

PERFORMANCE IN PERSPECTIVE: FIRMS, OLIGARCHS AND PUTIN

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Introduction

What difference does it make how much hypothetical money I have, if I have problems with the authorities?

Al'fa Group founder Mikhail Fridman (Vedomosti, October 12, 2004)

Before Putin's first term as President of the Russian Federation, 2000-2004, personal relations instead of business relations dominated the connection between the Kremlin officials and the Russian oligarchs. These oligarchs played an important role in the economic transition and the political reforms after the break-up of the Soviet-Union.

With the election of former KGB officer and Prime Minister Vladimir Putin the economic policy changed and Russian people hoped that the Russian Federation was going to be rebuilt into a more modern and well-functioning society. After his election, Putin was confronted with a system that contained enormous flaws wherein few parts of Russian society were functioning. Legislation, government institutions, economy and specifically energy policies were threatened by Russia's own policy inconsistency². Meaning that policies were not always an extension of laws, but the opposite. Moreover, both moral and social values were deteriorating. From then on, the Putin administration tried again to control society, which mainly meant regaining control over the former privatized companies and replacing Yeltsin's oligarchs with Putin's political friends as to recuperate Kremlin's control.

This thesis aims to identify the key issues in the dynamic interplay between the oligarchs and Putin. How does Putin's attitude towards the powerful oligarchs differ from Yeltsin's mind-set? Who were these powerful oligarchs and which companies did they own? How can we define the relation between the powerful fractions in Russian society, i.e. the Kremlin, individual oligarchs and oligarch firms? Is any change measurable within these oligarch firms by looking at the performance of the oligarch firms after Putin came to power? These above mentioned subquestions lead to the main research question, which is as follows;

¹ D. Herspring (2003), p 1.

² For A. Aslund 'Russia's Energy Policy: A Framing Comment', p. 321, and V. Milov 'Russian Energy Policy, 1995-2005', p 311.

³ D. Kotz and F. Weir (2007), p 8.

How did Putin's inauguration change the relation between the Kremlin, the oligarchs and oligarch firms, and how did his equidistance doctrine affect the firm performance of oligarch owned firms?

According to the literature, oligarchs and their companies are a positive actor for the development of a Russian market-based economy as these companies are seen as the only counterweight to the Russian bureaucracy.⁴ Moreover, the performance of oligarch owned companies is much higher than state and private (non-oligarch) owned companies. Especially companies operating in the resource sector perform extremely well when owned by oligarchs.⁵

This thesis contributes to the existent literature on oligarch studies in a number of ways. First, a limited timetable is used as to restrict the wide range of theories and ideas on oligarchs and their role in the Russian society. Second, an insightful examination is provided of the underlying factors and results of performance of oligarch owned companies after Putin's 'equidistance doctrine'.

Following the literature, the research question will be answered by taking a close look at the Russian resource sector, as this thesis hypothesis that the Russian resource industry is the main connection between the oligarchs, Putin and the oligarch owned firms. After examining the research question the main finding of this thesis is that the changed attitude of Putin has had enormous influence on the relation between the oligarchs and the Kremlin. Oligarchs who did not stick to the new rules could count on severe objections from the Kremlin. The case study showed that this troubled relation has negatively influenced the performance of these oligarch firms as former privileges have disappeared.

The structure of this thesis is as follows; the first chapter starts with a short outline of different interpretations scholars have given on the role of Russian oligarchs in the Russian society. Were the oligarchs helpful for economic and political change, or did the oligarchs only use Russian society for their own benefit. Additionally, the model of Russian corporatism is being discussed as it shows the connection and interdependence between the government and corporations. Chapter two gives an overview of the former economic systems and political structures, and it shows how they changed during Putin's presidency. The implications of Putin's new

⁵ S. Guriev and A. Rachinsky (2005), p 143.

⁴ S. Guriev and A. Rachinsky (2005), p 131.

policies and the results of these policies are also outlined in this chapter. We will also briefly discuss President Yeltsin's privatization process after the break-up of the Soviet Union. The definition of the Russian oligarchs and their personal enrichment are examined in chapter three. Additionally, this chapter surveys the expanding attitude of the Kremlin against the oligarchs. Why did Putin want to put all the oligarchs at the same distance of the Kremlin and how did he accomplish that? Chapter four will assess the Russian resource sector in order to give a clear example of the implementation of Putin's 'changed attitude'. Is there evidence in the resource sector that exemplifies a drastic change in the situation of the oligarchs after Putin became President? Chapter four also outlines which companies were very influential and profitable. Chapter five examines three selected companies and assess their firm performance in order to show how Putin's equidistance doctrine influenced this performance. The conclusion gives a summary of the outcomes of this thesis, and it will also suggest recommendations for further research.

Chapter I

Theoretical Framework

At the basis of President Putin's transformation process of the Russian society, is Yeltsin's restructuring of the political and economic environment. With the election of Putin as President of the Russian Federation in 2000, Putin's first priority became the restoration of a strong state by regaining the economic and political control Yeltsin had lost. The restoration of the federation was shaped by Putin's 'new Russian federalism', which can best be described as strengthening the authority of the federal government and bringing regional laws in accordance with federal legislation. ⁶ Before researching how Putin has changed political structures and the economic system it is important to give a short introduction on the theories scholars have developed on the political and economic influence of the oligarchs, as they are the ones that profited mostly from the lack of legislation and the business opportunities during the Yeltsin period. The relation between the oligarchs and the Russian government is subject of the model of corporatism. In short, corporatism can best be described as an arrangement or partnership between the state and social groups as they share the same interests⁷. It is thus useful to assess the model of Russian corporatism as it gives insight into the relation between these two fractions. In this chapter we try to explain the role corporatism has played in Russia's economy and politics. The questions and considerations mentioned above will be discussed in the next paragraphs.

In the first year of Putin's presidency Russia seemed to be stabilizing as Putin's interests were balancing between give-and-take. However, according to Archie Brown, Putin soon changed into an independent transactional leader, who began to be more 'take' than 'give' in the Kremlin's political bargaining.8 After the first year of Putin's presidency, his shift in leadership was accompanied by a policy move altering the relation between the Kremlin, the regional bosses and business elite. Oligarchs, as will be defined later more detailed, can be on the one hand regional bosses and business elite groups. On the other hand however, oligarchs can also be Russian political and economic players (who receive a wide-range of

⁶ A. Brown (2001), p 375. ⁷ P. Kubicek (1996), p 29.

⁸ A. Pravda (2005), p 25.

criticism). Some scholars recognize the oligarchs as the engine of the Russian economy; other scholars blame oligarchs for the flaws of the Russian privatization process. The first group of scholars are positive about the performance of the oligarchs and defend them, and the second group of scholars blame them for criminal activities. The arguments that support the views of both groups, are shown in the paragraphs below.

First, scholars such as Anders Aslund, Peter Boone, Denis Rodionov, Andrei Rachinsky and Sergei Guriev⁹ perceive the performance of the oligarchs i.e. their companies as a positive development for the Russian economy. They argue that oligarch ownership must be seen as positive as it is proven that oligarchs can be more efficient owners than other domestic Russian owners of Russian enterprises. Guriev and Rachinsky show that the productivity growth in 2002 is much higher in oligarch-controlled firms than in firms controlled by other private domestic owners, or the state. Of Moreover, Guriev and Rachinsky consider the oligarchs to be 'the only current feasible counterweight to the predatory and corrupt Russian bureaucracy.

In accordance with these statements, Benjamin Maury and Eva Liljeblom argue that the role of oligarchs in the Russian transformation process is determined by the economic relation between the state and the oligarchs. The performance of oligarch companies within the Yeltsin and Putin era is researched in their article. Their conclusion is primarily based on economic arguments stating that oligarch owners are in general better performers then firms that have other owners then oligarchs. Thereby they suggest that the collision between big business and politics (Yeltsin period) has a negative influence on the firm's performance (this is the case for all kinds of ownership). During Putin's presidency, the state and the oligarchs were more separated which had a positive result on the firm performance, as oligarch firms outperformed their predecessors.¹²

Andrei Shleifer, professor of Economics, and Daniel Treisman, professor of Political Science, both have researched the three most legendary Russian oligarch cases; Khodorkovsky, Berezovsky and Potanin, and concluded that their companies Yukos, Sibneft and Norilsk Nickel performed remarkably better than companies that stayed under state control, such as Gazprom and UES (an electricity company) or

⁹ A. Aslund (2004), Boone and Rodionov (2002) and Guriev and Rachinsky (2005)

11 S. Guriev and A. Rachinsky (2005), p 131.

¹⁰ S. Guriev and A. Rachinsky (2005), p 143.

¹² B. Maury and E. Liljeblom (2007), pp. 28-29.

even Lukoil.¹³ According to the scholars that have already been mentioned, oligarch ownership is also positive as oligarchs are visible in their new role as economic investors. The fortunes they make are also re-invested primarily in their companies where the Russian economy benefits from. Thereby, some oligarchs also tend to lobby for the rule of law and the establishment of proper functioning property rights (although this mostly benefits their own needs).

In his book Russia's Oil Barons and Metal Magnates (2006), Fortescue outlines that although Anders Aslund is convinced the oligarchs stripped the assets through the privatization deals and other corporate governance abuses wherein they kept the profits for themselves, but Auslund also describes the oligarchs as economically highly useful.¹⁴ Most of the enterprises that where involved in the loanfor-share deals did extremely well afterwards and Aslund even defends them for their involvement in these schemes¹⁵. According to Aslund it is better to describe the oligarchs as a product of the economic environment of that moment; 'the emergence of oligarchs is a natural consequence of the prevailing conditions¹⁶. Thereby, very large enterprises could not have been developed without the oligarchs.

Second, scholars such as Marshall Goldman, Joseph Stiglitz and Karla Hoff¹⁷ argue the opposite, as they are convinced that the role oligarchs have played in Russian politics and economy is mainly negative. The arguments they use are primarily political arguments in contrast to the first group of scholars that used only economic arguments. According to the second group of scholars, the oligarchs have weakened democratic institutions by their political influence. Moreover, oligarchs caused enormous inequality as they profited from the privatization process and the loans-for-shares deals during the Yeltsin era which almost everybody saw as 'stealing from the state'.

Neither Archie Brown nor Richard Sakwa see the Russian oligarchs as positive or negative. Brown argues that Putin targets Russian oligarchs, as they have not passed the 'loyalty test'. 18 According to Brown, the change of the political and economic environment has created opportunities for the oligarchs to develop their businesses partly through the economic chaos and the lack of legislation. This is not

¹³ A. Shleifer and D. Treisman (2005), p 161.

¹⁴ S. Fortescue (2006), p 18.

¹⁵ A. Aslund (2005), p 10.

¹⁶ A. Aslund (2005), pp. 7-8.

¹⁷ M. Goldman (2003), K. Hoff and J. Stiglitz (2004)

¹⁸ R. Rose, W. Mishler and N. Munro (2006), p 66.

positive or negative, but just a consequence of the changing situation, wherewith Brown agrees with Aslund. Sakwa concludes his article 'Putin and the Oligarchs' with 'A new model of political economy emerged in which the state advanced political claims that were historically anachronistic, namely, that while a capitalist economy was welcomed, the political demands of the capitalist class were to be constrained.' ¹⁹ The quotation explains that Sakwa does not lay the emphasis on Putin's project of controlling the threatening oligarchs on the one hand and the resource based companies on the other, but Sakwa emphasises the trend of creating a controlled democracy. In this 'phoney democracy' Putin sought to regain control over a number of state company holdings in key areas. And as we have already seen, the trend Sakwa describes is negative for both economic growth and democracy itself, as oligarch companies are performing better and profiting from the lack of legislation.

All scholars we have mentioned agree that there is a close connection between the state and the oligarchs. According to William Tompson this relation exists because both the government and the big business oligarchs have intertwined interests.²⁰ This connection is being discussed within the perspective of Russian corporatism. How can we characterize the relation between the state and enterprises? Why does the model of Russian corporatism give a helpful explanation for understanding this relation and the implications of it? The following paragraph interprets the theory of 'the Oligarchical Model of Russian Corporatism'²¹.

1.1 Russian Corporatism

With the collapse of the Soviet Union the market economy was not rebuilt *on* the ruins of the Soviet economy but also *from* them. This means that the interwoven ties between the state and business groups did exist and still exist.²² We shall later see how these ties or arrangements between state and business groups can affect economic reforms and/or growth and what implications this may have had for the companies that have been selected and examined in chapter 5.

¹⁹ R. Sakwa (2008), p 190.

²⁰ W. Tompson (2005), p 172.

²¹ A. Brown (2001), p 259.

²² P. Kubicek (1996), p 29.

In the last decade there has been an increasing fusion of state and business interests and power. This fusion, mostly in the resource sector, has been carried out in two ways. First, government officials were replaced on corporate boards of firms closely connected to the Kremlin.²³ Second, mutual interest of the Russian state and powerful corporations resulted in unofficial deals and growing intertwined interests. In order to describe this trend, the model of corporatism could be used, as it places the oligarchs in the Russian economic and political structure and makes a connection to the role of the Russian government in these structures.

How can we define corporatism and what does the model of corporatism imply?

Corporatism may thus be conceived as a non-competitive form of interest representation in which officially sanctioned groups have guaranteed access to processes of policy formation and implementation but are subject to controls on their behavior.²⁴

The definition of corporatism, as mentioned above, can be seen as the classical definition. It defines the way of interest representation wherein only officially sanctioned groups have access to the policy formation and implementation. However, the model of corporatism needs some adjustments in order to be useful for this thesis. In the case of Russia; the policy formation and interest representation are not only performed by officially sanctioned groups (government officials), but also by "unofficially" sanctioned groups (people who gained political influence, which is permitted or not-counteracted by the government, through their economic status). The unofficially sanctioned groups that do have (although unofficial) access to policy formation and implementation are mostly the wealthy and economic powerful oligarchs. They have mutual economic interest with the Russian government which they use to obtain also political access. Here we can see that these mutual interest results in an agreement wherein the governments profits from the wealth of the oligarchs companies and the oligarchs benefit from the political access they acquired. For this thesis the group that has unofficial political power and acquired unofficial access to political power via economic wealth, is to be focussed on.

The corporatist model is present in various countries and in different forms; however it is mostly linked to the fascist and oppressive systems of Latin America.

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²³ P. Rutland (2008), pp. 5-6.

²⁴ P. Kubicek (1996), p 29.

The 'oligarchical model of Russian corporatism', as part of the corporatist model, determines a present connection, which consists of mutual agreements between the state and the national economy; dominated mostly by financial-industrial groups and business conglomerates. In his article *Variations on a Corporatism Theme: Interest Associations in Post-Soviet Ukraine and Russia* (1996) Kubicek argues that the model of corporatism can be described as an arrangement or partnership between the state and social groups, as they have the same interests.²⁵ Within this model the arrangements that are being made (for example the loan-for-share deals) have a special role, because they show a conscious attempt by both sides (financial conglomerates and the state) to extract the maximum political rents and it is part of the redistribution of state property, mostly to the benefit of the oligarchs.

To sum up, this model of Russian corporatism outlines the mutual understanding between the state and the wealthy individuals that were dominating the Russian economy. As we will see in the next paragraphs, the understanding became troubled with Putin as President. He decided to change the rules and break through this mutual understanding, in order to make the state less dependent on these individuals and create an environment in which he could increase state control. President Putin's reassertion of state control, the changed attitude towards the oligarchs and the consequences of this change are outlined in chapter 2 and 3.

²⁵ P. Kubicek (1996), p 29.

Chapter II

Economic System and Political Structures in Russia

What were economic developments before Putin's presidency, and how was the political structure in Russia? How did this change with Putin becoming the new President? These questions will be discussed in this chapter.

We can interpret the fall of the USSR in two ways. First is to state that the fall of the Soviet Union is a process of slow change, as several anti-communist activities were already developing during the Soviet period. Second is to argue that this moment of change was a radical break with the past, as very sudden the ideological, institutional and economical framework collapsed. In this thesis we interpret this moment of change as a radical break, by using the word 'fall' as it implies a sudden and quick change in an existing situation.²⁶ Unfortunately the radical shift did not create a strong change within society, as we will see in the next paragraphs.

The fall of the USSR forced the Russians to redefine their identity and policies concerning the economic and political structures. This redefinition was difficult and caused many problems because Russia had never been a nation-state and could not revert to its past traditions. 1991-1993 was the first period of Russian independency and it can be seen as the starting phase of democracy, but people had communism still fresh in their minds. During this period Sakwa describes Russia as a 'phoney democracy'.27 The term 'phoney democracy' refers to the absence of elections from 1991 to 1993 when the Yeltsin government was formed, and it refers to the undemocratic political environment. Moreover, the conditions of the Russian economy were characterized by contradictory logics of Russian transition, as this shows on the one hand signs of development towards Western-style capitalism, and on the other hand towards a phoney democratic oligarchy with new Russian corporatism as an important element.²⁸

From the inauguration on July 10, 1991, Yeltsin created a Presidential administration and he defended a strong executive authority. But he also recognised

²⁷ R. Sakwa (2008), p 44.

²⁶ R. Sakwa (2008), p 35.

²⁸ G. Yavlinsky (1998), via http://www.foreignaffairs.org/19980501faessay1390/grigory- yavlinsky/russia-s-phony-capitalism.html, visited on January 12, 2009.

the need for the separation of powers, which led to the idea of "delegated legislation' in which the government is allowed to rule for a time through decrees with the force of law'.²⁹ After coming to power Yeltsin neglected his supporters as he freed himself from his promises of bringing democracy to the Russian Federation. This led to Yeltsin's loss of credibility, as he did not accomplish his earlier promises.

In order to increase his support, Yeltsin embraced the idea of segmented regionalism³⁰, whereby the regions and the republics were given privileges in return for loyalty to the Kremlin. This helped Yeltsin to receive political support from the regions, because regional politicians were obviously in favour of this idea as they saw that their republics almost turned into small sovereign fed rational subjects. Through this segmentation Yeltsin was able to expand his shrinking clique of followers. But giving privileges in exchange for gaining support, showed Yeltsin's return to the system of privileging which he had always waived from and which was "normal" during the Soviet period.

The period of 'phoney democracy' should have ended with the adoption of the Russian constitution, which came into force on December 12, 1993.31 The constitution was a liberal document and it upheld the basic principles of democracy and defines the independence of law and the rights and duties of government institutions. With this constitution the keystone for providing a legal framework was set. But the transition gave rise to enormous political and economic chaos and made it impossible to reform the old Soviet institutions and planned economy and to implement laws. The economic reforms, carried out through the privatization process and loan-for-share deals resulted in the upcoming of oligarchs, who were able to expand their economic and political positions through the transition.³² Until the end of Yeltsin's presidency in 1999, the two most influential fractions in the Russian Federation, the oligarchs and the privileged regional governors, were openly challenging the central administration and trying to maximally increase their political and economic power. It can be said that this challenge led to a situation wherein Russia was almost ungovernable as the powerful fractions acted mostly on their own behalf striving for the most powerful positions within society.

²⁹ R. Sakwa (2008), p 43.

³⁰ R. Sakwa (2004), pp. 130-131.

³¹ R. Sakwa (2008), p 64.

³² A. Brown (2001), p 83.

With Putin coming to power drastic reforms were implemented which decreased the power of the oligarchs and the regional governors by spelling out new rules of the game and attacking the oligarchs who did not stick to these rules, such as Berezovsky, Khodorkovsky and Gusinsky. These most prominent oligarchs were part of the Yeltsin 'family' and therefore we can say that challenging the oligarchs in fact meant challenging Yeltsin's regime, which was a doubtful act, as Putin came to power with help of Yeltsin's family. Although Putin acted respectful towards Yeltsin as the former President, he completely rebuked Yeltsin's legacy and his 'family'. ³³

Putin's primary challenge to the Yeltsin institutional inheritance came in Presidential decrees and legislative proposals issued in the weeks after the inauguration. These measures were designed to accomplish what Yeltsin had been unable to achieve during his two terms in office: the establishment of an effective mechanism of control – a ruling *vertical* – over the unruly provinces.³⁴

Putin's rise to power imposed a decline in national power for the governors, but their authority remained strong in the provinces. On March 7, 2000, the President spoke to the nation and called for a dictatorship of law, with restoration of a strong and centralised government. Putin insisted on the establishment of a regime that favoured command over compromise, which means law and administration over politics. To sum up, he told the Russian people that he and his administration were from now on in charge of the Russian Federation, wherein compromises were not favourable.³⁵

As we have seen both the economic and political reforms during the Yeltsin period created the Russian Federation that Putin inherited. As it was not a super Presidential order, Putin sought to build one. Paragraph 2.1 focuses on the changing political structure with special attention to the organisation of the state in order to establish a vertical power system. Paragraph 2.2 examines briefly the developments of the economy between the end of the Soviet Union and Putin's reform process.

2.1 Changing the Political Structure

During the Yeltsin era, the new structure of the state was implemented via the adopted constitution, which mainly meant that the regions and republics had a free hand in

³³ V. Shlapentokh (2007), p 36.

³⁴ A. Brown (2001), p 88.

³⁵ A. Brown (2001), p 87.

politics as long as they did not threaten to secede. After a decade of President Yeltsin his segmented regionalism and several attempts to start the democratisation process, Putin's introduced 'new federalism'³⁶ in order to develop an effective federal system wherein the unity of Russia could be preserved. New federalism meant the implementation of a program based on 'vertical power' with the creation of seven large administrative districts controlling the eighty-nine regions (referring to Putin's hero; Peter the Great who divided Russia in eight super regions³⁷). Several measures were taken to reduce the power of the regions, such as ending the sovereignty of subnational republics, legal conformity between the regional and the national laws, all inline with the Russian constitution, the establishment of a independent national judiciary system financed only from the federal budget to eliminate dependency on regional budgets, creating institutional uniformity, changing tax-laws so that more tax revenues went to the central government and less to the regions, and the regional governors were no longer elected but appointed by the President of the Russian Federation.³⁸ Especially the appointment of the governors reduced the autonomy of the regions, but it also raised the question whether the system of "new federalism" is actually compatible with federalism as this refers to a system in which sovereignty is constitutionally divided between the government and the regions. With Putin's new federalism power is not divided among the regions but controlled by the national government. So, the introduction of new federalism is rather misleading, as it suggests a division of power, which di not take place in Russia.³⁹

Putin's reforms had a mixed result. His new federalism entailed a new relation between the regions and the centre with a more top-down political process. The reforms led on the one hand to a decrease of segmentation of power within the Russian Federation, but on the other hand it did not overcome the lack of institutions that were present in most regions. President Putin had imposed several structural reforms; however, in the end the actual implementation of the new rules had to be done by the institutions, public administration and the businesses. Bureaucratic conflicts within the regions and government institutions, and complicated public administration procedures undermined the implementation which resulted in a slow

³⁶ R. Sakwa (2008), p 266.

³⁷ R. Sakwa (2008), p 267.

³⁸ R. Sakwa (2008), pp. 267-275.

³⁹ R. Sakwa (2008), p 277.

process of state reforms. 40 Besides, the reforms are also slowed down as the ideological and cultural spirit of federalism is missing within the Russian Federation. To sum up, the idea of new federalism entailed a new philosophy of central-regional relations introduced by Putin and it did not refer to democratic separation of power. Thereby, also ideological and cultural elements of federalism caused a visible slow process of reform in Russia.⁴¹

2.2 Reforming the Economic System

Within the 1990s, Russia underwent major economic transformations, which also occurred in other Eastern European states. The economic transition signifies a transformation from a planned economy to a market economy. This paragraph discusses two aspects that were most important during the reform process of the Russian economy namely the privatization of the state companies and the loan-forshares deals.

Yeltsin trusted his reform team consisting of Yegor Gaidar, Minister of Economic Affairs, and Anatoly Chubais, to take the right decisions in order to restore and recreate the Russian economy. However, his team was not quite sure how to reform the economy. Should this be done with a rapid transition or would a gradual approach be better? To stand against Gorbachev's gradual perestroika approach, Yeltsin chose for rapidly building capitalism which meant quick economic transition.⁴² The idea of rapid economic transition was based on the process of shock therapy, which proposed a set of economic policies:

- Liberalization of prices
- Macroeconomic stabilization
- Reduction of government spending to achieve a balanced budget
- Strict limits on the growth of money and credit
- Privatization of state enterprises
- Abolition of the remaining elements of central allocation of resources
- Removal of barriers of free international trade and investment⁴³

⁴⁰ W. Tompson (2002), p 947.

⁴¹ R. Sakwa (2008), p 283.

⁴² D. Kotz and F. Weir (2007), p 159.

⁴³ D. Kotz and F. Weir (2007), p 156.

Although the state institutions and laws that were needed to successfully transform the economy were not in place in Russia, Chubais and Gaidar wanted to sell the state companies so that private businesses would be established out of former state companies. Both wanted to privatize with widespread support from the population. Therefore Gaidar and Chubais, with the approval of Yeltsin, decided to introduce the economic reform process through mass voucher privatization ⁴⁴ Voucher privatization was used for the bulk of the inefficient industry, meaning that all Russian citizens received a voucher, which they could use to 'buy' a share of stock. Chubais and Gaidar predicted that the state institutions and state functions (such as banks, property rights, ownership legislature, controlling institutions etc.) would be more effective after private property was created. However Chubais and Gaidar were wrong in their predictions and the mass privatization process had failed as it did not result in effective state institutions. Moreover the opposite happened as the shortfall of functioning state institutions led to a lack of safeguard and security for the rights of the new private business owners. ⁴⁵

In other words: that the mass privatization had failed is obvious, but why did it result in the shortfall of functioning state institutions i.e. a lack of reliable property rights? Well, the prediction of Chubais and Gaidar was based on a false idea that in Russia property rights were already based on law. In fact this was not the case. Normally we can say that law acts on a particular set of legal facts (who owns what) and is placed in a social context (what other relations, options, and interest owners have). During the transition period, the social context was the most essential and legal facts had only a small meaning. This meant that although formally the laws were in place, only relations, interest and other options were the most important issues which could protect property. In order to create functioning state instructions, Chubais and Gaidar first had to transform the idea of the most essential issues (social context) of functioning laws into legal facts. This would give the opportunity for the state institutions to turn into functioning and effective state institutions based on the rule of law and secure fair and law-based property rights for the new private owners, without paying attention to social context.⁴⁶

⁴⁴ Companies that were considered important for the national interest and budget were excluded from the privatization process, such as Gazprom.

⁴⁵ M. Goldman (2003), p 75.

⁴⁶ D. Woodruff (2004), pp. 83-84.

Although mass privatization was over by the end of 1995, the revenues the government had generated by selling its companies were disappointing. The government budget remained in deficit and privatization of the energy sector via the loans-for-shares deals, which was *de facto* the most profitable part of the Russian economy, was already decided to be the new money maker for the state.

In late 1995 the cash-strapped government therefore accepted a proposal from major banks to pledge controlling stakes in twelve of the most profitable mineral resource-based enterprises as security on the loans equivalent to about \$1 billion. The loans were not repaid and the banks became owner of these enterprises.⁴⁷

The proposals were actually contracts which included an arrangement, that the banks (private banks established by the rich business men, such as Khodorkovsky's Menatep Bank) had the right to sell the shares of these resource-based companies in case of non-repayment. A few implications of the deals were curious. Firstly, the loan contracts were only made with banks favouring the government. Secondly, the loan amount was so large that it was already clear that the state could never repay within 9 months. Thirdly, after the deadline passed and the state could not repay, the banks started selling the shares, acting both as organisers and bidders (bids from abroad were mostly on technical grounds disqualified). Consequently, the banks themselves, or associated companies, bought the shares, which was possible due to the lack of transparency. The result of this program was the creation of huge conglomerates headed by oligarchs (chapter 3 will explain the term 'oligarch'). Important for Yeltsin and the re-distribution of political power, these people owed their property to Yeltsin and were therefore willing to support Yeltsin during the elections of 1996.⁴⁸ Furthermore, the sell of the recourse state companies had left the government with a new problem: the new owners of the private businesses could benefit from the lack of proper functioning state institutions and laws (Chapter 2 will discuss this in more detail).

With President Putin's inauguration a new tendency can be discovered as Putin tried to shift the co-operation between the government and too dominant entrepreneurs towards a more centralized policy. Putin's goal was to regain control over civil

⁴⁸ D. Gros and A. Steinherr (2005), p 239.

⁴⁷ D. Gros and A. Steinherr (2005), p 238.

society, to secure strong authority over large corporations in the resource sector and to block the possibility for oligarchs to access Kremlin politics.

As we have seen in this chapter there were many economic and political reforms introduced by Yeltsin and Putin. The 'power' triangle formed by the state, oligarchs and corporations reflects the complex connection within the political and economic structures. We will discuss the idea of a 'power' triangle in chapter 4. The next chapter will outline who the powerful individuals were and which companies were influential as these formed the 'power' triangle through their governmental connections.

Chapter III

Powerful Players

The term 'elite' is almost equivalent to the term 'oligarch' because both refer to a select part of society. 49 However, an oligarch is not 'just' individual elite, but powerful individual elite. This becomes more evident when the state faces a radical change which affects the balance of political and economic power, such as the collapse of the Soviet Union and the transition to democracy and capitalism. In this new environment opportunities arise for establishing stronger economic and political power. The people who could profit the most from these possibilities were the people that entered the strong industries (resource sector) or the financial sector mostly via the loan-for-share deals.⁵⁰

This chapter outlines the most powerful players in the Russian economy; the oligarchs but also influential companies as Gazprom, UES and Menatep (Yukos). These companies are part of the most powerful industry; the resource industry. How is this industry structured? How was the relation between the oligarchs and Putin? How can we interpret the relation between Putin and the oligarchs? These questions are researched in this chapter.

3.1 The Oligarchs

'Oligarch' is an old term which refers to the 'robber barons' in the US in the 1850s. These men were identified as the ones who built great industrial and transportation conglomerates in different US states. Nowadays, the term also labels businessmen simultaneously in Russia and Ukraine. The word 'oligarch' is in this sense used to describe 'small groups of people with economic power who use that power to make significant claims on political power, 'oligarch' refers to very wealthy and political men, who are main owners of conglomerates and are well-connected to the highest government officials.⁵²

 ⁴⁹ A. Brown (2001), p 259.
 ⁵⁰ S. Fortescue (2006), pp. 4-7.
 ⁵¹ S. Fortescue (2006), p 3.
 ⁵² A. Aslund (2005), p 6.

Two sorts of the oligarch group can be distinguished in Russia. On the one hand there are the nomenclature⁵³ oligarchs and on the other hand the business oligarchs. The first group consists of oligarchs with a nomenclature background, who received preferential treatment by old acquaintances who remained in the government after the fall of the USSR. In return, the nomenclature oligarchs helped the government, for example by financing election campaigns or by giving the government officials lucrative jobs after retirement. Before the Putin era, this phenomenon became 'common good' as many former officials switched jobs and became top managers.⁵⁴ The second group of oligarchs are the business oligarchs and for this group we will use Sergei Guriev and Andrei Rachinsky's definition given in their article The role of Oligarchs in Russian Capitalism (2005). They describe the business oligarchs as oligarchs who control sufficient resources to influence national politics which hold excessive market power in the sectors they control.⁵⁵ The sectors are mostly the media, resource and finance sector. What is at stake here is not only a list of names of this second group, but the social relation between the government and the second group; politicians and business oligarchs. For this thesis the focus will be primarily on this second group as these oligarchs are most prominent in the sector that is researched.

3.2 Expansion of State Control

As have been shown, the Russian economy is not at all based on formal rules and laws. Instead the Russian economy is the opposite of a regulative pillar as it continuously allows networks and informal ties to thrive. Therefore the expansion of the state is mostly present within those networks acting between the official government institutions and the powerful oligarchs. Figure 1 explains the connection between the different players within the Russian economy and the Russian state. It shows that all members of the three mentioned networks (market capitalism⁵⁶, siloviki

⁵³ The *nomenklatura*, as a collective noun denotes the occupants of all party *nomenklatura*-listed posts, who numbered some two million in the late Soviet period (T. Rigby (1999), p 234) ⁵⁴ O. Kryshtanovskaya and S. White (2002), pp. 234-238.

⁵⁵ S. Guriev and A. Rachinsky (2005), p 132.

⁵⁶ Market capitalism refers to the existence of a small market economy in Russia with private sector and competitive market. (S. Puffer, D. McCarthy (2007), p 4)

capitalism⁵⁷ and oligarchic capitalism⁵⁸) are attempting to influence the others. Although the circles are equally sized, in reality size can vary, depending on the criteria. The outer circle represents the role of the state, and as we can see, only parts of market capitalism is state-managed. However, most of the Russian economy is state-managed and therefore the Russian state can best be described as network capitalism.⁵⁹

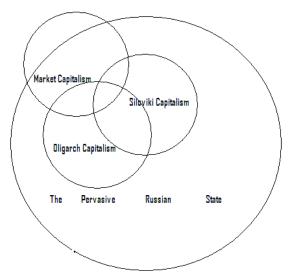


Figure 1. Russia's partly state-managed, network capitalism. 60

In the above figure we see that the smaller circles are closely interwoven which means that arrangements are made between the three network inner circles within the pervasive Russian state i.e. network capitalism. For this thesis we only focus on the arrangement or partnership between the government and business oligarchs, but we can say that all of the relations between the three circles are based on mutual interests. The government and business oligarchs both profit from interwoven relations which help them in extracting maximal benefits for themselves (Corporatism Russian style). Essential for this thesis is the implementation of Putin's 'equidistance doctrine' as it tries to put each oligarch at the same distance from direct access to political power. However, the implementation of this doctrine can be seen as an instrument for victimizing personal political enemies as Putin could use this doctrine to contravene

⁵⁷ Siloviki capitalism means the growing economic influence of the government by controlling major corporations (S. Puffer, D. McCarthy (2007), p 6)

Oligarchic capitalism refers to the economic activities of the oligarchs, predominantly in the resource sector. (S. Puffer, D. McCarthy (2007), p 5)

⁵⁹ S. Puffer, D. McCarthy (2007), pp. 3-4.

⁶⁰ S. Puffer, D. McCarthy (2007), p 4.

⁶¹ S. Markus (2007), p 295.

some oligarchs. Questions that arise are; why did Putin replace some of the oligarchs and not all of them? How did he do that? What does the equidistance doctrine inflict?

After Putin came to power he declared in 2000 that "as long as they stayed out of politics and paid taxes, Putin would respect their property rights". The oligarchs had now only one simple choice; stick to the new unofficial Putin rules or become a Kremlin enemy (which is a result, not a choice). The implication Putin's new policy had, was two-fold. On the one hand it had to result in a decrease in huge business conglomerates, as stronger state control towards the oligarchs would lead to an increased number of restrictions and we assume that this must also decrease the number of oligarchs and therewith the businesses they were able to own. On the other hand it led to a stronger relation between the oligarchs and the state as mutual interests showed the way to cooperation to the benefits of both fractions. Putin was constrained in his dealings with the oligarchs by the need to avoid any threat to political or economic stability. The oligarchs needed Putin for their protection and for his permission for the sometimes illegal businesses of the oligarchs. However, against all odds, during Putin's Presidency the number of Russian oligarchs in fact increased and therewith also their fortunes. 63 The effect of stronger state control was also apparent in the state administration as it strengthened the position of the bureaucracy. The bureaucrats were a group consisting of on the one hand the former Communist party nomenclature and on the other hand a growing number of former and acting military and the staff of special agencies. This trend led to the development of the new term 'militocracy'64, which described the power formation of Putin's Russia.

The new tendency in the development of business oligarchs became visible starting with the above mentioned declaration in 2000. Furthermore, during Putin's first term as President he changed a few elements, of which I mention three:

- Oligarchs activities were banned from the capital to the regions, and at the same time the state tried to increase its political and economic control over these regions.
- The stronger government control restricted the oligarch activities which led to a reduction in direct political influence of the oligarchs.

W. Tompson (2004), p 181.
 O. Gaman-Golutvina (2008), pp. 1036-1037.

⁶⁴ B. Renz (2006); O. Gaman-Golutvina (2008), p 1038.

 Oligarchs began to be eliminated from their own companies. The destruction of for example the Gusinsky and Berezovsky media companies and the arrest of Khodorkovsky were intended to show 'who's the boss'.⁶⁵

The developments mentioned above show that the changes under Putin have influenced the oligarchs' strategies within the battle for property.

No longer can Russia's business elite establish their own parties and engage in open criticism of the government. The new regime is engage in restoring state power, after a period in which it had been privatised by officials and businessmen. In this new social order there is no place for opposition, unpredictable elections, or insubordinate nouveaux riches; rather, the preferred model is analogous to the *cheibols* in South Korea – enormous economic conglomerates whose activity is closely regulated.⁶⁶

The quotation clarifies the new attitude Putin took against the businessmen. However, Putin had a very ambiguous strategy towards the businessmen which becomes apparent as these oligarchs were given an option to either support the Kremlin and play Presidents Putin's game, or become an enemy. The question remains if this changed attitude had implications for the performance of oligarch companies. It is possible that oligarchs who did not play Putin's new game were opposed by Putin administration which could have a negative affect on the firm's performance. It will become apparent if this was the case in the case study, when we look at the performance of the three selected energy companies.

But what were the ideas behind the expansion of state control, typically in the energy sector? First, state expansion in Russia can be better described as state-intervention. The increase of state control was carried out trough the measures mentioned above, which all were striving for direct state control in this specific profitable economic sector. Second, the leading members of the government thought that direct state control would be the only necessary condition for sustained and rapid growth in the Russian economy. Third, ownership had to be transferred to the only 'trustworthy' entrepreneur i.e. the state (this according to the governments own interpretation). Fourth, leading members of the Russian government, including President Putin, wanted to gain more status and become rich and economically

⁶⁵ O. Kryshtanovskaya and S. White (2002), p 306.

⁶⁶ O. Kryshtanovskaya and S. White (2002), p 306.

wealthy people. The easiest way to achieve this was to make the state owner of profitable resource companies.⁶⁷

In general we can characterize the development of the Russian economy as 'a turn to statism' where the state intervenes in economy and has direct control through state-owned companies. As we have seen in this chapter the state expansion started through Putin's declaration of the equidistance doctrine which has had major influences on the existing relations in the state. Some oligarchs owned companies were able to expand their profitable existence, other oligarchs owned companies soon discovered the more negative consequences of the doctrine.

3.3 Oligarch Ownership

Discussing the definition of oligarchs and the expansion of state control raises the question of the characteristics of oligarchs and their companies. The oligarchs became the wealthy individuals by controlling profitable (in true economic value) companies. What kind of owners were the oligarchs? What characteristics were present with most of the oligarchs owned companies? These characteristics are being outlined in this sub-paragraph in order to create a clear overview.

Oligarchs were mostly 'normal' Russian people who were aware of the fact that ownership of a firm was the key to success. The characteristics of oligarchs and their companies are described by Yuriy Gorodnichenko (University of California) and Yegor Grygorenko (University of Michigan). In their discussion paper *Are Oligarchs Productive? Theory and Evidence* (2008) both scholars (sometimes using the ideas of other scholars) outline the following characteristics⁶⁹:

- Oligarchs tend to choose large companies which generate loads of cash money,
 without regard for enterprise efficiency and profitability
- For oligarchs, the political influence that can be purchased along with the shares, is more valuable than the shares itself
- Oligarchs try to create vertically integrated production chains wherein the enterprises are suppliers or consumers to each other

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⁶⁷ P. Hanson (2009), p 18.

⁶⁸ P. Hanson (2007), p 875.

⁶⁹ Y. Gorodnichenko and Y. Grygorenko (2008), p 4.

- The real economic value of oligarchs companies are high, although the accounting profits are low
- Investments and improvements are made by the oligarchs in their own firms⁷⁰
- "... as the oligarchs gained more and more control over their companies, they became better stewards out of sheer self-interest. In the 1990s they fought bitter fights to gain majority ownership; now that it was all theirs, they were more inclined to treat the company nicely." This means that, as the new owners, they become better owners for their own property

The characteristics of the oligarchs and their firms all implicate that these firms perform well and that they will perform even better after oligarchs own these firms.⁷²

However, with Putin's 'equidistance doctrine' the Kremlin attitude changed and this may have had a negative result in the performance of oligarch owned firms. We will discuss this question in chapter 5 through a case study of three selected companies. The next chapter will examine the energy sector and make a selection of three oligarch companies. Furthermore, it discusses the role of these selected companies in the Russian economy and makes a connection between the state, oligarch owned enterprises and wealthy individuals.

⁷⁰ A. Shleifer and D. Treisman (2005), p 161.

⁷¹ D. Hoffman (2003), p. 500. Quoted in the Discussion Paper of Gorodnichenko and Grygorenko (2008), p 4.

⁷² S. Poukliakova, S. Estrin and D. Shapiro (2006), p 5.

Chapter IV

Economic Influence and Power

This chapter will give an overview on the resource sector and the intertwined relations between the three most powerful fractions in the Russian economy. These three fractions are the elements in Russian economy that have the most power, money and status. To sum them up: Russian government, oligarch CEO's (corporate officer or administrator in charge of total management) and oligarch companies. Through several similarities and benefits that exist in all these fractions and within the Russian economy, they are all connected to each other. We can say that it is the resource sector that is the most prominent joint element and we see this as the connection between the three fractions. Furthermore, this chapter highlights what kind of companies have the potential to become powerful and influential within the economic field and politics.

4.1 The Energy Sector

The Russian energy sector has always been of great importance for Russia's economy. During the period of state socialism the resource industry was characterized by state ownership and formal control of the production, transport and distribution. Thereby the government also controlled the export, prizes and investments of oil and gas. The different stages of the production process were divided among several ministries and only from the early 1980s a central Bureau for Fuel and Energy was established to coordinate the policies of the various ministries.⁷³

A radical restructuring of the energy sector took place with the transition from state socialism to capitalism, as functions of the previous ministries were taken over by firms, corporations, local administrations and associations. The management of the local companies was sometimes conduceted by the leaders of the local administration, who acted primarily in their own interests. To maintain control over the local

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⁷³ D. Lane (1999), pp. 15-16.

companies the Russian government wanted to form several holding companies⁷⁴. Mid 1992 the government formulated plans to reorganize the energy sector into twelve large, vertically integrated companies. This industry was crucial to the well-being of the economy and therefore some form of state control was desirable.⁷⁵

The privatization of the smaller resource companies made it possible for a few individuals to buy privatized energy companies and enter the energy sector. These individuals had no experience in the Russian oil industry, but they had access to financial resources through private banks. Also vital for entering this sector was close contact with the government, as it were the government officials that were selling the properties.⁷⁶ With this close connection the newcomers had ensured themselves of political friends which they needed to ensure of their own fragile and new position. We can see that there were different movements apparent in the energy sector as on the one hand smaller resource companies were privatized and from then on owned by individuals, and on the other hand the government wanted to regain control over the sector as it tried to form big holding companies.

The Russian financial crisis of 1998, caused by the collapse of the Russian Rouble, weakened the Russian economy. Simultaneously to the financial crisis the world crude oil prices were raising from 10 dollars a barrel in December 1998 to around 33 dollars a barrel in September 2000. 77 This meant an enormous stimulus for the Russian energy sector and also helped to recover the Russian economy. This sudden incentive boosted the company revenues and made the resource industry the most profitable sector of the Russian economy.

However, it was only with Putin's Presidency that Russia became a genuine 'petro-state'. The share of energy in the gross domestic product (GDP), the export of oil, but mainly Putin's self-created perception of the Russian citizens and employers towards the rest of the world made Russia a major oil and natural gas supplier. Putin knew that it was the Russian self-importance to be a world oil player and he also saw

⁷⁴ A company that holds several other companies (especially the shares) and is not producing the goods, but the purpose of this company is owning the shares of other companies, which in this case were then owned by the Russian government

⁷⁵ D. Lane (1999), p 17.

⁷⁶ F. Hill (2004), pp. 10-11.

⁷⁷ F. Hill (2004), p 10.

A petro-state could be described as a resource focused country with weak institutions and a malfunctioning public sector. Its most important feature are laws that grant subsoil rights to the government, from which spring the extraordinary size and duration of the "petro-rent" which is much greater than the profits which can be made in the private sector.

how profitable this sector was. This made it important to gain control over this sector as it would bring the country money and international power and status with great appreciation from the Russian citizens to their government.⁷⁹

In order to structure the energy sector in a more effective and efficient way, a strategic document entitled; 'Russia's Energy Strategy for the Period up to 2020'⁸⁰ had been developed. The strategy implies that the energy sector has a clear regulatory system for the domestic and international market. In practice, this is not the case which makes it difficult to implement the strategy. This means that the strategy is usually ignored and all essential elements for creating a competitive energy market are not implemented and remain theoretical constructs. Although some progress has been made, the energy industry is still primarily dominated by personal relations, mutual agreements and interests.

In sum, Russia's energy policy is fragmentary and contradictory. Its structure is dictated by rather short- and medium-term interests that are detached from the functioning of the capital-intensive energy sector. The current policy model is limited to "planned indicators" for long-term resource production, and the government's ambiguity has become more apparent in 2004–2005, as the Russian leadership intensified its interference in economic processes.⁸¹

As the resource sector is the most prominent link between the Russian government, oligarch CEO's and oligarch companies the next paragraph outlines how we should interpret this power triangle.

4.2 Power triangle

The questions that will be answered in the next paragraph are; how are the relations within the power triangle? What is the basis for this relation and what does the triangle relationship imply?

In order to clarify the unofficially sanctioned political power and economic influence oligarchs have in Russia, this paragraph focuses primarily on the triangle that has been formed within the energy sector between three fractions; the Russian

⁷⁹ P. Baev (2008), p 19.

⁸⁰ V. Milov, L. Coburn and I. Danchenko (2006), p 285.

⁸¹ V. Milov, L. Coburn and I. Danchenko (2006), p 287.

government, oligarch companies and the oligarch CEO's of these companies (Figure 2, wherein A, B and C are the indicators for the relation between the fractions).

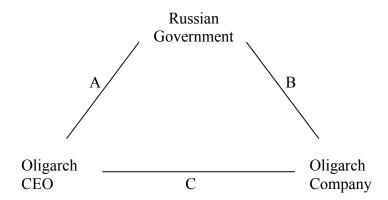


Figure 2. Russian power triangle within energy sector

The relation between the Russian government and the oligarch CEO (A) is primarily based on family, friendship and mutual interest. For the Russian government the interests are mainly economic as they can control and influence oligarch companies via the oligarch CEO. Oligarch CEO's are mainly interested in increasing political influence and increasing the performance of their enterprises. The link between the Russian government and the oligarch companies (B) consists of mutual economic interests and extracting maximal profits for both. Moreover, we see a shift in this relation because during the Yeltsin period the relation was mainly based on privileges for the oligarch companies. In the Putin era this shifted to a more substantial relation as it became directed to the regulation of the economy as a whole. The connection between the oligarch CEO and the oligarch company (C) is most obvious as the oligarch CEO acted as selfish owners, this was mostly not the case because oligarch CEO's invested in their companies and employers, in order to improve firm performance through higher efficiency and productivity (which is not a selfish act). Selfish act).

We need to pose the triangle against the background of the changed attitude of Putin towards the oligarchs before drawing any conclusions. Because what does this

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⁸² S. Poukliakova, S. Estrin and D. Shapiro (2006), p 8.

⁸³ O. Kryshtanovskaya and S. White (2005), p 306.

⁸⁴ S. Guriev and A. Rachinsky (2005), p 141.

triangle implicate after Putin's attitude has changed? It certainly means that any change in Putin's attitude will have a consequence for the balance in the power triangle as the existing relation is disturbed. However, it is difficult to measure the changes in balance, except for the Yukos-case. For most scholars it was obvious, although not admitted, that Putin's changed attitude towards the oligarchs resulted eventually in the prosecution of the Yukos oligarch CEO, Khodorkovsky. However, for other cases it is more difficult to show any change after Putin's new attitude, and therefore we will look in the next chapter at the performance of these oligarch companies as this is a useful indicator for measuring any change in a company.

Before looking at the performance of oligarch companies, three companies need to be chosen for our case study. This can only be done if there is a clear idea which companies were influential in politics and the economy, and would hypothetically suffer or profit from most changes in the existing Kremlin-oligarch-company relationship.

4.3 Influential companies

In 2002 there were eleven most influential oligarchs (business groups) in Russia, mostly in the energy, media or finance sector. Barnes article *Russia's New Business Groups and State Power* (2003) classifies these groups in 'deep'; 'broad'; 'deep and broad' and 'narrow and shallow' companies. Herewith, Barnes tries to classify the vulnerability of the companies. The 'deep' companies are the companies that have control over several stages of the production chain and therefore they are less vulnerable to changes in supply and demand. (The exact meaning of the 'broad', 'deep and broad' and 'narrow and shallow' companies are not discussed and explained, as this is not necessary for this thesis. For a complete list of these companies and their classification, see annex 1) These companies are thus the most strong and prominent in the Russian economy which makes it attractive for the government to keep good contact with these companies. As these 'deep' companies are mainly resource companies, closely connected to the government and led by powerful magnates, three of these companies are chosen.

Although the 'deep' companies are the strongest companies, it is not said that this strong position is a guarantee for success within the new Putin era. The most

important 'deep' holdings are UES (Electricity Company led by Chubais), Gazprom (Gas Company led by Miller) and Menatep/Rosprom (integrated holding in the bank and oil sector concentrated on the oil company Yukos, and lead by Khodorkovsky). Both Gazprom and UES were part of the Soviet Ministry during the Soviet period and after the collapse of the Soviet Union both were transformed into independent companies.

The most important selected deep holdings to focus on are: Gazprom, UES and Menatep. The three selected companies have in common that they are strong, powerful and deep holdings, however, after Putin became President this changed. However, our assumption was that oligarch companies perform better than state-owned companies. The problem that is faced then is whether the selected companies are oligarch-owned or state-owned. For Menatep it is obvious that it is oligarch-owned. Menatep, with major stakes in the oil company Yukos, had the strongest growth in the value of total assets, i.e. performance, but they did not acted within the new rules and, as we will see in the next chapter, they had to pay the price.⁸⁵

But who are the actual owners of Gazprom and RAO UES and are these owners also oligarchs? RAO UES is a privatized company but the Russian government still holds the majority of the stock. But although the government has strong control in this company, Mr. Chubais is the CEO of the company and he leads RAO UES his own way. This means that he does not always act as the Russian government wants him to. However, Chubais stays in good contact with the Kremlin because he is aware of their influence in the company. The 'equidistance doctrine' is in this case an unofficial measure that is, to a certain degree, accepted by Chubais and enables the Putin administration to stay in close contact with the company. Also, the Putin administration informally controls this company, as Chubais knows the dangers of acting too much against the rules of the game (this will be shown in the next chapter). Gazprom is also owned by a figure we can classify as an oligarch, according to the definition we have outlined in paragraph 3.1. Before Aleksei Miller, Rem Vyakhirev holds the highest position in Gazprom. 'Vyakhirev's successor, Aleksei Miller, is a close Putin associate and an outsider to Gazprom. He has thus relied on the Kremlin's support since his appointment and has not really established himself as

⁸⁵ A. Shleifer and D. Treisman (2005), p 161.

an independent figure as Vyakhirev did.'⁸⁶ Although Miller has entered Gazprom as an outsider and with Kremlin support, he also fits the description of an oligarch (namely the oligarch that has come to power with help from the government and therefore it is impossible to act slightly away of the Kremlin, as he is thankful to the Kremlin). As Guriev and Rachinsky describe; oligarchs are individuals who control sufficient resources and market power in order to influence national politics.⁸⁷

All three companies are led by an oligarch who all have a distinct relation with the Kremlin and all the oligarchs took another stand against the equidistance doctrine which resulted in a distinctive change of the strength of these companies. The next chapter portrays the three companies and will give a detailed overview of the results of the changes in company strength after Putin introduced the 'equidistance doctrine'. How this change affected their performance and how this performance will be measured, is discussed in the next chapter.

⁸⁶ W. Tompson (2004), p 2.

⁸⁷ S. Guriev and A. Rachinsky (2005), p 132.

Chapter V

Case Study

This chapter will focus on the three selected companies that were strong and deep holdings when Putin took office in 2000. Before taking a close look at these companies it is important to keep in mind that the Russian power triangle is centred on the model of Russian corporatism. As discussed in paragraph 1.2, this model demonstrates which individuals and institutions have official access to the process of policy formation. In examining the three companies we will take into account if these companies are officially sanctioned to enter the policy formation and implementation process. As has been outlined in the previous chapter, the basis of the relation between the three fractions that are apparent in Russian is the resource sector. This chapter will focus on three major companies in the energy sector: Gazprom, UES and Menatep.

In this thesis the idea of firm-performance of oligarch owned companies will be discussed in paragraph 5.4. The idea firm-performance is connected to the principle of out-performance. Out-performance means that someone or something surpasses another in performance. Performance or out-performance is thus crucial to see how oligarchs' companies have performed. The question arises why oligarch ownership is or might improve firm performance?

According to Guriev and Rachinsky, oligarchs theoretically have a great possibility to improve firm performance. They argue that there are four main reasons why oligarch owned firms will perform better than state-owned companies. First, oligarch owners hold a very large majority of the shares so they have a strong incentive to improve the value of these shares. Second, many oligarch empires are vertically integrated in order to prevent hold-up problems⁸⁸. Third, due to access to the financial institutions (banks), oligarch companies can benefit from their strong financial positions in the underdeveloped market. In these markets finances are mostly an entry barrier for smaller firms (not oligarch owned firms), which is an advantage for oligarch owned companies as their position is stronger within a less competitive market. Fourth, the large conglomerates are effective in influencing the

⁸⁸ Buyers and sellers are depending on each other and generate a surplus. Vertical integration makes the company less depending on outside buyers and sellers as the whole chain is part of the company and makes it therefore less vulnerable for external economic changes.

rule of law in Russia to their benefits, and are therefore better in protecting their private property from the 'grabbing hand' of the government.⁸⁹

For example Guriev and Rachinsky show that the oligarch companies managed to increase their total productivity growth with 8 percent (in 2002) above the rest of the firms (state firms, firms owned by other Russian businessmen), by retaining inputs at the same level and improving their firm performance. In their article they explain the methodology they use for measuring the total productivity growth of oligarch companies. The outputs are measured in logs. However, it is beyond the scope of this thesis to measure more outputs by using logs as it is too mathematical. The regression they show in their article *Ownership Concentration in Russian Industry* (2004) compares the change in output, holding constant the inputs of capital and labour. Moreover the regression shows the effects of the different forms of ownership on the growth of total factor productivity ⁹¹.

For this thesis we follow the argument of Guriev and Rachinsky; after oligarchs become the owners of a firm, the firm performs better. However, with Putin's 'equidistance doctrine', the Kremlin's attitude changed and this may have had a changed (negative or positive) affect in the performance of oligarch-owned firms. Through the case study we are able to answer the following questions; what are the performance indicators? Are the performances of the three companies in accordance with what we would expect from the performance indicators and their changed attitude towards the Kremlin? Do the outcomes of table 1 (the performance indicators of the three selected companies between 1998 and 2005, page 39) support the theory? What conclusions can be drawn from these figures?

5.1 Gazprom

Gazprom was set up in 1965 as an offshoot of the Soviet

Gas Ministry. Until 1989 it was part of the Soviet system and produced gas for

⁸⁹ S. Guriev and A. Rachinsky (2004), p 14.

⁹⁰ S. Guriev and A. Rachinsky (2005), p 143.

⁹¹ S. Guriev and A. Rachinsky (2004), pp. 15-16.

⁹² S. Guriev and A. Rachinsky (2005), p 141.

Russian consumers and state companies. After the Soviet period it became an independent (on paper) company led by its first chairman Viktor Chernomyrdin. 93 On February 17, 1993, according to the Decree of the President of the Russian Federation dated November 5, 1992, Gazprom State Gas Concern was transformed into Gazprom Russian Joint Stock Company (RAO Gazprom). In 1998, RAO Gazprom was transformed into the open joint stock company (OAO Gazprom).⁹⁴ According to Nadejda Viktor's working paper Gazprom: Gas Giant Under Strain it was in this period that Gazprom acted as a state within a state. Meaning; that Gazprom was the most powerful state institution that was not formally controlled (as most shares were managed by Gazprom itself) and informally (the state was not able to gain enough influence in Gazprom) by the state and acted primarily in the interests of its management. The tolerance of the state towards Gazprom was based on mutual interest between the state and Gazprom which consisted of an unofficial agreement that Gazprom would deliver gas at a very low price to the Russian consumers. The economy could benefit from the cheap supplier of gas, and Gazprom could benefit from certain financial advantages like privileged access to hard currencies from its export.95

However, the relationship between the state and Gazprom changed after Putin became President. For Gazprom's performance and the connection between the Kremlin this change was positive (as we will see in table 1, page 42), but both became more and more intertwined. This was noticed because many members of Gazprom's management were replaced by Putin's friends after Putin entered the stage. For example the former Chairman of Gazprom's Board of Directors, Dmitri Medvedev had been Putin's Chief of Staff (After Medvedev was Deputy Prime Minister he became the new President of Russia on 7th May 2008). The current Chairman of Gazprom, Alexei Miller, has also been a close friend of Putin and Medvedev. The management change between 2001 and 2005 was just the beginning. Soon the whole team was changed into the 'St. Petersburg Team'96, who controlled almost 60 percent of the oil-industry and almost all gas production in Russia. 97 The replacement can be seen as a re-nationalization of Gazprom and it showed the closer ties between the

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⁹³ C. Paillard (2007), pp. 9-10.

⁹⁴ http://old.gazprom.ru/eng/articles/article14964.shtml visited on July 16, 2009.

⁹⁵ N. Victor (2008), p 52.

⁹⁶ Kremlin elite during Putin's presidency.

⁹⁷ N. Victor (2008), p 51.

state and the company, which demonstrates that the combination of energy and politics has made Gazprom an instrument of political-social regulations in Russia. 98 In other words, Gazprom is not part of the state i.e. it is not an official state institution, nor is it officially sanctioned to enter the policy formation and implementation process; but some functions that are normally performed by the state are transferred to Gazprom. For example, normally the state is concerned with the employers of their companies. In Russia, the state uses Gazprom to help them protect these employers. This means that Gazprom sometimes helps herewith the state to ensure the survival of some enterprises if this contributes to the protection of employers. Resulting in buying or selling of state property carried out by Gazprom. We see here that Gazprom operates as part of the government. We can therefore argue that there is an institutional struggle between Gazprom and the government, wherein that state sets the rules of the game (inviting foreign investment and blocking most competition) and Gazprom helps the government by protecting employers, providing state budget, expertise on techniques, and buying/selling businesses.⁹⁹

To refer to the model of Russian corporatism; the above mentioned denotes that Gazprom must be unofficially sanctioned to enter this process and be entrusted with controlling the free market in name of the Russian government. With this process many problems can be distinguished. One of the problems is that with these intertwining, Gazprom sometimes represents the worker's interests, and sometimes the state's interests. However, in the case of Gazprom and the Russian state, both share several fundamental values and have mutual interests, which lead to a form of co-operation (with the critical note that in the end the state is the boss) that is based on extracting maximal benefit for both. 100

5.2 RAO UES of Russia

In December 1992, RAO UES (Russian Joint Stock Company; Unified Energy System of Russia) was set up by Presidential decree. All non-nuclear generation, transmission and distribution assets were divided

98 C. Paillard (2007), p 10. 99 N. Victor (2008), p 53

¹⁰⁰ V. Kryukov and A. Moe (1996), p 38.

between RAO UES and 75 regional power utilities known as AO-energos. To secure its control over the electric power industry, the state retained control over 52.55% of the shares of RAO UES. After 10-years the government wanted to create a more competitive electricity industry and announced a plan which had to improve the sector's efficiency, transparency, investments and ensure reliable supplies. 101

From 1999 Antoly Chubais, one of the architects of the privatization process has been the CEO of RAO UES.¹⁰² Chubais' task was to bring the house in order. The years that followed were characterized by reorganizing sales, insisting on cash settlements and the cutting of non-payers. This was also prominently seen with Chubais and UES. After becoming President, Putin criticized the reforms UES had introduced as he feared that UES wanted to control the energy sector. Henceforth, UES and Chubais needed to act as the Kremlin wished, which meant that UES and Chubais had to give up his economic ambitions with UES. The critics have been seen as Putin's last warning to Chubais and UES, mainly resulting in the dumping of the UES stocks by shareholders. Putin's problem was that he could not remove Chubais easily because; on the one hand it was problematic to remove Chubais as 75 percent of the shareholders of UES had to agree (52 percent was state-owned, approximately 30 percent was foreign-owned), on the other hand Chubais was also internationally active and could not be removed without creating a scandal. 103

Soon after this incident, Chubais had the ambition to join the Presidential election in 2004. 'Many members of the Union of Right Forces (URF), primarily Chubais himself, seem to believe once more that the head of Russian Joint Energy Systems (RJES) has a real chance of winning a Presidential race. This idea was based on the use of the marginal method of the determining of electricity rates.

> That is, the rates will only cover the costs of electricity generation. The secret is that a marginal rate is determined based on the costs at the most expensive facilities. As a result, power plants which are operating more successfully will begin to make substantial profits. Hydro-electric power stations will become the most profitable, or rather mega-profitable. The primary cost of electricity at such power plants will only amount to 5-7% of the new rates, so the profit would be 93-95% respectively. A few people now know which power plants will actually become profitable and which won't. RJES will be broken up by the time the new rates are introduced, and the power plants will be privatized.

¹⁰³ B. Humphreys and M. Bivens Chubais, 'Other Oligarchs Under Fire' on http://www.cdi.org/russia/johnson/4099.html#2

A. Hajarov (2002), http://www.cdi.org/russia/johnson/6103.htm

¹⁰¹ OECD Reviews of Regulatory Reform (2005), p 180.

¹⁰² T. Sabonis-Helf (2007), p 1.

The federal budget will gain considerable sums of money; and about a year later, the socio-economic situation in Russia will become quite favourable. The nightmare will happen later, in 12 to 14 months, when the rates will be increased by 3-3.5 times. The socio-economic consequences of this measure will be catastrophic, but not for Chubais himself. He will not head the electricity sector by that time. 105

If this plan had been implemented the national economy would collapse also brining down President Putin. However, Chubais was unable to bring his idea into practice and it only troubled the relation between the state and UES, i.e. Putin and Chubais. 106

In 2003 a set of laws and regulations was adopted to break-up the vertically integrated structures into competitive companies. The regulations dealt with access, pricing, investment, crisis management and institutional arrangements. ¹⁰⁷ On 29 May 2003, RAO UES adopted a 'conceptual strategy' which came to be known as the '5+5 strategy¹⁰⁸ for the period 2003-2008. The strategy defined the basic principles of restructuring the electricity sector. Simultaneously, the government laid out its own 'action plan' for restructuring the electric power industry. According to the publication of the OECD, this process has been carried out in three phases, of which the last phase is now being implemented. 109

> RAO UES is an important and highly visible company in Russia, but Chubais's relations with the Kremlin are not always positive: when portions of the Russian electricity grid failed in May 2005, President Putin blamed Chubais personally, accused him of focusing too much on international projects rather than day-to-day operations, and had prosecutors summon him for questioning. It is an indication of how important Chubais is in the international investment community that charges were not brought against him. 110

For Chubais the accusation did not have many consequences as he is a prominent person in Russia and also very well known abroad, because of his political past. However, it indicates that the management of a private company must always be aware of the Kremlin and its policies, in order to prevent acting against these Kremlin policies. The Chubais incident shows how a relationship can change and how

¹⁰⁵ A. Hajarov (2002), p 1.

¹⁰⁶ A. Hajarov (2002), http://www.cdi.org/russia/johnson/6103.htm

¹⁰⁷ OECD Reviews of Regulatory Reform (2005), pp. 180-181.

¹⁰⁸ The plan was developed by RAO UES over the period of five year (1998-2003) and is expected to be implemented between 2003 and 2008. OECD Reviews of Regulatory Reform (2005), p 181. For more information see www.rao-ees.ru/en/show.cgi?info/con2003.htm#1

¹⁰⁹ OECD Reviews of Regulatory Reform (2005), p 182.

¹¹⁰ T. Sabonis-Helf (2007), p 1.

individual persons and companies were mostly unable to act as they wished although it would officially be a legal act.

5.3 Menatep

Bank Menatep, lead by Michael Khodorkovsky, was a major player in the oil sector as it is centred on the very profitable oil company Yukos ('Menatep began playing a subordinate role, as



its income could not be compared with Yukos's oil revenues'¹¹¹). Yukos was established by the Russian government in 1993, by integrating various production, distribution and refining companies. In 1995 Menatep acquired 33% of Yukos' shares and via the loans-for-shares deals Menatep increased its direct influence to 85%. In return for this deal Khodorkovsky had to support Yeltsin's election campaign for a second Presidential term. Through its political influence and privileges, Yukos could reduce costs and violate company laws.¹¹²

Bank Menatep collapsed during the financial crisis of 1998; however Khodorkovsky moved the assets into a new bank called Menatep-St. Petersburg. Yukos bought out its minority shareholders and Khodorkovsky's group started to deepen and expand its holding structure. Several companies in the oil and gas sector were purchased and brought under Menatep-St. Petersburg. ¹¹³

The years after the financial crisis were profitable for Yukos as the oil price raised and the new management turned the company into a well-functioning competitive enterprise. Thereby, the relation with the Kremlin was good, until the Yukos-Khodorkovsky scandal. The conflict started when Khodorkovsky openly criticized the corrupt Putin administration. In addition, Khodorkovsky refused to donate money to Putin's political party United Russia at Kremlin's request. Instead Khodorkovsky donated money to the opposition parties. The conflicting agenda's and ambitions between Putin and Khodorkovsky was according to Tompson the reason for the conflict, as Putin did not tolerate any opposition from Khodorkovsky (Putin actually did not tolerate any threatening opposition that could have been a real threat to his own position, this means that Putin in fact did not see Chubais as a great danger for keeping his Presidential position). The charges against Yukos shareholders and Khodorkovsky involved matters that were part of previous agreements between

¹¹² B. Maury and E. Liljeblom (2007), pp. 8-10.

¹¹¹ D. Gololobov (2008), p 7.

¹¹³ A. Barnes (2003), pp. 164-165.

¹¹⁴ B. Maury and E. Liljeblom (2007), pp 10-11.

Yukos and the state. As Khodorkovsky had made Putin furious with his actions, Putin felt no obligation to sustain these agreements any longer. Putin chose to single out Yukos via unclear procedures and tax legislation.

It was not until two years later, in June 2005, that Victor Gerashchenko, the head of the company's board of directors, admitted that Yukos had been close to selling 45% of its shares to ExxonMobil in October 2003. However, Yukos had been delaying the deal in order to complete its merger with Sibneft first. President Putin's declaration in the New York¹¹⁶ Times meant that the planned sale of Russia's largest oil company's shares had not been consulted with the Kremlin. It seems that the key reason behind Khodorkovsky's arrest should be sought here.¹¹⁷

Yukos had to be an example for the rest of the oligarch owned companies as now all oligarchs had seen what could happen if Putin's new rules were neglected. Soon, Khodorkovsky was jailed under great applause by the Russian citizens as they felt betrayed by the rich businessmen. Putin was seen as a hero for imprisoning the thief of the state, Khodorkovsky. The implications of these actions were and are enormous. The rest of the wealthy businessmen had to reinsure their property rights by paying large amounts of money for these rights to the Kremlin. The result of these actions was different than expected. Instead of scaring and weakening the oligarchs, their empires were becoming stronger. However, the smaller companies were victimized by these practices and tended to be bailed out. Consequently, the oligarch empires also benefited from less competition as there were less small Russian enterprises and foreign enterprises active in Russia. 118

5.4 Performance and Indicators

After examining the three selected companies we have seen that the relation with the Kremlin has been changed due to Putin's equidistance doctrine. The next paragraphs will look at the consequences of this changed relation. Can we see a difference in the firm's performance between the three companies after they took another stand towards the Putin administration? Or does a troubled relation with the Kremlin result

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¹¹⁵ W. Tompson, (2005), pp. 159-162.

¹¹⁶ Declaration: "Mr. Putin clearly desires order, and to him that means a strong central government. Asked about reports that ExxonMobil was negotiating to buy a large share of the newly merged YukosSibneft, Russia's largest oil company, Mr. Putin said Russia welcomed foreign investment. Then he added that the government ought to have a say in so significant a deal." S. Myers (2003), p 2.

¹¹⁷ W. Konończuk, (2006), p 45.

¹¹⁸ A. Aslund (2005), p 12.

in a fall of the firm's performance as the Kremlin is hoping for? For example, after Chubais had trouble with Putin, this should be reflected in the performance of UES as the company is then contravened by the Kremlin.

Before researching the above mentioned hypothesis, it is important to examine the firm's performance. Indicators for measuring the performance of the firms are widely discussed among scholars. As these indicators define whether the performance of Russian oligarch-owned companies increase or decrease after Putin's equidistance doctrine, it is of great importance to explain what we understand by 'performance' and which indicators will be used for measuring this performance.

We use firm size as a proxy for measuring firm performance of the three selected companies. Firm size is calculated (or: defined) as the book value of total assets. ¹¹⁹ In the article *A Normal Country: Russia After Communism* (2005) Schleifer and Treisman also use the figures of total assets for measuring firm performance of three leading Russian companies (Yukos, Sibneft and Norilsk Nickel). Thereby, they also show how much money these companies have invested and both conclude that oligarch-owned companies invest significantly more than firms controlled by other Russian owners. ¹²⁰ However, we have chosen to look only at the total assets of Gazprom, RAO UES and Menatep (Yukos) as these figures give us clear insight in the firm's performance over time.

Table 1 gives an overview of the total assets of the three companies between 1998 and 2005. As Khodorkovsky and its partner Platon Lebedev were arrested in the summer of 2003, the figures of Menatep (inclusive Yukos assets) are only until 2002 as after that the Yukos assets were no longer owned by Menatep and became owned by state oil corporation Rosneft.

Table 1. Total Assets of Three Russian Energy Companies

(mln Russian Roubles)	1998	1999	2000	2001	2002	2003	2004
OAO Gazprom							
Total Assets	1.165.405	1.316.222	1.410.545	2.339.787	2.474.624	2.656.709	2.913.263
UES							
Total Assets	731.027	826.846	979.878	1.090.098	1.061.436	1.087.541	1.126.998
Menatep (OAO Yukos)							
Total Assets	117.660	165.000	294.075	320.460	459.936	31.181*	29.715*

¹¹⁹ For more information on performance see R. Frydman, et all (1999), p 1158, S. Estrin, S. Poukliakova and D. Shapiro (2009) and J. Hanousek (2004), p 13.

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¹²⁰ A. Schleifer and D. Treisman (2005), p 161.

* National Bank TRUST (formerly Bank Menatep St. Petersburg) Consolidated financial Statements 2003-2004. Figures: Schleifer and Treisman (2005), p 162.

Source: Audited financial statements and annual reports of the three selected companies, available on their websites

In the next paragraphs a closer look will be taken at the above figures. What do these

figures tell us and is this what we had expected?

5.4.1 Gazprom

As we have seen the total assets of gas giant Gazprom have been very high and increasing every year. Most prominent is the increase in total assets between 2000 and 2001 with 65.87 percent. This extraordinary growth is in enormous contrast with the growth of the total assets of Yukos and UES in the same year (11.25% and 8.97%). We suggest that a difference in the attitude towards the Kremlin can affect this unusual increase in performance. As the relation between Gazprom and the state grew stronger between 2000 and 2001 as Putin became President in that year and Miller has entered the stage, we should expect that Gazprom can profit from this situation and increase its performance. The results in table 1 show an increase in value of Gazprom's total assets i.e. their performance, which supports the idea that there is a positive correlation between the performance and the relation with the state. Thus, it seems that also the introduction of the equidistance doctrine in 2000 has had a positive influence on the performance of Gazprom as the value between 2000 and 2001 almost doubled. In general we can state that between 1998 and 2004 the relation between the Kremlin and Gazprom has been stable and growing performances have even made the company acquire a number of oil-companies in 2005-2007, such as Sibneft, Sakhalin Energy (Shell-lead) and Russia Petroleum. 121

The market strength of Gazprom is enormous and they are making loads of money and they are also backed by the government. A critical note can also be made as Gazprom is also facing several problems concerning present and future performance. Because the company is still managed Soviet style, which means that they use an outdated system of distribution and consumption, Gazprom's efficiency is very low. Only a few investments have been made in improving infrastructure, the production process and efficiency; resulting in production stagnation, declining energy fields and rising costs. The company value has been growing, driven by the rising gas prices which made it interesting for the Russian state to try to control this

¹²¹ For the complete list see: W. Tompson (2008), pp 15-16 or P. Hanson (2007), p 876.

money maker. However, now that prices are decreasing, it is possible that the Kremlin's urge to control Gazprom will also decrease. 122

5.4.2 RAO UES of Russia

The total assets of RAO UES of Russia grew steadily with an average growth percentage of 14 percent between 1998 and 2001. However, the performance of RAO UES stagnated after the performance declined in 2002. To solve the stagnation problem, ROA UES wanted to attract foreign investors to sell their shares too, and they wanted to restructure parts of the company into independent commercial firms. For these measures they needed to have the opportunity to operate under the conditions of a free electricity market. However, many experts and also members of the government believed that these measures would not solve the problem. The results of these measures would be price reduction, as a more competitive market would generate price liberalization. But, price liberalization can hardly be achieved in a country were prices are already barely covering costs. 123

The ideas RAO UES had for solving their problems were not followed by the government. This is partly because they really thought that the measures that RAO UES wanted to take were not solving the problem, but the government also doubted whether the measures would help as it would attract foreign investors. Trying to liberate prices too early would be a crucial mistake, as it would slow down growth even more. Thereby the Russian governments doubted if foreign investors would provide the company with the billions of dollars as promised by Mr. Chubais. The government primarily saw this distribution of shares as a way to transfer shares at bargaining prices to the companies' insiders, personal friends and other oligarchs in exchange for political and economic support. 124

All the measures RAO UES and Chubais tried to introduce in order to strengthen the position of RAO UES have been blocked by the government. The government claimed that the measures were not solving the objected problems. But this is what formally happened. What were the underlying motivations for the government's objections? Is it possible that the objections are an expression of Putin's dissatisfraction?

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¹²² N. Victor (2008), p 62.

¹²³ O. Trofimenko (2001), pp. 119-120.

¹²⁴ O. Trofimenko (2001), pp. 119-120.

We can state that after Putin became President in 2000 and Chubais challenged the government and specificly the head of the state, RAO UES growth figures fell. However, is there a direct relation between this? As Putin was not able to remove Chubais, he could easily influence firm performance and weaken the position of RAO UES and therewith Chubais' position. Surely there is no direct proof that Putin influenced RAO UES performance? But we can assume that through influencing firm performance, Putin was able to show his dissatisfraction with Chubais' behavior.

5.4.3 Menatep

Table 1 shows that the value of Menatep's total assets is lower compared to the other companies. However the value is increasingly high-flying compared to the other two companies. Only between 2000 and 2001 the rise in total assets slowed down to 9 percent. As world oil prices are strongly raising in the last decade, part of the increase of Menatep's total assets is caused by this phenomenon. However, this does not completely explain the raising value of the total assets, as these figures are also determined by better or improving management of the oligarch CEO's. 125 The figures of 2003 and 2004 are not taken into account as that was the start of the attack on Yukos. This attack came together with the arrest of Khodorkovsky based on a revisitation of Yukos tax returns (which had been approved and signed earlier).

The changed attitude of Putin resulted in a conflict wherein it was clear who would be the winner. Moreover, we can say that the 'Yukos affair' is a good example of the government shift towards statism, wherein we see the state turn from a policeman to a legal criminal. 126 It shows that the attack and the assault on one of the major figures, Khodorkovsky, was part of the new game that could be played with the new rules Putin had set out.¹²⁷ To sum up, the 'Yukos affair' shows how Putin's 'equidistance doctrine' could have a negative effect on firm performance, i.e. they could destroy the performance by using their power.

The next chapter will connect all of the findings and draw a conclusion on the information that has been outlined in the previous chapters.

A. Schleifer and D. Treisman (2005), p 161.
 Translation of statism according to: http://aynrandlexicon.com/lexicon/statism.html
 P. Hanson (2007), pp. 879-880.

Chapter VI

Conclusion

This thesis studies how Putin's inauguration changed the relation between the Kremlin, the oligarchs and oligarch firms, and how Putin's equidistance doctrine affects the firm's performance of oligarch owned firms. Therefore, it has been shown how the Russian economy and the political system has changed after Putin came to power. Moreover, it has been outlined what the performance indicators are, and how the performances of the three selected companies were between 1998 and 2005. It has also been discussed how these figures are related to Putin's 'equidistance doctrine'.

The main findings of this research are as follows. First, it is found that during the Yeltsin period state-owned companies were privatized and became owned by the new rich businessmen, i.e. the oligarchs. This created a situation in which the oligarchs, that had control over sufficient resources, were unofficially sanctioned to enter the policy formation. Second, after Putin took over the Russian Federation from former President Yeltsin, Putin's first priority became strengthening the authority of the Russian federal government and regaining control over the Russian economy and politics. As the resource sector was making money and gaining international status, this primarily oligarch-owned sector had to be under government control again. Putin introduced his 'equidistance doctrine' and a new game with new rules had to be played between the Kremlin and the oligarchs. This changing relation has had consequences for the oligarch owners and for their companies. Third, through the study of three resource companies; RAO UES, Gazprom and Menatep (Yukos) the impact of the changed relation through firm performance figures between 1998 and 2004 has been measured. The outcomes showed that after Putin's 'equidistance doctrine' both the figures of RAO UES and Menatep have fallen as of the changed relation with Putin.

As a critical note it must be highlighted that all findings only suggest that the introduction of the equidistance doctrine may have had an affect on the firm performance of the researched oligarch companies. Surely, other factors also could have influenced the performance change. We do not have any proof that there is a direct connection between the firm performance and Putin's 'equidistance doctrine',

but we assume that there is a link between the negative figures and the troubled relation, based on the findings of table 1.

Evaluating oligarch performance in relation to Putin's equidistance doctrine has been an interesting field of research. It is an even more challenging topic in the light of today's debate in financial markets of short-term versus long-term focus on performance. Also the current financial crisis has affected the position of the Russian oligarchs, which is an interesting object of study.

Our research contributes to the academic literature by investigating firm performance of three oligarch owned companies over a specific period of time and by showing a change in performance after the introduction of a specific doctrine. We suggest further research could be done on different oligarch firms in other economic sectors to evaluate abnormal firm performance in the light of the equidistance doctrine. Finally, one could dig deeper into other measure techniques to evaluate the performance or compare the performance of oligarch owned firms with state owned firms.

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Annex 1.

Leading Industrial groups in Russia, 2002

Type of holding	Name of group	Name of leader(s)	Major assets		
Deep					
Gas	Gazprom	Miller (replaced Vyakhirev)	Assets of former Soviet Ministry of Natural Gas		
Electricity	UES	Chubais	Assets of former Soviet electrical monopoly		
Oil	LUKoil	Alekperov	Oil fields, processors, and pipelines		
	Menatep/Rosprom	Khodorkovskiy	Yukos (oil) Rospan (gas) Regional power stations (electricity)		
	Surgutneftegaz	Bogdanov	Surgut oil fields and affiliated enterprises		
Metals	Interros	Potanin	Noril'sk Nikel' (metals) Perm' Motors, Silovyye Mashiny (machine-building) Agros (agriculture)		
	Severstal'	Mordashov	Cherepovetskiy Metallurgical Combine, its suppliers, and severa customers		
	Metalloinvest	Kiselev	Rossiyskiy Kredit's metallurgical holdings		
Broad					
	Al'fa/Renova	Fridman, Aven / Veksel'berg	Oil (TNK, Onako, Sidanko) Aluminum (SUAI) Cement (Al'fa Cement) Telecommunications (Golden Telecom, Vympelcom, Vympelcom-R) Food products (United Food Company) Banking (Al'faBank)		
Deep and broad					
-	Bol'shaya MADAM				
	Millhouse Group	Abramovich	Sibneft' (oil) KrAZ, BrAZ (aluminum) Aeroflot (airlines)		
	Base Element (formerly SibAl)	Deripaska	SaAZ (aluminum) GAZ, PAZ (automobiles)		
	UGMK/ Yevrazkholding	Makhmudov/ Abramov	Urals Mining and Metallurgical Combine (metals) Magnitogorsk Metallurgical Combine (metals) Coal mines		
	MDM Group	Mel'nichenko	MDM Bank (banking) Coal Steel Pipes Fertilizer		
Narrow and shall	ow				
	Sistema	Yevtushenkov	Telecom companies		
	"2nd tier" groups		Often based on a single firm and/or concentrated within a single region.		

 ${\it Sources:} \ {\it Mukhin} \ (2001); \ {\it Dynkin} \ and \ {\it Sokolov} \ (2001); \ {\it Pappe} \ (2000, 2002); \ {\it Paszyc} \ and \ {\it Wisniewski} \ (2002); \ press \ accounts.$