



OCGG Economy Section

Advice Program
Russian Economic Policy

Governance Area
Russian Competitiveness Policy

Russian Capitalism

by André Nilsen

Rosneft, the Russian state controlled oil company, is due to list on stock exchanges in Moscow and London on Friday 14 July 2006. It is aiming to raise \$10bn-\$11.7bn, making it one of the largest ever initial public offerings and valuing the company at up to \$80bn. Is the float a concrete sign that Russia finally is embracing the neoliberal reforms that American economists and bankers have tried to

impose on the country since the early 1990s? Not so fast.

In the IPO prospectus, Rosneft has been obliged to list all the conceivable risks it faces. One can only commend the company for its honesty. One risk it lists are possible legal liabilities of at least \$14.7bn arising from the fact that its main production asset, Yuganskneftegaz, was acquired through rather kafkaesque

MAIN POINTS

The Rosneft IPO has focused attention on the state's involvement in the economy in Russia. Contrary to criticism, Putin is embracing the capitalism model that is best suited to the country and most likely to sustain comparative advantages. He should now embed it in rule of law to make sure it stays.

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government orchestrated proceedings in 2004 following the forced break-up of Yukos, the private oil group of Mikhail Khodorkovsky, the jailed oligarch. Another risk that is mentioned stems from the fact that the Kremlin controls the board, six out of nine directors being officials of the government, suggesting maximizing shareholder value and protecting minority shareholders may occasionally have to take a backseat to political objectives.

Rosneft is not however a unique case of state involvement in the economy in Russia. Under Vladimir Putin the state has increasingly used a number of public mechanisms to steer the economy.

One set of tools consists of state financing, ownership, and control, government orchestration of or intervention in corporate restructurings, and industrial policy to build national champions. They ensure that the main corporations play coordinating or supporting roles at different levels.

At the commanding heights are a handful of conglomerates that function as transformative agents. Gazprom, one of the largest companies in the world, holds one-sixth of global gas reserves having bought Sibneft but also owns television channel NTV, newspaper Izvestia, finan-

cial institution Gazprombank, and engineering company OMZ, with many of the key assets acquired from former oligarchs. Rosoboronexport, the state arms export agency, despite owning no shares controls car manufacturer Avtovaz, possibly to be merged with vehicle makers Gaz and Kamaz, and is despite the resistance of the private owners about to take over titanium producer VSMPO-Avisma as well as the two largest navy shipyards.

At the intermediate level are a number of corporations in the making that will dominate each their strategic sector. Tvel, already controlling Priargunsky, may become a national champion in nuclear fuel and engineering through the new subsidiary Atomenergomash and acquisition of Power Machines and OMZ. A national champion in energy transport may be created by merging Transneft-eprodukt and Transneft. A national champion in mining and metals may be created by merging Alrosa and Norilsk Nickel. United Aircraft Corporation is being created as a national champion in aerospace by merging Sukhoi, Irkut, MiG, Ilyushin, Tupolev, and Yakovlev. Aeroflot is set to become a national champion in air transport through the acquisition of several regional airlines. And a national champion in shipping

may be created by merging Sovkomflot and Novorossiysk Shipping.

These will join the ranks of giant state companies including Russian Railways in train transport, Vneshtorgbank in finance, Svyazinvest in telecoms, Almaz-Antey in defence. And in addition there are a number of privately held companies that are state loyal such as Lukoil, TNK-BP, and Surgutneftegaz in energy and Rusal in aluminium.

Another set of tools are constituted by political-managerial elite networks and career paths. They weave the state and the main corporations closely together.

Igor Sechin is deputy head of presidential administration, former St Petersburg colleague of Putin, reputed former KGB colleague of Putin, and chairman of Rosneft. Dmitry Medvedev is seen as possible successor to Putin, first deputy prime minister, former head of presidential administration, former St Petersburg colleague of Putin, and chairman of Gazprom. Alexei Miller is former St Petersburg colleague of Putin and CEO of Gazprom.

Sergei Chemezov is close friend and former KGB colleague of Putin and chairman of Rosoboronexport. Andrei Belaninov is head of customs, former KGB

colleague of Putin, former chairman of Rosoboronexport, and former chairman of Novikombank founded by the Association of Foreign Intelligence Veterans.

Alexander Zhukov is deputy prime minister and chairman of Russian Railways. Vladimir Yakunin is former St Petersburg associate of Putin and CEO of Russian Railways. Igor Shuvalov is aide to the president and chairman of Sovkomflot.

Vladislav Surkov is deputy head of presidential administration and chairman of Transnefteprodukt. Viktor Khristenko is industry minister, chairman of Transneft, and chairman of commission to create United Aircraft Corporation. Viktor Ivanov is aide to the president, former KGB colleague of Putin, chairman of Aeroflot, and chairman of Almaz-Antey.

Sergei Prikhodko is aide to the president and chairman of Tvel. Alexei Kudrin is finance minister, former St Petersburg colleague of Putin, chairman of Alrosa, and chairman of Vneshtorgbank. And Leonid Reiman is telecoms minister, former St Petersburg associate of Putin, and chairman of Svyazinvest.

The Financial Times has found that eleven presidential administration members held six chairmanships and twelve fur-

ther directorships and that fifteen senior government officials held six chairmanships and twenty four other boards seats.

So what to make of it all? What is the best way to understand and assess the nature, dynamics, and developments of Russian capitalism? Comparative political economy has developed sophisticated frameworks for analyzing and evaluating different types of economies.

One key point is that it is less helpful to talk about “degrees of capitalism” than “varieties of capitalism”. Broadly speaking there are three different models of capitalism. These are distinguished from each other by the type of mechanism that coordinates the economy and its subsystems of corporate finance, industrial relations, corporate governance, technological development, and vocational training. The neoliberal model, which for example the US and the UK economies correspond to, is governed by markets through competition. The coordinated model, which for instance the German and Swedish economies approximate, is underpinned by private non-market institutions that facilitate cooperation. And the public model, which most notably the French economy resembles, is directed by public institutions exercising political control.

Another and perhaps more surprising key point is that these models over time perform more or less equally well. Despite the current widespread belief, there is actually no consistent and compelling evidence that the neoliberal model is superior. That this view nonetheless has become the paradigm of economic research, policy making, and media commentary these days is due partly to misguided thinking and partly to the influence of the special interests that stand to gain from it such as the US government and American institutional portfolio investors. The data however suggests that over time the coordinated and public models are equally good. The reason is that the different models yield different but equally good comparative advantages.

So what we see in Russia under Putin is nothing new or unusual or bad. Public institutions coordinating the economy are long standing common features of French capitalism that have been integral to its comparative advantages.

Russia went from under communism being a completely non-capitalist economy via under Yeltsin being a half-built neoliberal capitalist economy to under Putin becoming a full-fledged public capitalist economy. A bumpy road to be sure. Few people have managed to drive safely all

the way. But although one can occasionally question Putin's driving skills, as with the Yukos case, it is important to emphasize that there is nothing wrong with his destination of a public capitalist economy.

Indeed Putin has showed great vision and courage in steering Russia towards the model that is best suited to Russia's history, culture, and society and therefore most likely to sustain unique and lasting comparative advantages. He should now show even greater wisdom and audacity in recognizing that even a model in which the state plays an active role in the economy needs to be based on rule of law.

Putin's break-up of Yukos was probably no more dubious than Khodorkovsky's construction of the company in the first place but correcting one wrong with another wrong is not a good way of achieving justice. Equally importantly, however, embedding the public governance of the economy in rule of law will make it harder for anyone to reverse his achievements.

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