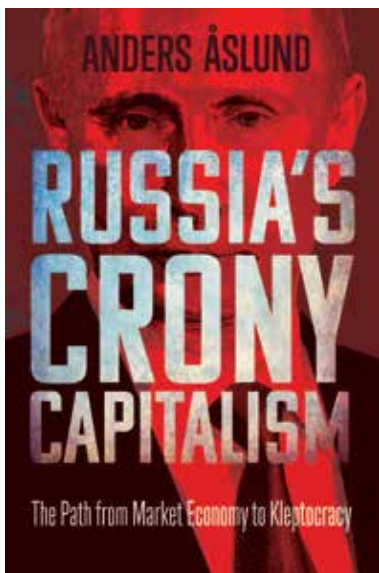


How *He built four circles of power.* Vladimir Putin Rose to the Top



An excerpt from
Russia's Crony Capitalism by
Anders Åslund (Yale University
Press, 2019).

With the help of his loyal friends, [Russian President Vladimir] Putin has built three circles of power—the state, the state enterprises, and the cronies' companies. Putin's first term appears to be a masterpiece of consolidation of power by a budding authoritarian. He was everything to everyone. In the eyes of liberals, he pursued excellent market economic reforms and seemed to build the rule of law. The giveaway was his immediate clampdown on independent television, which was well understood by human rights activists, but he pursued an elaborate salami tactic, cutting off one television channel after the other, accusing each one of poor finances or specific crimes.

State power comprises Putin's first circle. As chairman of the FSB in 1998–1999, he seized control over the secret police. In the summer of 2000, he took charge of television. Next, he established his “vertical of power” over the federal and regional administrations. His “dictatorship of law” over the judicial system ensued. In the elections in December 2003, Putin gained solid control over the State Duma and the Federation Council. At the Security Council, the pinnacle of power, his top men are three contemporary KGB generals from St. Petersburg, his successors as FSB chairs—Sergei Ivanov, Nikolai Patrushev, and Alexander Bortnikov.

Putin's second circle consists of the big state enterprises. He seized control of them one by one, starting with Gazprom in May 2001. He appointed his loyalists as chief executives and chairmen of their supervisory boards and rounded off his victory lap with the formation of the state corporations in 2007. The state

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enterprises have been allowed to expand with cheap state funding, often monopolizing their sector. They have been buttressed with protectionist measures, and the only governance that matters is obedience to Putin. Russian state capitalism is peculiarly disinterested in competition, investment, technological development, entrepreneurship, and productivity. The state sector is treated as a source of power and rents instead of an object of economic growth. The three top state managers are Igor Sechin of Rosneft, Alexei Miller of Gazprom, and Sergei Chemezov of Rostec.

The third circle is more idiosyncratic. It comprises Putin's top private cronies and their companies. The four top cronies appear to be Gennady Timchenko, Arkady and Boris Rotenberg, and Yuri Kovalchuk. Their activity usually appears not only corrupt but kleptocratic. Yet because he controls Russian legislation, Putin has legalized many of their dubious activities. The cronies are entitled to buy assets from state companies at basement prices and provide state procurement at high prices without competition. Since 2006, the ruble has been fully convertible and Russia maintains liberal currency regulations. The cronies can thus transfer their palpable gains to offshore havens.

International offshore havens form the fourth circle. The two biggest offshore havens are the United States and the United Kingdom. The United States even allows law firms to circumvent bank regulations on a massive scale. The U.S. and UK acceptance of secrecy of ownership and anonymous currency inflows is critical for the sustenance of the Putin regime.

The Putin economic system is based on monopolies and cartels. The most important economic sectors are divided among a few companies, which in turn are each dominated by one person. Oil and gas production belongs to five companies—Gazprom, Rosneft, Novatek, Surgut, and Lukoil. Pipelines are built by the companies belonging to either the Rotenbergs or Timchenko. The crony company Sogaz is the leading insurance company. Rotenberg's Mostotrest is responsible for big road construction projects. Mergers are allowed, but antitrust is not. Creative destruction appears to be declining, as is new enterprise formation. Competition is dissuaded or worse, allowing the incumbent companies to

reap monopoly rents. Outstanding new entrepreneurs tend to emigrate. The South Korean *chaebols* (family-owned conglomerates) are quite an inspiration. This system is the opposite of a competitive market economy.

These four circles comply with the German fascist thinker Robert Michels's idea of the iron law of oligarchy, with various circles of power reinforcing one another and, eventually, all organizations controlled by a leadership class. In 1993, Daniel Yergin and Thane Gustafson published a book offering various future scenarios for Russia in 2010. One scenario, the "two-headed eagle," is remarkably similar to contemporary Russia. It "is based on a coalition of three groups, managers of large industries (with the defense industries at their core); the central bureaucracies in Moscow; and military, police, and state-security officers." The only elements missing are the cronies and the financial offshore havens.

The countries that are most comparable to Russia are China and Brazil, which are both big countries with a system of crony capitalism that are at a similar level of economic development, but they are very different. China is fast-growing and innovative, still ruled by the Communist Party. The Chinese state sector is far smaller than the Russian, and shrinking, and China is more decentralized. But Russia has a freer market than China and has long been recognized as a market economy by both the European Union and the United States.

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Brazil appears to be a more relevant comparison for Russia, but its disparities are also great. However imperfect, Brazil is a democracy, and it has a surprisingly strong judicial system that, in sharp contrast to Russia, has sentenced its past three presidents to prison. Brazil's private sector is far larger than Russia's, but so are its income and education differentials.

In a BRICS context, Russia stands out as having particularly centralized authoritarian politics, a large monopolistic state sector without interest in development or profits, and an elaborate crony system, while it performs well in terms of economic level, education, and openness. ◆