the shadow economy into the official one.

The impressive export performance intensified the internationalisation of Russian and Ukrainian companies into world markets and forced them to adopt international standards of doing business. After the economic crisis of 1998, good corporate governance and transparency became essential. The case studies on the Russian and Ukrainian oil and gas sectors confirm the ongoing implementation of corporate governance norms, and as the business and ownership structures became more transparent, international book-keeping norms were launched, and companies and corporations began to develop long-term strategies.¹⁴ It also meant that the use of illegal “shadow” resources to ensure financial capital and market benefits by means of state capture or corruption was scaled back.

The current growth trend has an eclectic character built upon exports of intermediary, semi-finished and low-quality goods. The efficiency of the basic exporting industries is low and energy wastage is high. At the same time, the employment of new technologies and the modernisation of production capacities are important for competitiveness on world markets. Because the state is not able to supply financial resources to local corporations, private investment, local or foreign, is required.

13 The output data in Russia and Ukraine present a distorted picture of the economy. Due to transfer pricing, the large scale of GDP generated by natural resources and metallurgy sectors is not reflected in the accounts of the extraction and producing companies, but in the trading ones. As a result, export-oriented industries are under-estimated and trade is over-estimated in Ukrainian and Russian national accounting.

14 Heinrich, Andreas: Globalisierung und Corporate Governance. Russlands Erdöl- und Erdgassektor, in: Osteuropa, 2004 (vol. 54), No 9–10, pp. 355–365; Zheka, Vitaliy: Corporate Governance and Firm performance in Ukraine. CERT Discussion Paper No. 5, 2006, May.

This is an even greater challenge for Ukraine, as metal products are more vulnerable than oil and gas. In 2004, Ukraine's steel industry reached one of the highest levels of capacity utilisation, 95.4%, up from 52.1% in 1998. The replacement of outdated production facilities and the increase of their efficiency are the current goals of the Ukrainian oligarchic clans, whose assets are concentrated mostly in the metallurgy sector. This challenge is accelerated by the forecasted fall in prices for metal products after 2008, rising prices of imported Russian energy and higher transport costs. Unsurprisingly, the investment rates in the steel sector grew by 43% and 56% in 2004 and 2005, respectively.¹⁵ Nevertheless, Ukrainian metallurgy attracts less investment than the Russian steel, oil and gas industries. In addition, Ukraine's metallurgical exports are permanently under anti-dumping investigations.¹⁶ To escape high anti-dumping fines as well as a discriminatory attitude, Ukrainian metal companies are striving for market status for their individual enterprises as well as for Ukraine as a whole. They are also expanding globally. The companies are thereby trying to improve their access to international capital markets and increase the capitalisation of their assets. These actions are leading to more financial openness, the disappearance of transfer pricing and the reaping of taxable profits.¹⁷ Thus, in the second phase of transition, entrepreneurs began to demand solid formal institutions that could secure their capital regardless of who happened to be in office. Formal institutions can secure property rights and encourage sustainable growth in the best way. State rulers, who are in a position to act as arbiters and change and implement these institutions, are beginning to play a very important role.

By and large, both Russian and Ukrainian oligarchic clans, whose business was becoming more and more export-dependent, were pressed to implement international standards of transparency and corporate governance. It seems that the Ukrainian clans are more aware of these requirements.

Emergence of an arbiter

A good government that enforces order in the country and protects property rights and business contracts is essential for the sustainable growth of the tycoons' empires and the countries in general. Sound corporate governance requires sound political governance.¹⁸ "Windfall" factors such as the real depreciation of the hryvnia and rouble have disappeared, the boom in the metal industry is slowing down, and oil and gas prices seem to have stabilised. Therefore, the current growth seems to have deeper structural and institutional roots. The quality of a country's institutions affects its ability to achieve sustainable growth and be successful in its long-term development efforts. Figure 3 shows the positive development of institutions in Russia and Ukraine since 2000.

The separate analysis of three institutional dimensions reveals different speeds in the progress of political, executive and legal institutions. The development of political institutions in Ukraine and Russia was more advanced during the early stages of transition. If one takes into account the fast transition from socialism to democracy, with the accompanying change of formal rules and laws (albeit lagging in implementation), the differences in institutional dimensions seems to be quite plausible. The influence of informal rules impedes the implementation of newly established formal rules, a fact which becomes evident in the estimation of administrative and legal institutions. The improvements with respect to institution building in the following years were primarily made in the executive and legal areas. This trend was even stronger in Russia than in Ukraine.¹⁹ However, Ukraine radically improved the quality of its institutions due to some

15 The Ukrainian Cabinet Resolution, "On the State Programme for Developing and Reforming the mining and metalworking for the period until 2011". Kyiv, 2004, July 28.

16 From 1993 to 2001, there were 43 anti-dumping cases. More in: Eremenko, Igor / Lisenkova, Katerina: The Impact on Ukraine of Joining the WTO: Subsidies vs. Antidumping in Ferrous Metallurgy. CERT Discussion Paper No. 11, 2004, December.

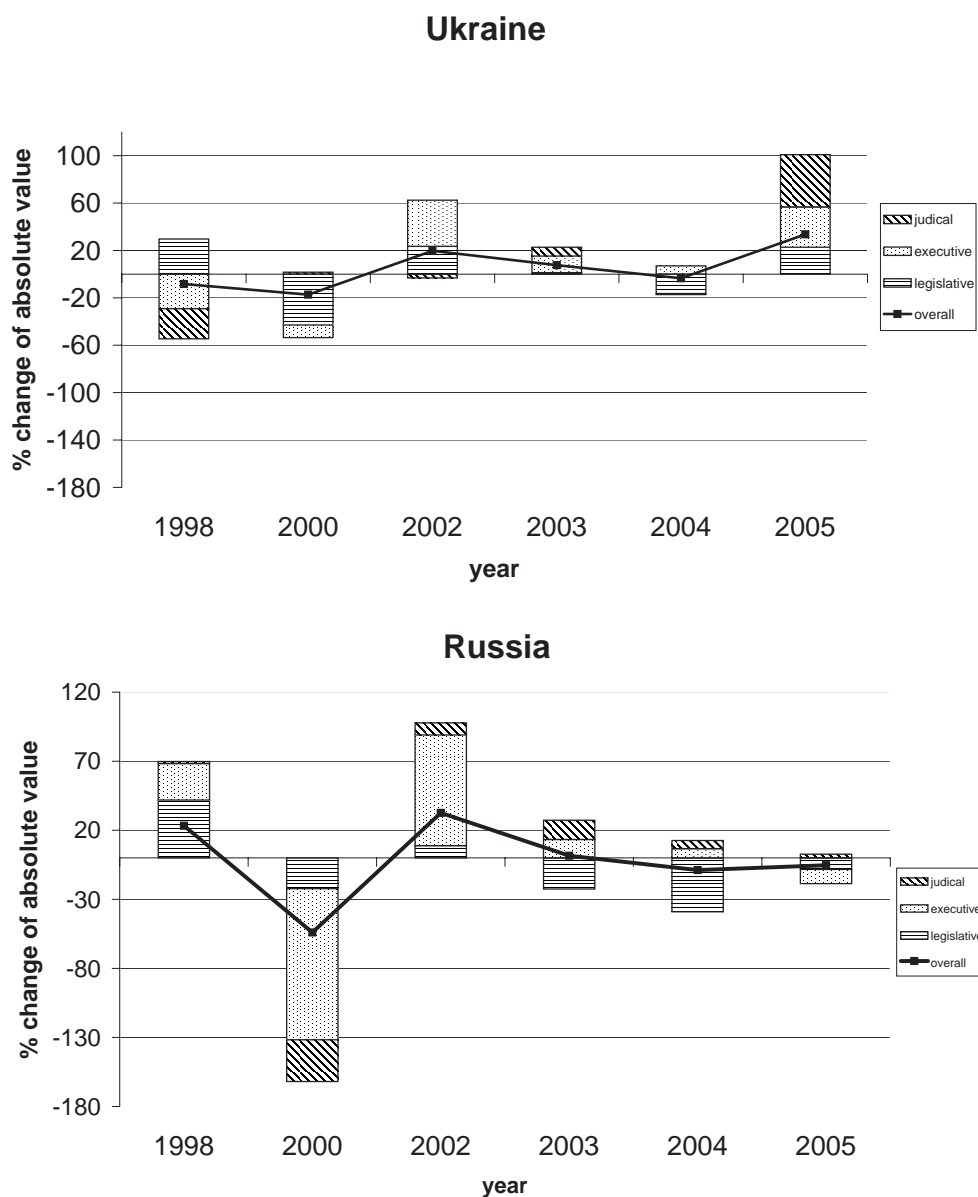
17 Ukraine's metal companies own metal works, wholesalers and retail metal traders in Europe.

18 Oman, Charles / Fries Steven / Buiters, Willem: Corporate Governance in Developing, Transition and Emerging-Market Economies, OSCE Policy Brief No. 23, 2003.

19 Administrative institutions in Russia are better developed than political institutions. However, political indicators take

structural changes made following the Orange Revolution. These developments indicate that institution building CIS-style may be different from the “western” concept of good governance.

Figure 3. Progress in institution building in Russia and Ukraine, 1996–2004



Source: World Bank Governance Indicators; own calculations.

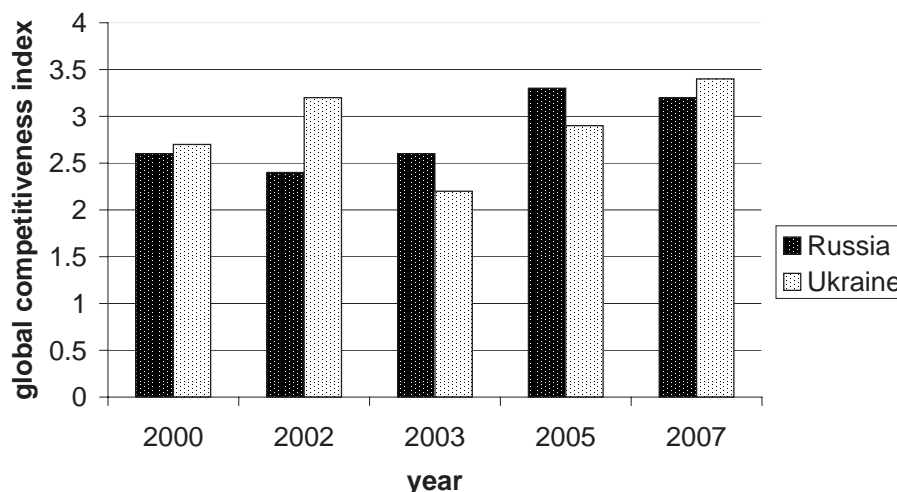
Particular attention is devoted to the institution of property rights. The Global Competitiveness Report shows a similar emphasis as the World Bank Governance Indicators. Until 2004, Russia boasted the most secure property rights (Figure 4).

In the era of Presidents Kuchma and Yelsin, property rights were secured with the informal rules applying to networks between politics and the economy. The essence of these informal rules was that “the security of a financial empire depends on the position of your patron in state bodies”. This kind of strategy, based on patronage protection, was extremely short-sighted. If a political patron lost power, the financial empire of the oligarchic clan dependent upon this patron ran the risk of going under. As oligarchs had accumu-

democratic institutions as an instance of good governance. Thus, the quality of political institutions has a poor rating in countries with authoritarian regimes.

lated their capital illegally, they could not claim the protection of the formal laws and were vulnerable to prosecution by the state, which could favour the interests of a rival business group. Even having the same regional origin did not guarantee continued prosperity and security of the property rights for the accumulated capital. Additionally, maintaining patronage networks was extremely costly.

Figure 4. Security of property rights in Ukraine and Russia, 2000–2007



Source: The Global Competitiveness Report

The political systems of Russia and Ukraine belonged to the so-called “hybrid” regimes stuck in the “gray zone” between democracy and authoritarianism. The terms used to describe these hybrid regimes in the FSU – “imitative”, “façade-like”, “pseudo” – suggest a rather unsuccessful mix of democratic and authoritarian features. What distinguishes these countries is the presence of an arbiter – a dominant state actor able to monopolise state power without making compromises with other actors. The holder of this office is also capable of closing the “structural holes” among the various branches and to establish the balance and stability in the distribution of power among oligarchic clans. The presence of such an arbiter is also fundamental for sustainable economic growth. Hare contends that a state that holds a monopoly over the means of enforcing order can protect property rights and business contacts, levy taxation and manage the public budget.²⁰ Carothers calls a political system without a dominant actor “feckless pluralism”, whereby a significant amount of political freedom is combined with the floating of power between different political groupings.²¹ In such circumstances, the state remains a weak actor. Burt argues that political systems like these are characterised by “structural holes” – which can be exploited by other actors to their own advantage – between state bodies.

The syndrome of “feckless pluralism” was visible during the Kuchma era in Ukraine. His policies were seen as highly corrupt, clan-dominated and less than beneficial for society as a whole. Kuchma’s “divide and conquer” strategy consisted of the perpetual rotation of persons in state government. Additionally, he appointed representatives of rival oligarchic clans into offices with comparable degrees of power.²² In such a way, he thwarted the rise of potential internal rivals. However, the regular circulation of officials with various clan loyalties meant a high degree of instability and insecurity vis-à-vis accumulated assets and provided fewer incentives for investors.

20 Hare, Paul: The Political Economy of Growth and Governance. Paper presented at the CASE Conference, “Winds of Change: The Impact of Globalization on Europe and Asia”, Kyiv, March 23–24, 2007.

21 Carothers, Thomas: The End of the Transition Paradigm, in: *Journal of Democracy*, 2002 (vol. 13), No.1, pp. 5–21.

22 The offices of the head of the Presidential Administration and prime minister were objects to be exchanged between Kyiv’s, Donetsk’s and Dnipropetrovsk’s clans.

The struggle for a dominant position started in Russia while Yeltsin was still in office. President Putin later successfully closed “structural holes” between legislative, executive and judicial branches, and established a political system of “dominated-power” in Russia.²³ It is not exactly clear whether Putin represents the interests of a single clan (often called “siloviki”) or plays the role of an independent arbiter, securing the current distribution of power between oligarchic clans. However, the success of his reforms confirms their congruence with the preferences of the Russian clans.

In order for a strategy of confrontation with an incumbent to be feasible, the following conditions are necessary:

- widespread dissatisfaction with the current political regime among the population, based on the perceived lack of individual economic well-being;
- a free media to inform citizens about electuary falsifications and to mobilise the masses for demonstrations;
- a perceived probability of avoiding punishment in the worst-case scenario, based upon previous “defections” in the “principal-agent” relationship .

The paper identifies the following results:

(i) In the 1990s, Soviet legacies shaped the actors and their preferences. However, as the clans became more and more integrated into the global economy, they were forced to follow international standards of doing business. Additionally, the demands of international markets changed over time. After the 1998 crisis in Russia, transparency and good corporate governance gained importance.

(ii) The behaviour of elites also reflects learning from the transition experiences. Initially, elite groups preferred to avail themselves of informal practices and individual economic privileges. However, having accumulated properties and capital, they became owners, and therefore became interested in the security and sustainable growth of their empires. The existing patronage relationships were highly unstable and could not fulfil these new preferences properly.

(iii) The oligarchic clans in both countries are evolving from “roving” to “stationary” bandits (Mancur Olson). Under the pressure of globalisation, which constrains their rent-seeking possibilities, and due to the instability of the informal networks, they have changed their preferences. Now, they are striving for good and secure state governance. However, due to differences in the sources of profits and economic rents, rent-seeking for the Ukrainian clans was limited through anti-dumping measures aimed at their metal products. In addition, higher oil and gas prices led to higher production costs and reduced competitiveness. These factors forced the Ukrainian clans to adapt their behaviour faster than their Russian counterparts.

(iv) The state should play the role of an arbiter capable of protecting property rights and guaranteeing stability. While Putin consolidated state authorities and created a system with a “dominating power”, Kuchma pursued a “divide and conquer” policy in circumstances of “feckless pluralism”. The relatively free media and the population’s dissatisfaction with its political ruler as well as the abandonment of punishing “defections” helped the Ukrainian clans to develop a confrontational strategy towards the incumbent regime.