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AHEAD OR BEHIND? LESSONS FROM RUSSIA'S POSTCOMMUNIST TRANSFORMATION

Introduction

Russia is a mirror in which we can see some of our own future. Sometimes the picture is optimistic sometimes threatening, but in general is far from what we currently tend to say about Russia. The main argument of this chapter is that the postcommunist transformation in Russia is—in our understanding—a specific blend of the communist past and a Western future in its experience of global change. In other words, postcommunism not only reveals the regional character of the current phase of transformation of the system but also corrects our understanding of globalization. Moreover, it puts forward concrete, regionally-based evidence as to its specific modes of operation and institutionalization.

The 'usual' conceptualization of transformation in Russia goes like this:

Russia has created the most corrupt market economy in the world and has buried democracy for a long time to come. The opposition forces, particularly those on the right, have practically disappeared. The media are rigidly controlled by the government. The oligarchs who did not support Putin have fallen from grace and are either behind bars, like Khodorkovsky, or have emigrated, like Gusinsky and Berezovsky. The Russian regions which used to fight for greater independence have completely surrendered to Putin the Victor. Not a single one of the country's 89 regions had less than 55% of voters cast their ballot for Putin. Many area specialists are now skeptical about the prospects for a convergence of the increasingly "uncivilized" Russia and a united Europe, while others even foresee a return to dictatorship.

The pessimism over Russian democracy was further reinforced by the terrorist hostage taking in Beslan in September 2004 and Putin's immediate proposals that governors be appointed (with the later approval of the regional legislatures) and that the Duma elections be based solely on party lists. The talk these days is more and more about a new authoritarian empire, within the boundaries of which one can already see the resurrection of the Soviet Union, like the Phoenix rising from the ashes, threatening not only the rights and freedoms of ordinary Russian citizens, but also the former Soviet republics, Eastern and Western Europe, in fact, the whole world...

This picture is at best incomplete—at worst false. In this light, a new perspective is needed, and we believe we are offering one here. Initially, then, a note of orientation is required to serve

as a guide to this chapter. Our analysis starts with a description of market reforms in Russia in the 90's and their social consequences. Next we discuss the multiple effects of these reforms on the Russian state. In the third section we explain Putin's quest for constructing a re-centralized, "strong" state. Fourth, we describe relations between democracy, institution building and rule of law in Russia. The fifth section forms the core of the argument by proposing a theoretical generalization based on the empirical material presented in the previous sections. It provides links between the transformation of the global scene with the regionally specific transformation experiences. Finally, on the basis of our discussion, we will lay out several key implications for the lessons we can draw from Russia's transformational path which will facilitate better understanding of a notion of the turning points in a global scene.

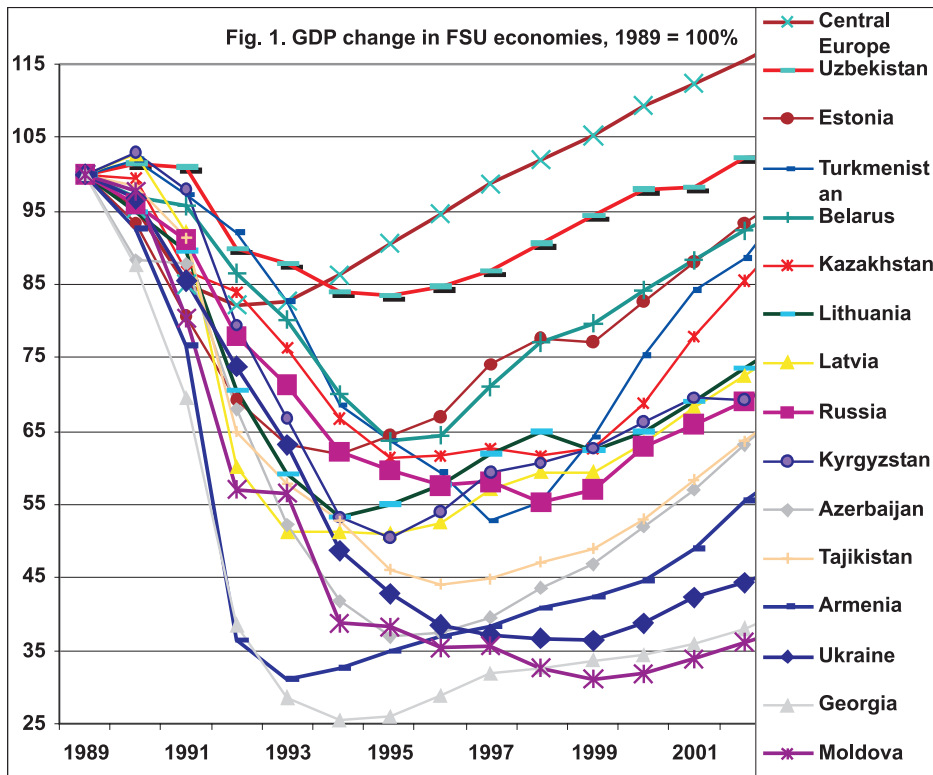
Big Bang—the economy and the social sector

Everyone knows, production dropped in the 90's in Russia; however, not everybody knows that this decline was of a magnitude unprecedented in the 20th century. Neither the First World War along with the revolutions of 1917, with the subsequent bloodshed of the civil war, nor the horrors of the Second World War brought about such a dramatic drop in output as was seen in the 90's. The national income fell by more than 50% between 1913 and 1920, but by 1925, 12 years later, had rebounded, surpassing the pre-war 1913 level. In 1998, at the lowest point in the transformational recession of the 90's, Russia's GDP was 55% of the pre-crisis peak of 1989—slightly more than the percentage of the 1913 level achieved in 1920. However, the current recession is lasting much longer: the GDP will only reach the pre-crisis 1989 statistic, at best, in 2009, four years from now (fig. 1). By way of comparison, the national income never fell that far during World War II. In 1942, it was 80% of the prewar 1940 level, then climbed back up to the prewar level in 1944, and then once again descended to the 80% mark in 1946 during the conversion of defense industry. But, by 1948, it had already substantially exceeded the 1940 level. So the economic losses from the 90's recession were exceptional in scale, greater than those suffered as a result of world wars and revolutions.

The transformational recession of the 90's in Eastern Europe and the countries of the former USSR was a phenomenon truly unprecedented in world economic history. The scale of the decline in production in Central European countries is roughly comparable to the losses of the Great Depression of the 30's—an approximate 30% drop in 1929–32 with the output restored by the late 30s (fig.2). However, the world had literally never before seen output drop by 50% or more and take 15–20 years to be restored. Examples of deeper and even more prolonged declines in production can be found in certain countries, but only in times of war, epidemics, natural disasters, and never as a result of economic policy. The drop in output in the countries of the former USSR is described in economics textbooks as the biggest manmade economic crisis in the history of mankind, that is, a crisis produced by the efforts of the policy makers¹.

Leaving aside the question about the reasons for the recession or how it could have been avoided, let us only point out that such an unprecedented plunge in production caused just as unprecedented tension in the social sector. In the 90's, real incomes and consumption decreased on average by a minimum of a third, which was less than the drop in production (since the recession was more significant in the defense and investment sectors, while consumer goods imports grew), but still very substantial. Moreover, due to the immense growth in income inequality, the real

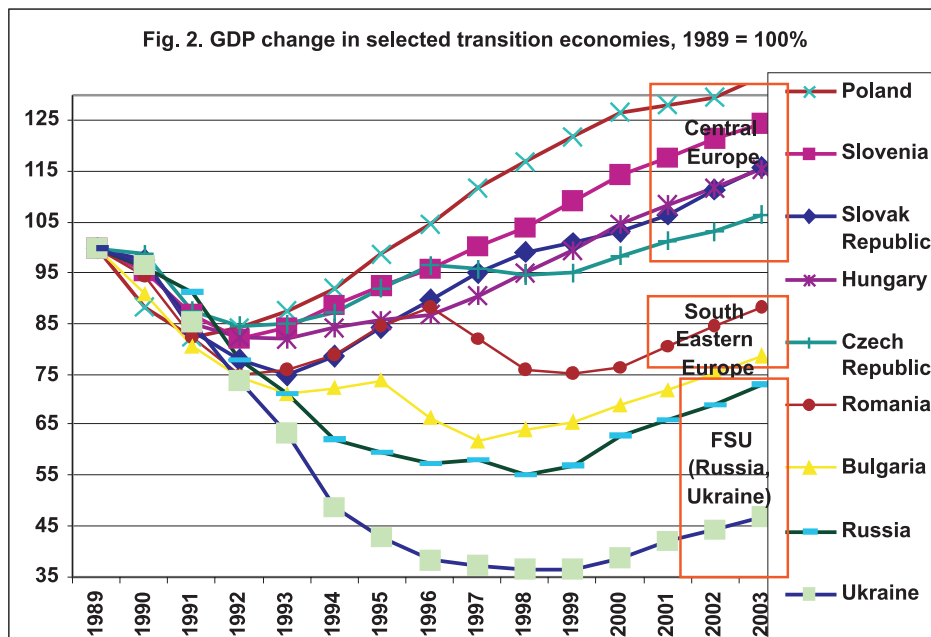
¹ See, for details: V. Popov. Shock Therapy versus Gradualism: The End of the Debate (Explaining the Magnitude of the Transformational Recession).—*Comparative Economic Studies*, Vol. 42, Spring, 2000, No. 1, pp. 1–57.



incomes of the absolute majority—80% of the more vulnerable population—were approximately cut in half. As for wealth inequality, during the privatization, there occurred a redistribution of national wealth of unprecedented scale. In just a few years, somewhere around a third of all state property passed into the hands of a few dozen oligarchs for a song.

Inevitably, the brunt of these hardships have been borne by society's more vulnerable groups because they have fewer resources with which to cushion the impact of economic decline and increased insecurity. This is further exacerbated by their limited ability to respond constructively (either by political or economic means) to rapidly changing circumstances and by a lesser capacity to protect their vital interests in the political process. Unfortunately, in today's Russia, the great majority of the population turned out to be vulnerable in this sense. It is difficult to exaggerate the degree of the resulting social and economic collapse. One would think that in such a situation it would have been impossible for policy makers to ignore the necessity to react as this posed a fundamental challenge to the Russia's future. However; it was not only ignored, but also exaggerated by the artificial but politically convenient creation of the hyper-rich class.

How do you explain to today's 20-year-olds, who don't remember the 80's, that people lived much better, on the average, under Soviet rule? They don't believe it. They think that the elderly habitually exaggerate the past, where they left their youth, never to return. But, the statistics are inexorable: the mortality rate has risen by 50%, the crime and murder rate has more than doubled, the suicide rate has almost doubled, and the average life expectancy has decreased by 5 years. Despite an influx of migrants from other republics of the former Soviet Union, the population of Russia has dropped from 148.5 million in 1991 to 143 million at the beginning of 2005.



Special studies² have shown that the increased mortality rate was, for the most part, not caused by reduced real incomes and the resulting deterioration in diet, not by smoking or alcoholism, not by the breakdown of the health care system or environmental pollution, and not by an upswing in the crime and accident rates. No, the main cause of the rising mortality rate was cardiovascular diseases in 40–50-year-old males, who could not deal with the stress of the instantaneous transition to a market economy. The stress index, determined by the unemployment rate, the frequency of changes in employment (firings and hiring) and place of residence (migration), the marriage and divorce rates, and disparity in income distribution, is an index that closely correlates with the mortality rate both in countries with economies in transition, as well as in Russia's regions. In China, where reforms were undertaken gradually, the life expectancy has grown from 65 years immediately after the death of Mao to its current level of 70 years, while in all other former socialist countries, including the GDR, the transition to a market economy has created so much stress that people have begun dying earlier.

The transformational recession was brought on not so much by the market liberalization, as by the virtual collapse of the state: countries that were successful in keeping government revenues and spending from plunging (Central Europe, Estonia, Uzbekistan and Belarus), the decline in production was less substantial. In contrast, in Russia and other FSU countries, apart from those mentioned above, spending on "ordinary government" (excluding spending on defence, investment and subsidies, and debt servicing) in real terms decreased three-fold and more, so that purely government functions—from collecting custom duties to law enforcement—were, to all intents and purposes, transferred to the private sector or were de facto "privatized."³ The state capture index, which was calculated by the EBRD on the basis of polls of enterprises in the late 90's and reflected the degree of subordination of government bodies to private interests, showed

² G.A. Cornia, R. Paniccia, Eds. *The Transition's Mortality Crisis*. 2000. Oxford University Press, Oxford, UK.

³ Piotr Dutkiewicz, Marketa Geisler, Vladimir Suchan, *Postcommunism and Globalization in: From Global Security to Transborder Initiative*, Cambridge/Kielce, 2000. ed.I.Suchanek, p.81–91

that Russia and the other new CIS democracies were much worse off than the Central European democracies and even the authoritarian regimes of Uzbekistan and Belarus⁴.

The shadow economy, which the most generous of estimates place at 10–15% of the GDP under Brezhnev, grew to 50% of the GDP by the mid 1990s. In 1980–85, the Soviet Union was placed in the middle of a list of 54 countries rated according to their level of corruption, with a bureaucracy cleaner than that of Italy, Greece, Portugal, South Korea and practically all the developing countries. In 1996, after the establishment of a market economy and the victory of democracy, Russia came in 48th in the same 54-country list, between India and Venezuela⁵.

The regionalization of Russia was happening in leaps and bounds in the first half of the 90's. In 1990, in an attempt to win the Russian regions over to his side in his battle with the Gorbachev government of the Soviet Union, Yeltsin promised them as much sovereignty "as they could digest." As a result, the percentage of the regional budgets in the revenues and expenditures of the consolidated budget increased, while the federal government was forced to haggle with the subjects of the federation over the division of powers, including financial jurisdiction. Many of them directly blackmailed the federal government, threatening to withhold money from the federal treasury. In 1992–94, agreements were signed with many regions, establishing different levels of tax contribution to the federal budget in each specific case. One of the Russian regions, Chechnya, virtually left the federation.

The voucher privatization of 1993–94 and the "loans for shares" auctions of 1995–96 led to state property being sold off for a pittance, and this at a time when the state needed money more than ever before. During the whole 18 months that the vouchers were valid, they were never quoted at more than \$20 a piece, so about 150 million vouchers, issued one per resident, were worth less than \$3 billion all told. This amount could have bought out somewhere around a third of all the assets in a country with an annual GDP of more than \$500 billion (purchasing power parity). At "loans for shares" auctions, companies with an annual output of several billion dollars were sold on the auction block for hundreds of millions. Yes, by and large, the privatization was legitimate, but the fact is that the laws were such that the supply of property was tens of times greater than the solvent demand, so plants, factories and banks went for simply ridiculous amounts. As a result, anyone who could call themselves the least bit well-to-do at the time not only had unlimited opportunity for incredible enrichment, but also took control of the economy of the former superpower. As journalists so aptly put it, the country ended up under the thumb of the "seven bankers" ("semibankirschina") along the lines of the "seven boyars rule" ("semiboyarschina") during the Time of Troubles of the early 17th century, the most anarchic period in Russian history between two tsarist dynasties.

The worst-case scenario — "privatization" of the state

An indispensable attribute of any state is a minimum of three monopolies—a monopoly on force, on tax collection and on currency issue. All three monopolies were undermined in the 90's. The unprecedented rise in crime and the notorious assassinations of leading politicians, journalists and businessmen testified to the bankruptcy of the law-enforcement agencies. The decline in tax revenue resulting from the growth of the shadow economy to all intents and purposes meant the "privatization" of those revenues by the bureaucracy and the criminal element, which took the place of the state as the "protectors" of business. The increased spread of monetary substitutes

⁴ J.Hellman, G. Jones, D. Kaufmann. How Profitable Is Buying the State Officials in Transition Economies?—*Transition. The Newsletter About Reforming Economies*, April 2000, p.8–11.

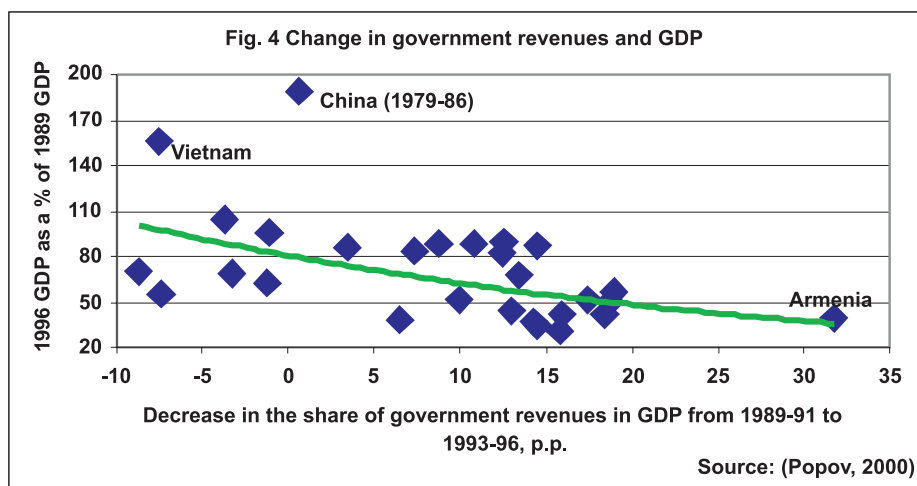
⁵ Transparency international (<http://www.transparency.org/>).

(bills of exchange of regional governments) in 1994–96 and the tremendous rise in barter and non-payment (trade and tax arrears), which peaked in the summer of 1998, right before the August crisis) virtually stripped the central bank of its power to regulate monetary circulation.

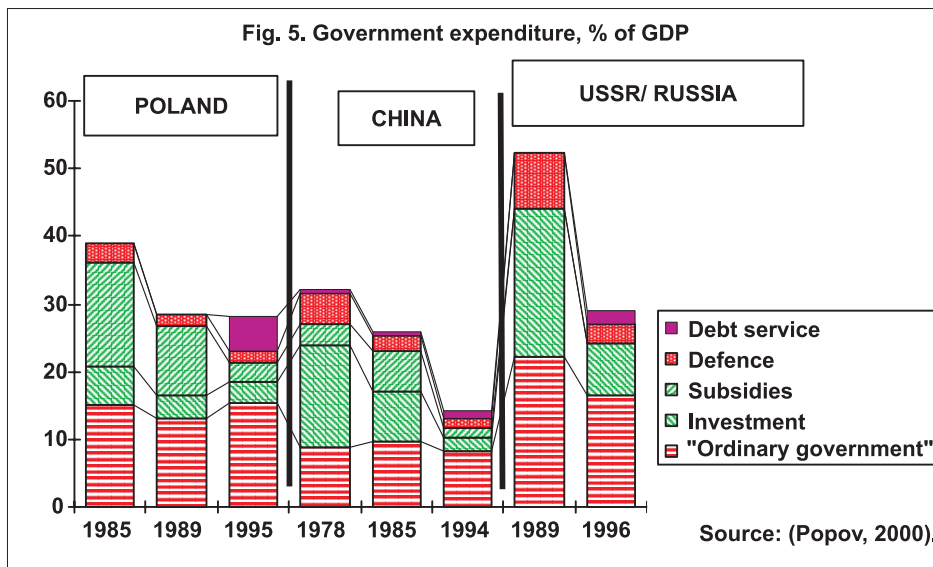
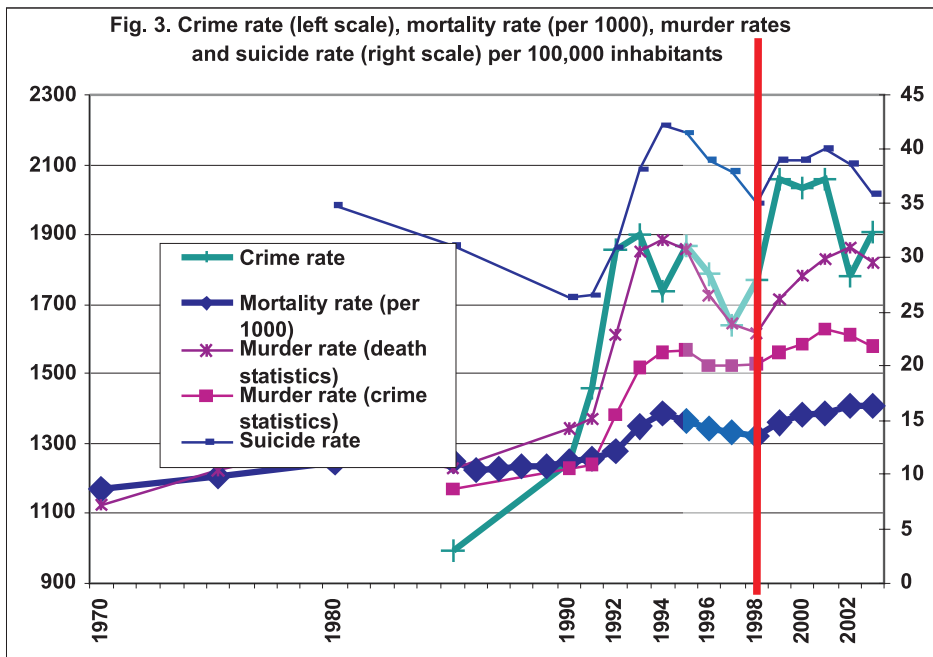
In 1995–98, in the period of macroeconomic stabilization, it finally became possible to bridle inflation by linking the exchange rate of the rouble to the dollar, and it seemed that things were going to get better. A small increase, but growth all the same (1%), was detected in 1997 after 7 years of unabated decline in production. The mortality, crime and suicide rates began to drop. However, there was no healthy underpinning to this stabilization—the pyramid of government debt and non-payments continued to grow, the real exchange rate of the rouble rose, undermining the competitiveness of Russian goods, the balance of payments deteriorated, and production slumped once again in 1998 due to the stubborn unwillingness of the authorities to devalue the rouble. As a result, in 1998, the short-lived stabilization ended in stunning failure after only three years—with the August devaluation of the rouble and default. Real incomes on a month-to-month basis fell by 25% in the fall of 1998, only climbing once again to the pre-crisis mark in 2002.

Immediately following the August currency crisis, economic growth returned, unemployment began to fall, although this was insufficient to prevent an increase in the mortality, crime and suicide rates. Although the official statistics did not capture this, it seems that after the August crisis the income inequalities intensified, with the incomes of the poorest population groups not only plummeting at the end of 1998, but also continuing to shrink in 1999–2002. Consequently, there followed a surge in the number of murders to more than 30 (!) per 100,000 of the population, as compared to 1–2 in Eastern and Western Europe, Japan and China, Israel and Mauritius (fig.3). Only Columbia and South Africa had a higher murder rate than Russia, while Brazil and Mexico had a murder rate of about half Russia's level. Even the US rate, the highest among western nations at 6–7 per 100,000 of the population, seems low in comparison.

The state crisis had reached its culmination: federal government revenues and spending fell in 1999 to 30% of the GDP at a time when the GDP itself was almost half of what it had been 10 years before. The state debt and foreign debt had hit a maximum; the currency reserves had shrunk to \$10 billion, less than in Czech Republic and Hungary with their population of 10 million (figs. 4–6).

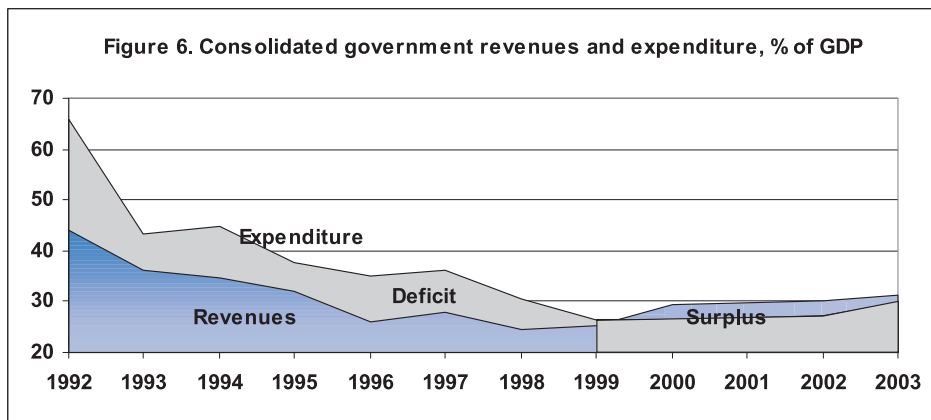


Even on December 31, 1999, when Yeltsin handed the presidency over to Putin (who had spent by that time 5 months as Prime Minister) and even in March 2000, when Putin was elected



President for his first term by a majority of 52.5% of the votes, the federal government was weaker than it had been any time since the civil war of 1918–21. In August 2000, the Ostankino television tower in Moscow went on fire and the nuclear submarine Kursk sank, and the feeling was that the federal government might as well just shut down it was so useless.

In 1997, the Russian oligarchs turned up for the first time in Forbes' list of the world's billionaires; five years later, in 2003, the same list included 17 names from Russia. With a per capita GDP lagging behind Mauritius and Costa Rica, with a life expectancy of 65 years compared to Cuba's 77, and with 25% of the population making an income below the subsistence minimum



(slightly more than \$2 a day by the official exchange rate), Russia had outdone all the countries of the world, except the USA, Germany and Japan, in the number of billionaires it had. In May 2004, Forbes had already counted 36 billionaires in Russia, which left Japan in the dust and Russia in 3rd place after the USA and Germany. A full and final victory for capitalism in Russia! The Russian robber-barons were the richest in the world! Incidentally, China, with a level of development similar to Russia's, has only one billionaire (not counting Hong Kong, where there are 11).

In its property and control structure, Russia was to be found in the middle between the developing and the developed world at the beginning of this century. In 2003, according to a recent World Bank study, 23 oligarchs controlled 35% of the industrial output (the state had 25%) and 17% of the banking system assets (the state had 26%). In the late 90's, in the USA, the 15 richest families controlled around 3% of the GDP, 2% in Japan, but 62% in Indonesia, 38% in South Korea and 53% in Thailand⁶.

However, it is unlikely that there are many countries where the oligarchs, first of all, started with nothing and became "world leaders" in only 10 years and, secondly, openly pitted themselves against the government, in effect demanding its privatization.

To find analogies one would have to go to the Latin American history: the overthrow of the Arbens government in Guatemala in 1954 by United Fruit Company of the U.S. or of the Allende government in Chile in 1973 by Anaconda and ITT, in both cases with the support of the CIA. True, in Russia the challenge came from homemade oligarchs and not American transnationals, and the army was after all on the side of the government, a valuable legacy of the Soviet past which is still have to be duly appreciated by future historians.

But it would be hard to name countries with a developmental level similar to Russia's, where the state lost so much of its independence in its relationship with "big capital" in the 90's. A virtual merging of big business and the middle management levels of the bureaucracy occurred in Russia, and their interests became practically indistinguishable one from the other. Neither the civilian ministries, nor even the top bureaucracy were able to counter this force; even the "power" agencies, such as the Ministry of Interior, the army and the security services began "privatizing."

As a result of this process, the division between private and public became blurred and the interests of mid-level bureaucratic and business elite merged; thus the state became neo-patrimonial (feudalized) and almost privatized. In such an environment, the issue of improving

⁶ S. Guriev, A. Rachinsky. Ownership concentration in Russian industry. Background paper for Russia CEM 2003 (<http://www.nes.ru/files/OwnershipConcentrationMarch2004.pdf>); S. Claessens, S. Djankov, L. Lang. The separation of ownership and control in East Asian Corporations.—*Journal of Financial Economics* 58 (2000), pp. 81–112.

equitable policies became irrelevant (as it is almost impossible to implement any kind of policy interventions that might allow change a situation of fusion of such powerful interests). The economic and social collapse served the elite well.

It is easy to imagine what would happen in Russia if the trends of the 90's were to continue. The continuing criminalization of the country, the complete "privatization" of the machinery of government by the oligarchs, the collapse of civil society, the weakening of the federal government as a result of the shift of real power to the regions, a battle between criminal groups, the oligarchs and the regional governors for the remaining power in an ocean of anarchy...In short, not the "wild west," but the "wild east."

This scenario may now look like a "communist horror story," but, just a few years ago, it seemed not only possible, but in fact most probable. In reality, what would the Russian "oligarchs" do, if they could completely determine government policy? Obviously, they would reduce the taxes that "strangle business and support the bureaucrats," as "any child could tell you" now. Either money would have to be printed to cover the budget deficit, or there would have to be cuts in spending—on education, health care, pensions and law enforcement. In either case, public dissatisfaction would damage the investment climate, so the oligarchs would consider it a blessing to move their money and their person to safer countries, as was the case last year with the governor of Chukotka, oligarch Roman Abramovich, who bought the Chelsea soccer club in England for a quarter of a billion dollars and, to all intents and purposes, moved to England.

To paraphrase Marx, you could say that the worst state differs from the best oligarchs in that it has a longer planning horizon. The oligarchs, despite all of their "civilizedness" and commitment to democratic ideals, nevertheless think more about profit in the here and now than they do about long-term national interests. Do you remember what the oligarchs were doing during and after the currency crash of 1998? In 1998, the oligarchs were "siphoning off" the assets of their banks into "clean" companies, leaving only debt in the bankrupt banks. In the end, most personal deposits were returned, but only under pressure from the government and only following five years of litigation. Is it at all surprising that the people supported Putin and not the oligarchs?

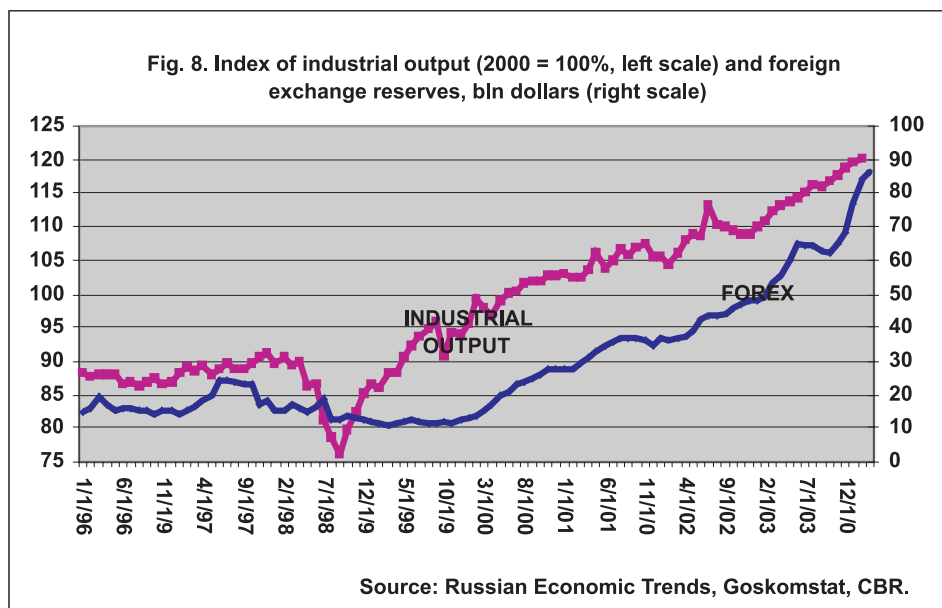
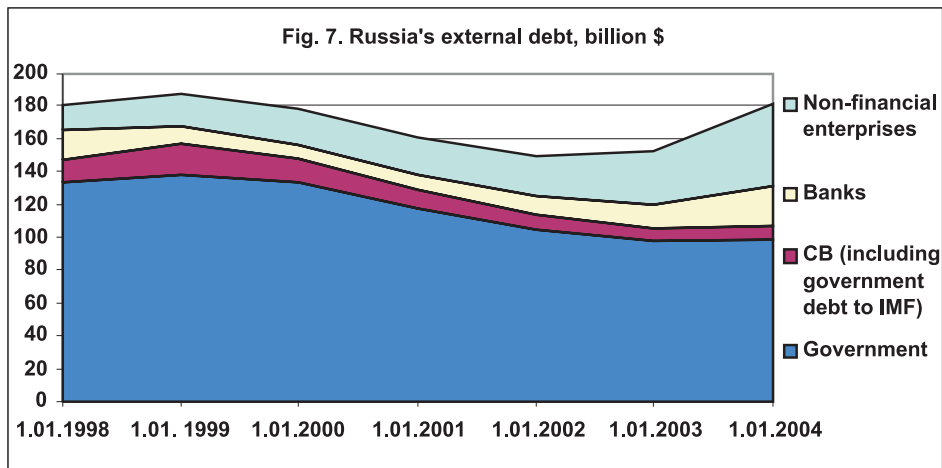
Restoring institutions—persistence goes the distance

The victory of "Yedinstvo", the "party of power", in the parliamentary elections of 1999 was, among other things, a victory for the have-nots (subsidized regions) over the haves (donor regions), which had joined forces in the Primakov-Luzhkov bloc "Otechestvo-vsya Rossiya". Putin tried to limit the all-powerful regions by changing the principles of fiscal federalism, appointing presidential viceroys in 7 amalgamated regions and reforming the Federation Council, the upper chamber of the Russian parliament, which represents the interests of all 89 regions. In 1999, Putin began and continues today to wage a second war against Chechnya, refusing to negotiate in any way, shape or form with the separatists. He launched court proceedings against the oligarchs, remaining, it must be said, within the limits of the law. They were accused of failing to pay taxes and engaging in financial machinations; some of them emigrated, others were arrested. The only non-governmental television channel, NTV, was shut down (incidentally, also for totally legitimate reasons, as oligarch Gusinsky had refused to pay off the debt to the state-owned Gasprom, having seemingly decided that freedom of speech was not worth that much money).

Meanwhile, the economy was continuing to revive: economic growth reached 6% in 1999, 10% in 2000 and 4–6% annually in 2001–2004 (fig. 1). Unemployment dropped from 13% in 1999 to 8% in 2003, and inflation shrank from 84% in 1998 to 12% in 2003–04. The budget deficit turned into a surplus, and the government revenues and expenditures as a percentage of the GDP began,

ever so slowly, to rise (fig. 6); the foreign debt as a percentage of the GDP decreased (fig. 7), capital flight decelerated and currency reserves expanded (fig. 8). The state began to regain ground, even though the process was extremely gradual.

But the most important result of the last five years is probably this: the growth of the economy and the stability of leadership have finally led to increased order and an improvement, although almost imperceptible, in the social climate. The number of murders, having hit a sky-high peak in 2002 dropped back down in 2003; the number of suicides has been on the decline for 2 years running (fig. 3); the birth rate, which struck a 50-year minimum in 1999, has begun to rise, as has the number of registered marriages (although this is partly a result of the demographic wave of the 70's); the divorce rate, having reached a maximum after many years, is now on the down slope. In effect, this means that Russia is gradually backing away from the edge of the abyss of anarchy and chaos, into which it systematically descended in the 90's.



It is these very improvements in the social sector in the past few years that inspire the most hope. Economic growth and low inflation alone cannot prevent the disintegration of the country if social inequality and crime increase. Building the vertical of power and intensifying centralization may not be able to stop the collapse of the state, if they don't bring about stronger law and order and limit the shadow economy. In fact, Putin has been criticized precisely for taking all the power into his own hands without greater order resulting. Well now, it seems that the first signs have appeared of a real, rather than an ephemeral, stabilization: the crime and suicide rates are falling, the mortality rate has leveled out, the number of marriages and the birth rate are rising, and the divorce rate is down. Yes, the trend is hardly noticeable and has only appeared in the last 2-3 years. Yes, notorious terrorist attacks have been undermining confidence in the authorities, but still there is a ray of hope, hope that was non-existent before.

Putin's popularity, which the polls say is, in fact, greater than 71% of voters who cast their ballot for him in the March 2004 elections (many of his supporters simply did not turn out to vote, as they were certain that he would win anyway), is explained precisely and primarily by his ability to stop the collapse of the state caused by the reforms of the 90's. All other problems pale in contrast to the threat of social and national disintegration. The majority of Russian citizens are prepared to forgive Putin his hard-handed tactics in dealing with the oligarchs and even with entrepreneurs of a lesser stature, and his "purgings" in Chechnya, and the constraints placed on democracy and freedom of speech, all in the interests of strengthening law and order and putting limits on a situation that knows no bounds.

Here is how Russians responded in polls conducted on the eve of the February 2004 elections. When asked what they expected first and foremost of the new president, 58% wanted him to reinstate Russia to its status as a great and respected power; 48%—to ensure a just distribution of income in the interests of ordinary people; 45%—to strengthen law and order; 43%—to put an end to the war in Chechnya; 41%—to return the funds that ordinary people lost during the reforms; 39%—to strengthen the role of the state in the economy. Such priorities as "keeping Russia on the road of reform" and "continuing the policy of closer ties with Western countries" garnered only 11 and 7% respectively. "Are you concerned that Putin could establish an iron-fisted dictatorship supported by the 'power agencies'?" In January 2000, before Putin's first presidential elections, 34% said yes to this question, while in January 2004, 26% showed concern. Respectively, 57 and 67% showed no concern⁷.

Where is Russia headed? The future harbours many obvious dangers. The current real exchange rate of the rouble (the ratio of domestic to world prices) is too high. It has been growing throughout the past 5 years and in 2004 has reached the 1998 pre-crisis level. Therefore, a drop in world energy prices could easily provoke a new currency crisis and interrupt economic recovery, despite what would seem to be the major contribution to stability provided by the large currency reserves. Domestic fuel and energy prices remain several-fold lower than world levels, creating incentive for inefficient energy consumption and the highest energy intensity in the world. And so, unlike Eastern European countries and many of the former Soviet republics, where the price of energy sources is already approaching world levels, the restructuring of the Russian economy is still far from complete. What Russia should have done in past years was slowly devalue the exchange rate of the rouble, accumulating reserves even faster, and at the same time increase domestic prices for oil, gas and electricity, compensating the producers for losses from the rising cost of energy with the benefits of stronger competitiveness resulting from the depreciating rouble rate. However, such a policy is not even on the drawing board for the moment.

Another danger is too rapid a decrease in taxes, which the government has already implemented and plans to continue implementing (income tax, corporate tax and the unified social

⁷ Press releases of VTsIOM (<http://www.levada.ru/press/>).

tax). The critics of such measures, including the Moscow office of the IMF, justifiably point out that the current revenues of the budget and the current surpluses are based primarily on high prices for energy sources, and, therefore, if these prices should fall, the government could once again find itself penniless.

Other dangers also continue to exist: the absence of tangible progress in the battle with corruption, crime and social inequity. But, the danger of the death of Russian democracy and of Russia's transformation into an authoritarian regime, which will, moreover, threaten its neighbours—according to us is not going to materialize. Obviously, democracy is imperfect in Russia, but where is it perfect? It looks like Russia is on the way to having a “one-and-a-half-party system” (one big ruling party and many small opposition parties), which has existed and still exists in many countries, from India to Mexico and from Japan to Botswana. To all

appearances, this system is far from the worst-case scenario for developing countries with weak law and order. Furthermore, there is convincing evidence that democratization in countries with poor rule of law undermines institutions and leads to the decline of growth rates, and to the increase of social disparities and crime.

Perhaps the most convincing example in this context is Hong Kong, where the British colonial authorities only began introducing rudimentary democracy on the eve of the handover of the territory to China (but did not in the end manage to complete the job), which in no way kept Hong Kong from surpassing its mother country, the birthplace of democracy, in GDP per capita. At the time, under the British, and now, under a communist government, following the handover of Hong Kong to China, law and order in Hong Kong remains at a level unattainable for the majority of the world's countries, although the democracy that never was still doesn't exist. Or, take the example of Haiti. Little law and order, but lots of democracy with 30 coup d'états in 200 years, the latest in March 2004 involving the deployment of foreign troops to stop the wave of banditry. What country would you like to live in, which neighbour would you prefer to have?

Institutions and democracy

One of the most fundamental issue for the region's citizens is one of democracy. Democracy as we know it today has many faces. Who does not claim today that democracy is a good thing? Those who have their system “democratic” are those “civilized” by contrast to the noncivilized part (actually the majority) of the world. What politician and government today do not claim that they do not plan to maintain or extend democracy, in some cases even globally? But it all depends on the content we put into a word. One possible definition, of course focuses on the guarantees of freedom from arbitrary political power.⁸ This approach can lead us in the direction of looking at citizen's rights from the individualistic liberal position (the set of so-called civil liberties would usually include guaranties of free and fair elections, a multiparty system, a lack of direct political control over the media, opportunity to profess one's religious faith, etc.). We recognize how valuable these rights are in particular when they are subjected to constraints, or become unavailable, as one sees in recent Russian and Eastern European experience. Yet there is another serious but under-discussed dimension within the debate about how democracy should be measured. We would wager the thesis here that for the majority of the population in Russia—as well as in most transitional societies—(all the while civil liberties are seen as valuable, desirable, and important), the quality of the political process is somehow measured differently. The issues that are of primary concern to most people hit by enormous dislocations, and accordingly their political priorities, are

⁸ Immanuel Wallerstein, *The Decline of American Power*, The New Press, 2003, p. 150

focused predominantly on their and their children's (a) prospects for material well being (and a fear of the consequences of growing material inequalities), (b) corruption, and finally their (c) chances to be equal citizens within the state (by eliminating sources of discrimination based on age, disabilities, gender, ethnicity etc.). Did we ever seriously ask what the democratic priorities for the majority of the population are, and how one might address them? Therefore, as we can see, the discourse about democracy (which is mainly an intra-elite discourse) should also include these other substantive issues, and submit them to consultation by citizens, not limiting the matter to its Dionysian face or to various mimeries of the "civil liberties" scorecard.

Popular demand for democratization for the "average person" is in part mainly a demand for a more fair redistribution of accesses to health, education and lifetime income). There is nothing wrong in the fact that people are concerned for themselves and their families and would like to prolong their lives in good health, arrange education for their children to improve their life opportunities, and worry about the stability of their incomes. At the moment at all these fronts we witnessed a massive retreat in Russia between 1991–2001 and a meager improvement at best from 2001–2005. The unequal participation in "transitional rent" seems to us to be the main cause of the growing gap between the democratically elected elite and the public. The main problem of the late 1990s in Russia is that such a gap (or rather series of a fundamental gaps) was barely mentioned by the policy makers and politicians, as if it did not exist, with the consequence that people felt deeply betrayed by their own elites. Only a few were able fully to use the fruits of democracy. We call this phenomenon a **commodification** of democracy in the region.

That is, "democracy" became a commodity in Russia like anything else (a "thing" that one can buy and sell on the "democratic market"). By buying access to the political process, the redistribution of property, the media, and decision makers and politicians (in other words, the purchase of civil liberties for specific narrow interest groups), those few who were able to do so became the de facto owners and enjoyers of democracy. Politically speaking, the most profound result of this process was the liberation of the elite, mostly political and business figures, from the state, from the executive powers that it represents, and from the rest of the population.

Corruption is not a new phenomena and exists in every system. In our part of the world it seems that we started to believe that everything is happening only because of corruption as, it seems to be the most obvious grease that enables things to go smoothly. Therefore there is enormous amount of the cynicism on this subject but overt bribery we argue (as the exchange of payments for services) is rather a small part of the story. A much more fundamental issue is the degree to which money buys political and economic access. When almost an entire Russian elite's economic and political success in the mid 1990s was mostly dependent on corruption (i.e. privatization), that means the state failure. It also means the commodification of democracy by which we mean a situation in which narrowly defined interest groups (using existing democratic procedures) could have literally bought Russian regions and could have significantly (in a very short period of time) increased their economic power base by purely political means⁹.

How to achieve the effectiveness of institutions when carrying out market reforms (liberalization)? If we speak not of specific measures (which are in principle known), but rather of a general approach, the question inevitably moves beyond the realm of economics and into the domain of political science. Government institutions can be effective in both authoritarian and democratic regimes. Both have proven capable in principle of ensuring an institutional environment conducive to economic growth. At the same time, it is known that in countries without solid democratic traditions, the transition from authoritarianism to democracy is usually accompanied by a reduction

⁹ Citizenship is an under-discussed issue in Russia (defined as the level of inclusiveness in the society). Sources of discrimination that jeopardized full membership in the society such as gender, class, age, disability for instance, that everyday affects millions of people were barely on the agenda.

in the effectiveness of institutions. Time is required—not only in Russia— to create new, hitherto non-existent democratic institutions, and so the transitional period, when the old authoritarian institutions have already been dismantled, but the new ones are not yet in place, is the most institutionally vulnerable.

Liberalism refers to the degree to which the rights of the individual and economic agents are guaranteed. This applies to property rights, contractual rights, creditors' and debtors' rights, the right to protection of the life and dignity of the individual, and the right to just judicial recourse. It is natural that only strong institutions, above all state institutions, can ensure these rights since "private property cannot exist without the state." Under this approach, Europe became liberal and only later democratic. In the 19th century, in European states, the rights of the individual and companies were more or less ensured, although these countries could in no way have been called democratic. At the turn of the century, more than half of the adult population did not have the right to vote due to settlement requirements, as well as property and other qualifications, and mostly due to the fact that women were not permitted to vote. The first European country where women were granted the vote was Finland. At the turn of the century, this right was bestowed upon the better half of the population of the then Russian colony by a tsarist government that could not be called the most democratic in the world. The countries of East Asia, which had achieved impressive economic successes in past decades, went the same route (some are still on the way), from liberalism to democracy¹⁰.

The countries of Latin America, and then Africa took another road—first democracy, then liberalism. Democracy without liberalism, that is, without effective institutions to guarantee the rights of its economic agents, has turned out to be a less than favourable economic environment. Africa and Latin America lost ground in the world economy in the postwar period, falling behind in the GDP per capita growth rates.

In the 90's, many Soviet republics and Southeast Asian countries joined the ranks of illiberal democracies, with similar economic development ramifications. Strictly speaking, the Latin American countries are already close to creating effective institutions, judging, for instance, by the confidence in government index (which is approximately the same as in Southeast Asia and the Middle East). As for Africa and the CIS, they are for the moment very far from doing so, farther than any other major economic regions of the world. Liberalization does not work for these two regions, and so they do not fit into the framework of traditional economic wisdom. In the 90's, only these two groups of countries continued to fall behind the Western countries in their level of development (per capita GDP), and it seems this trend will be maintained until they have created effective institutions capable of transforming illiberal democracies into liberal ones.

In other words, whether we like it or not, democratization without truly guaranteeing lawfulness and law and order; has an adverse impact on economic dynamics, and sometimes even leads to a slump in production. This is the price that has to be paid for early political democratization, that is, for the introduction of the procedure of democratic elections at a time when fundamental liberal rights have not yet become established in society. If you group the countries according to the degree of law and order (such indices are calculated by the World Bank) and the level of democracy (Freedom House political rights index), then the worst economic dynamics are observed precisely in those countries with an unfortunate combination of weak rule of law and a relatively high level of democracy. In the average instance, authoritarian regimes with weak rule of law are not very good for the economy either, but are still better than the democratic ones. It would seem that they are capable of compensating for their lack of law with an excess of order; that is by filling in the institutional vacuum by authoritarian means.

¹⁰ F. Zakharia. The Rise of Illiberal Democracies.—*Foreign Affairs*, Vol. 76, No. 6, November/December 1997, pp. 22–43.

Statistical accounts demonstrate that democratization in the world in the past 30 years has led to an increase in growth rates only in those countries where rule of law has been up to scratch; in contrast, countries with weak rule of law have seen democratization lead to deceleration of the growth of state revenues and deterioration of the effectiveness of the machinery of government, expansion of the shadow economy, growth of the budget deficit and inflation and, finally, downturns in economic growth rates and life expectancy. The constraints of this article will not allow for presenting the regression results, but these do exist¹¹.

In addition, the system of priorities or, if you like, life values, varies in countries with different developmental levels. People over the world value not only material well-being, but also social equality and justice, security, a clean environment, the possibility of living to a ripe old age, and much more; but, the relative value of these prosperity indicators is different. What should an unexpected injection of an additional billion dollars into the federal budget be used to finance? Wildlife protection, the battle against child mortality or the fight against crime? The answer would be different in Columbia and the USA, as would be the reply regarding the relative value of democracy. Needless to say, in a poor country with a low life expectancy and high crime rate, the voters are more likely to support the program for economic recovery, mortality reduction and establishment of order; even if this means placing limitations on democracy¹². There are more than enough examples of this kind of voting from Pakistan to Russia.

The uncompromising proponents of democracy ("here and today") will naturally answer, no matter what, that democratization is not only a goal, but also a means to achieve other developmental goals, such as improving life expectancy, and ensuring social equality and low crime levels. In truth, does not democratization lead to establishing strict control over the activities of government officials, to reducing corruption, to increasing the effectiveness of government, as well as to ensuring a more even distribution of incomes? Yes, it does, but only under one indispensable condition: that a certain level of the rule of law is established, and that all civil rights and freedoms of the individual, apart from democratic ones, are ensured.

We will, therefore, risk concluding this section by saying that the shortest path to full-fledged liberal democracy in countries with a low level of rule law, including Russia, lies not through immediate democratization "at any price," but rather through strengthening order based on the rule of law. Immediate universal election of officials where rule of law is at a low level leads only to "privatization" of democratic procedures themselves, to the buying and selling of officials' services on the political market, where the winner is, of course, big business, and the majority of ordinary electors are divested of any influence they could have had on political decision-making.

Dramatic economic collapse between 1991–1999, slower than expected recovery (2001–2005), parallel social and institutional upheavals and an explosive growth of poverty that we have outlined above were the main causes of the growing gap between the democratically elected elites and the public. The main problem of the late 1990s was that such gap (or rather series of a fundamental gaps) was barely mentioned by the policy makers and politicians as it did not exist, while people felt deeply betrayed by their own elites.

The key question for any Russian statesman (current and future) is how to re-bureaucratize the state (again making it a citizen-oriented public domain). Usually the first task in such a situation is to impose a regular and predictable line of command and then a *Rechtstaat* (state of law) which is historically the only by-pass to further democratization. Let us risk a statement

¹¹ VPolterovich, V. Popov. Democracy and Growth Reconsidered: Why Economic Performance of New Democracies Is Not Encouraging.—Paper presented at 6th GDN Annual Conference, Dakar, 2005 (http://ctool.gdnet.org/conf_docs/PopovDemocracy2004Aug.doc and http://ctool.gdnet.org/conf_docs/PopovDemocracy-charts%202004.xls).

¹² Also democracy is an expensive project and many bureaucrats are tempted to "scratch" for the system to be more competitive internationally.

that what many see as a process that marks the beginning of the end of the new-born Russian democracy, we see—in the right political environment—as a chance or even a prerequisite for the beginning of a process of further democratic consolidation. Obviously there are multiple and very real risks involved, such as the inevitable struggle between those who would like to see in the new situation a state of rule of law and those who would stop short on the stage of the rule by law that obviously will effectively block any reasonable prospects for a liberal democracy. The other issue is the quality of the law itself. Therefore, the process is anything but certain. As usual, there will be many interest groups ready to “capture” the process for their own narrowly defined ends (including private enrichment). There will be also genuine protests from those who feel that diminishing the scale of civil liberties is unacceptable (and their claims should be taken very seriously). The point is, however, that to sustain the democratic process in Russia would have been impossible without the measures taken by Putin (or any other leader in the position of real power in Russia), taking into account the scale of the state collapse combined with the effective privatization of its key functions.

Global lessons from the local experience¹³

Is Russia the enigma of the 21st century? We would rather see Russia as being a massive social and political laboratory with many experiments exercised on the country’s living social organism. As with any experimental endeavor of such scale, there might be some generalized conclusions to be drawn. We tentatively offer ten of them.

The first is related to the relations between postcommunism and global change (sometimes labeled as “globalization”). We would offer a proposition that globalization and postcommunism are twins because they came into existence together, both in fact owing their life to the death of Communism in the form of the so-called Soviet-type “real socialism”. Remarkably, however, much of the current literature either ignores or downplays the singularly essential fact that, without the fall of Communism, globalization—the removal of the bipolarity of the world and its replacement with one global system—would be by definition substantially different. In a word, the end of Communism made globalization both possible and credible. At the same time, with the removal of the “second world” of Communism, the “third world” of the developing countries ceased to be what it was as well.

Secondly—we argue—the working class ceased to exist as a politically active and effectively organized force (even if its only latent power in the last stage of the system was the ability of not producing, but being paid). This is perhaps the single most important result of the demise of Communism that has been generally overlooked. Equally remarkable is the fact that this dissolution of the political power of the working class came about not only with its acquiescence, but also, at least initially, with its active backing. As Timothy Garton Ash astutely put it, “the people had deleted the People.”¹⁴ In the place of working-class solidarity and collectivism, society placed its faith in various channels of liberal and conservative individualism. As a result of these seismic transformations, therefore, the solidarity of the poor with the poor quickly broke up both within and without the former communist bloc.

¹³ This section owes much to the forthcoming article by Piotr Dutkiewicz and Vladimir Suchan: “The Twins of Postcommunism and Globalization” in: Teresa Rakowska-Harmstone and Piotr Dutkiewicz (eds.): *Lesson from EE transition*, Collegium Civitas and Polish Academy of Science Publisher, Warsaw, Forthcoming: 2005. We are grateful to Dr. Vladimir Suchan for allowing us to draw from the arguments presented in that joint article.

¹⁴ Timothy Garton Ash, *The Magic Lantern* (New York: Vintage Books, 1999), 12.

Thirdly, we argue that globalization and postcommunism can be observed and analyzed as forms that imitate each other in dialectical mimesis. Implementation of the neo-liberal blueprints regionally led to strikingly similar consequences. Postcommunism built its own market economy and liberal-democratic political shell (with parliaments, elections, banks, cellular phones, charity dinners and all the other ingredients of Western systems). What is important, however, is that this shell hides different content than in the West—most of the time the West takes the form for the content. Banks are not the same as banks, the media play their political roles, the police are far from performing the same functions as their Western counterparts, corruption is smarter; political elites are not accountable, states are frequently adrift, the law sometimes operates selectively, organized crime is tougher, and even wars are different (in most cases they are conducted against their own citizens). The list could go on, but the point is that postcommunism can be seen as a mutation of communism and neo-liberalism made under increased pressures (or even guidance) from the global economic and technological environment (globalization).

Fourth, the particular character of this mimetic reflection is that it has the power to show or unveil what is elsewhere still obscured and undetermined. This especially appears to be the case with regard to what postcommunism can tell us about the emerging nature of globalization. Namely, that the problematic practice and experience of postcommunism—especially in its large-scale economic and social dislocations, merciless monetarization of politics and criminalization of society in the place of “civil society” and the rule of law, and purposeful un-politization of society—are not so much embarrassing “aberrations” or “deviations” from the “right” path of globalization (or “erroneous implementation” by the Eastern European politicians, or as some say “history’s long degeneration”) as they are rather crude manifestations of emerging global trends. In this perspective, what is called “globalization” in Eastern Europe may very well be a mirror held up in advance to the processes and structures yet to come in more industrialized countries.

Fifth, the empirical evidence shows that the transitional market economies (in our case Russia, but this is equally valid for most Eastern European states) are either far from being prosperous, or benefit only a minority. The costs associated with the launching of the transition are visible everywhere in the form of growing income differentiation, health problems related to the so-called “transitional stress,” child poverty, and homelessness (these are particularly statistically notable in CIS countries and South Eastern Europe). Inevitably, the brunt of these hardships has been borne by society’s more vulnerable groups, because they have fewer resources with which to cushion the impact of economic decline and increased insecurity. This is further exacerbated by their limited ability to respond constructively (either by political or economic means) to rapidly changing circumstances and by a lesser capacity to protect their vital interests in the political process.

Sixth, the rule of law in many instances remains arbitrary, sporadic and politicized. Court systems are still inadequate and cases remain unclosed for many years.¹⁵ In some cases, the rule of law is “instrumentalised” by elites for their own purposes. In other words, in too many cases law depends on the will of whoever is in power.

Seventh, abuse of the system and widespread corruption have become systemic. State elitism and paternalism, societal atomization, apathy, feelings of anomie, low efficacy, distrust of all things political, and a retreat to the private realm all seem to flourish along with dynamism, initiative and self-confidence. It is not surprising then, that the public has become disillusioned with “democracy” (as is well documented by the opinion polls from most Eastern European countries, in particular from the mid-1990s to the end of the decade).¹⁶

¹⁵ For instance in Poland, the highly publicized court case of Fund of Servicing Foreign Debt (FOZZ) for alleged fraud of tens of millions of dollars is continuing without a ruling for the last fifteen years by 2005—probably the dubious new Guinness Record: *Polityka*, Warsaw, No.8 (2492) 26 February, 2005: 24.

¹⁶ Data available include variety of surveys from central Europe and Russia

Eighth, the communist and postcommunist modes of appropriation have one important thing in common: the essence of such power is its nihilistic character, which can be defined as a disrespect for, or indifference to, the notion of justice and the common good (defined in national or community terms). Conversely, the nihilistic core of this political economy is the will and the relative freedom to cross the boundaries of the good or the permitted, including morality and positive law.

Ninth, the Eastern mutation of capitalism is transformed into a system of a complex symbiosis between nominally legal structures and “organized” crime that becomes not only a systemic economic force but also a political actor in its own right. As Ken Booth has indicated, this postcommunist liberalism or reinvented liberalism, which he calls “hyperliberalism,” “is globally more of a threat than hypernationalism.”¹⁷

Tenth, this new, altered form of liberalism may be dubbed “lumpenliberalism.” To paraphrase Marx, “in the way it acquires wealth and enjoys it, the winners are the lumpenliberals, the forces of a new order, reborn at the pinnacle of global society.”¹⁸ These ruling “lumpen” elements also form a new transnational class to which can be applied the characteristics used by Marx to define his “lumpenproletariat;” that is, they constitute a class “without a definite trace,” “without hearth or home, varying according to the cultural level of their particular nation.”¹⁹ Like the old lumpenproletariat, the new lumpenliberalism is a “charitable organization” of sorts by means of which the winners “provide themselves with charity at the expense of the nation’s labor.”²⁰

Conclusions

So what can we in the West learn (as globalizers, that is) from this regional experience? In our view, the agenda comes down to at least three main lessons. These are the following: (1) The welfare state is costly, in particular when state-provided services are of a relatively good quality, and so lesson number one is that one can dismantle such costly machinery with no significant political costs (please note: social costs are not a relevant argument here). (2) Eastern Europe served as a laboratory for a second important test—how far can one push labor without significant social protests and dislocations? Lesson number two, then, is that one can make labor flexible enough to diminish their collective demands to a bare minimum, and push them almost as far as possible, while still containing social protests. (3) Lesson number three is that the co-optation of local elites is less expensive and requires less energy than was originally thought. Not only that, these same elites themselves might become willing agents for global interests.

Thus, postcommunism in our understanding is a specific blend of the communist European past and the future of the West in its experience of globalization. It is a mirror—as we already said—in which the West may see some of its own future. There is nothing Machiavellian or cynical in this interpretation. Obviously we do not think in terms of a “Western plot.” Simply, Eastern Europe has taken the lead in the experience of globalization largely by default rather

¹⁷ Ken Booth, ed., *Statecraft and Security: The Cold War and Beyond* (Cambridge and New York: Cambridge University Press, 1998), p. 348.

¹⁸ See Karl Marx, “The Class Struggles in France: 1848 to 1850,” in Karl Marx, *Surveys from Exile, Political Writings, Volume 2* (New York: Penguin Books, 1992), p. 39. Marx’s original sentence reads: “In the way it acquires wealth and enjoys it the winners are the lumpenproletariat reborn at the pinnacle of bourgeois society.”

¹⁹ See Karl Marx, *ibid.*, pp. 52–53; cf. Karl Marx, “The Eighteenth Brumaire of Louis Bonaparte,” *ibid.*, p. 197.

²⁰ J. Hryniewicz, *Political Context of the Economic Development*, Warsaw 2004,

During the last ten years the salaries of top managers in the US have increased on average by 340%; if in 1980 an average yearly salary of a top US manager was equal to 42 yearly blue collar worker salaries, by the year 2000 the ratio was 1 to 531, without any dramatic growth in productivity: J. Hryniewicz, *Political Context of the Economic Development*, Warsaw 2004, p. 280

than through aims of its own making. This default pioneer status arises from the very fact that Eastern Europe is plowing through the most complex economic and social project of the last century, guided only—or rather misguided—by strategies which in most cases are entirely irrelevant to this new experience. It is obvious to us that this experience is of utmost value—not only to social scientists—and provides invaluable insights into one of the key turning points of history.

