TITLE: PRIVATIZATION IN RUSSIA: TRUE and FALSE

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Executive Summary

This analysis identifies a variety of particular aspects in which the program of privatization has developed weaknesses and/or unanticipated consequences and distortions; among these aspects are:

• by forbidding any new leasing of state property in preference for employee buyouts, the program halted one of the most dynamic and entrepreneurial features of the Russian economy in transition – the spinning off of new ‘small enterprises’ such as cooperatives and leaseholds.

• the worker buyouts characteristic of the program typically are manipulated by the current managers for their own benefit, resulting in their holding of a majority of shares (and control) of the new "Joint Stock Company." The managers have thereby been able to consolidate their property rights and shield themselves from outside discipline - precisely the opposite of what the market transition is supposed to accomplish.

• due to the structure, design and implementation of the Russian voucher program, the pace of voucher investment on JSC shares has been slow, and the prices paid for vouchers much lower than hoped for. The one exception has been voucher auctions involving firms which hold assets ripe for "stripping" (selling off of real estate, trucks, materials), driven by investors seeking speculative short-term gains rather than long term interest and control over the enterprise.

• based on the ruble/dollar exchange rate and the market price for vouchers at the time of this study (early autumn 1993) the implied dollar value of the entire Soviet industrial sector is estimated at an absurdly low $5-10 billion.

• although the privatization of the small retail sector has been relatively successful, its full potential has been hindered by much slower privatization of the cumbersome and inefficient wholesale and transport network on which it depends.

This paper reflects events through early Autumn 1993. The author provides an evaluation of his findings beginning on page 16. For convenience, a copy of this evaluation immediately follows this summary.

* Prepared by NCSEER staff.
Evaluation

The main criterion for judging the success of the program at present seems to be the simple numerical score - how many firms have been privatized, how many vouchers invested. Larger questions such as are new owners emerging, and are they having an impact on the operations of the plants, are dismissed as premature. At a press conference in August 1993, for example, Chubais declined to provide a single example of a privatized firm which he considers a success story. Critics also argue that the emphasis on the voucher program is keeping other capital sources (including foreigners) out of privatization. Another major problem with privatization is that firms are shedding social services and local soviets cannot afford to maintain them.

Leaving aside the privatization of small shops, in only a very few cases has privatization achieved its avowed goal of putting new owners in control of enterprises. The process is better described as 'commercialization' than 'privatization', since what it involves is the conversion of state-owned and centrally planned enterprises into profit-seeking, legally independent companies, owned and controlled by their former managers and workers.

This process is obscured by the bewildering variety of legal forms now in existence, from holding companies owned by their members to firms in which a majority of shares are formally held by the work force. The latter has been the predominant form of privatization thanks to the voucher method - contrary to the intentions of those who introduced the scheme.

What of the political goals of the privatization program? The proponents of the scheme are now claiming that privatization has successfully built a constituency of support for reform, and has been partly responsible for Eltsin's victory in the 25 April referendum. They also argue that privatization can claim at least
partial credit for the depoliticization of Russian industrial enterprises - while conceding that allocation of credits is still a highly politicized process.

However, one may question whether these political gains can really be attributed to the privatization program. The crucial tests of Eltsin's popularity - his electoral victory as President in May 1991, his defiance of the August 1991 coup - predate the launching of the privatization program. And the real depoliticization of Russian enterprises came long before the 1992 law on privatization. The erosion of central authority set in at least as early as 1983, when worker collectives were given the right to elect directors. The 1987 Law on the State Enterprise repealed this right, but went on to grant considerable autonomy to state firms, which they eagerly took advantage of amid the mounting economic chaos of 1990 and 1991. The break-up of the central USSR ministries in the fall of 1991 was the final blow, but long before then local managers with the tacit cooperation of their workforces had established de facto control over their factories. Thus one can argue that there has been a systematic pattern of managers seeking autonomy from outside control, and if they have merely utilized the privatization program to consolidate their autonomy. If this is true, then it has worrying implications for the impact of privatization, since managers will not be very amenable to seeing control flowing into the hands of new outside investors.

It is nevertheless true that the privatization program has enjoyed considerable public support - no small achievement in a land of massive public alienation from political institutions. However, a June 1993 poll showed that while 69% approved of the idea of small private firms, only 27% favored large private firms - and only 13% approved large private firms owned by foreigners.62

The economic transformation of Russia is proving to be a slow and painful process - more slow, and more painful, than anybody predicted. Nevertheless, it is moving forward - and steps
towards the legal definition of property rights, even if they are enjoyed by the managers and workers, should be a positive step towards a market economy.

On the other side, one could argue that focusing the government's scarce political and administrative resources on privatization has diverted attention away from other more pressing problems, such as the stabilization program, or the acute need to resurrect some sort of payments system with the neighbouring successor states. One can argue that the impact on GNP of the collapse of inter-state trade has been far more devastating than the putative efficiency gains expected from the privatization program.
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Introduction

Against a background of political chaos and continuing economic decline, privatization seems to be one of the few positive fruits of post-communist Russian economic policy. According to the Russian government’s Western advisors, the privatization now taking place is ‘the fastest in human history’, sweeping up 3-4% of state industry per month, and is ‘the most successful reform in Russia’.1 Is this really the case, or is the program a mere Potemkin village, disguising Russia’s continuing economic disintegration?

The shift to privatization

Laws allowing for the privatization of housing, shops and factories were introduced by the Russian Federation parliament in July 1991, but were not seriously implemented because of the confusion caused by the August coup and the collapse of the USSR.2 The new Gaidar government which came together in October 1991 concentrated its efforts on price liberalization (the shock therapy of January 1992), and structural reform took a back seat.

However, by mid-1992, strong opposition from the parliament and from industrial directors (with close ties to Eltsin’s ruling circle) meant that the government was unable to cut back on budget subsidies to industry, which amounted to more than 20% of GDP. The crucial failure for the stabilization package was the government’s inability to free energy prices in April 1992.3 Thus the stabilization program was a failure: inflation continued at more than 20% a month and the budget deficit yawned ever wider.

As the year progressed Gaidar switched attention to privatization as a way to regain the reform momentum. Anatolii Chubais, the energetic head of the new State Committee for Administration of State Property (GKI) argued that transferring assets into private hands through a Czech-style voucher giveaway
scheme would build a popular constituency for change and outflank the opposition to reform. Direct sales to new outside owners was not a feasible alternative: it would have taken too long, and would not have generated mass privatization. There were very few Russians with the required capital, and the selling of firms to foreigners would be highly unpopular.

In June 1992 Eltsin persuaded the parliament to pass an ambitious privatization program. Some Russian parliamentarians suggested that the quid pro quo for parliament’s passing of the law was an understanding that the Central Bank would remain under parliamentary control - which meant that its anti-reform head V. Gerashchenko would continue to pump credits into the economy.

The June law obliged all firms with more than 1,000 workers or R50 mn base capital to convert themselves into joint stock companies (JSCs) with openly traded shares. Certain categories of firm were excluded - energy and mineral resources, defense industry, and transport and communications. Projects were to be submitted for approval to one of GKI’s 80 regional offices, or to the national GKI in the case of firms with more than 10,000 workers. All other forms of spontaneous privatization, such as leasing, were forbidden. GKI laid down a strict timetable of the number of firms to be privatized in each region per month. All told, about 25,000 firms are to be involved. Once a firm becomes a JSC, the government’s shareholding is passed over to the newly-created National Property Fund (NPF), which will dispose of the shares over the next several years.

Under pressure from the parliament, Chubais’s program was modified to give some privileges to worker ownership. In firms sold by auction, the workers get 30% (20% in the case of tender) of the purchase price as a cash bonus. Workers in units leased to them before 1992 still have the right to exercise the buy-out option (often at a bargain price). However, any new leasing of state property was forbidden. This means, paradoxically, that the privatization program has halted one of the most dynamic and entrepreneurial features of the Russian economy in transition -
the spinning off of new 'small enterprises' such as cooperatives and leaseholds.

Each firm's workers get to vote on which of three variants to adopt:

1) the workers are given 25% of the shares (non-voting), and have the option to buy 10% of voting shares at 30% discount;
2) the workers can opt to buy 51% of voting shares (with no price discount); or
3) the workers can buy 20% of voting shares at the end of one year of profitable operation.

In buying shares and bidding in auctions, workers can use cash, vouchers and 'individual privatization accounts' made up of funds contributed from the firm's incentive fund and from up to half of the firm's 1992 profits. Future purchases of shares from the NPF can take place using ploughed-back profits of the firm, in an ESOP type arrangement. Worker ownership advocates pressed unsuccessfully for such measures to be formally added as a fourth variant in the original law. Workers' rights to buy shares are typically allocated on the basis of their length of employment and current wage (indicating that they are being regarded more as employees than as investors).

Thus as the program passed from conception to implementation it turned out to be much more favorable to worker ownership than its authors had intended. However, not all the details of the scheme favor the workers. For example, under the GKI regulations governing option 2, shares to be auctioned are distributed in proportion to the amount requested in sealed bids - a procedure which favors the managers, who confidently over-bid.

The firms' fixed assets are priced at a mere 70% of the January 1992 book value for the first variant, and 170% for the second. Given that capital assets were already under-valued in the Soviet economy, and that between January and December 1992 retail price inflation was 1,200%, in most cases the book values
are gross under-estimates of the current value of the assets. In other cases, of course, the current market value of the assets is zero. Working capital and stocks were valued at current prices, which led to the unrealistic situation where fixed assets often only account for 25% of total capital.

By July about 20% of industrial firms had been privatized, with the hope that 40% will be privatized by the end of 1993. As of 1 July 1993 a total of 6,477 JSCs had been created, of which 1,838 were formed out of the firms slated for mandatory privatization (out of a total of 2,918 in process), 518 as spin-offs from existing firms (out of 1,237) and 4,121 firms voluntarily converted themselves JSCs (out of 6,508). 77% of them have opted for the second variant i.e. the worker buyout, 21% for the first and only 2-3% for the third variant.

Typically, these worker buyouts are orchestrated by the current managers, who personally buy up many of the shares, and use their administrative authority to control the remainder. In all three variants most of the remaining shares are held either by the National Property Fund or by other state enterprises (often the clients or suppliers of the firm in question). There have been only a handful of cases in which firms have been privatized in auctions for cash as opposed to vouchers (and these all seem to involve real estate in central Moscow).

It is important to bear in mind that the legal structure governing privatization is more honored in the breach than in the observance. The government has granted countless exemptions to firms wishing to avoid strict adherence to the program. For example, one Eltsin decree gave four oblasts special rights in approving privatization projects for firms under federal jurisdiction (Nizhnyi Novgorod, St Petersburg, Sverdlovsk and Belgorod). Also, where disputes arise over privatization it is usually political manoeuvring that resolves the disagreement, and not recourse to courts of law. Although closed JSCs (where resale of shares without the company's permission is forbidden) were supposed to be illegal, they still appear to be widespread.
Initially, a majority of managers were hostile towards Chubais's program, and saw it as at worst a threat or at best an irrelevance. However, their opinion has slowly shifted in its favor - as they have learned how to manipulate the scheme to their own advantage. Many managers see privatization as a way of consolidating their property rights and shielding themselves from outside discipline - precisely the opposite of what the market transition is supposed to entail.

The launching of the privatization program was a considerable political achievement for Chubais. He was able to turn GKI into a powerful new administrative agency, seizing effective control of industrial decision-making from the hands of the already fatally-weakened central ministries. He also gained a large degree of control over the new bankruptcy procedure, introduced in December 1992. Chubais wanted to use bankruptcy as a threat to wield against industrialists resisting voucher privatization, but the bankruptcy measure which finally emerged was so laden with delays, protection for workers and provisions for rehabilitation (sanatsiya) that it remains a dead letter.

Although GKI faced little opposition from the central ministries, there has been considerable controversy at local level. Many regional GKIs have crossed swords with local soviets and with regional branches of the National Property Fund. Disputes often break out over whether to break up existing firms so as to privatize the most profitable parts separately ('cherry picking'). Some of the ethnic regions, such as Tatarstan, have refused to cooperate with the program, and are trying to implement their own schemes. These tensions are being reignited in the run-up to the December elections, with for example Moscow Mayor Y. Luzhkov denouncing the GKI program as 'mass swindling and squandering of the nation's wealth.' GKI organs also fought off a bureaucratic challenge by the regional branches of the State Anti-Monopoy Committee, which was subordinate to the Supreme Soviet.
GKI has received considerable technical assistance from Western agencies, mostly from the US AID. GKI also received a $10 mn grant from the EBRD, and was awarded a $90 mn loan from the World Bank in March 1993 (not yet disbursed).\textsuperscript{18} Chubais is on record calling for no less than $4 bn in aid to fund GKI, and to go into regional investment funds run by private companies (not subject to governmental controls, as is the case with World Bank loans).\textsuperscript{19,20} In a land of diminishing government resources, the tens of millions of dollars poured into privatization have created a little state within the state, with salaries for top officials many dozen times higher than their counterparts in other state agencies. On one hand, this means that the program is actually being implemented, on the other hand, it creates resentment and isolates the program from other government agencies.

The voucher program

The team of Western economic advisers who had helped put together the Polish reform program had been opposed to the Czechoslovak voucher method. They saw it as a political gesture which would disperse share ownership and do little to achieve effective new owners. Thus for Poland they devised a complicated scheme in which citizens would be issued vouchers for shares in mutual funds (some with foreign managers), which would in turn invest in state firms. The Polish scheme was so complex, and so politically unattractive, that it never got off the ground.

After this sobering experience, the criteria for a successful privatization program mellowed considerably. It was no longer a question of whether the program would lead to improved 'corporate governance': it was more a case of whether the program would be implemented in any shape or form at all. For Russia, the Western advisers were arguing that the voucher method was superior to the mutual fund approach in that it offered efficiency, equity, speed and flexibility, but the real issue was
simply political and administrative feasibility.\textsuperscript{21}

The Russian government began issuing vouchers to the general public in November 1992, with a face value of R10,000 ($20 in 1992 prices). After a slow start, and a rather anemic GKI publicity campaign, interest in vouchers picked up, and more than 90\% of the population collected their vouchers. Some sociologists suggest that most people saw the distribution of vouchers not as a chance to become a part-owner of a capitalist enterprise, but as part of the long-standing patrimonial tradition of the distribution of special permits which enable one to acquire something without queuing (and without paying).\textsuperscript{22}

There were some small but important technical differences from the Czech model. In Russian voucher auctions investors can name a reserve price, the theory being that this gives some advantage to more sophisticated investors, and allows them to shape final price. This seems to have aided inside managers in capturing large blocks of shares. And, unlike in Czechoslovakia, there was no nationwide computer bidding system in place. Some firms sell their voucher-shares through advertisements in national newspapers, but most shares have been sold in locally-organized voucher auctions. GKI, in collaboration with Price Waterhouse, is attempting to set up a national trading system for the shares of 400-500 leading firms. A small number of inter-regional share auctions have also been held.

The first auction of shares for vouchers took place in a blaze of international publicity at the Bolshevik biscuit factory in Moscow in December 1992. In January there were 105 auctions, in 15 regions, rising to 188 (in 27 regions) in February and 632 in June. A total of 2,418 auctions had taken place by the end of June, involving plants with 3.17 mn employees (18\% of the industrial labor force) and R25 bn in base capital.\textsuperscript{23} Some 14 million vouchers (10\% of the total) have been exchanged for shares. The plan is to hold 5,600 auctions in 1993.

There was little incentive for firms to sell shares for vouchers. The average proportion of shares actually sold for
vouchers was a mere 21% (rising from 11% in January to 23% in June). Elstsin issued a decree on 8 May 1993 insisting that at least 29% of shares must be sold for vouchers. But judging by the lists published in the Russian press, most firms are choosing to auction exactly 29% of their share capital for vouchers. This is true even in cases touted as success stories, such as the Vladimir Tractor Factory (whose share ownership is 48% workers, 29% NPF and 22% outside investors). At Uralmash 44% of shares went for vouchers, with the largest outside investor controlling 18%, while the auto giant Zil plans to sell 35% for vouchers. At the original Bolshevik Biscuit only 25% of shares were sold for vouchers. Even in Nizhni Novgorod, the region where the economic reforms have been most radically pursued, not a single one of the 128 firms to be auctioned in July 1993 proposed to release more than 29% of the shares for vouchers. In order to try to raise the resale price of vouchers, GKI has been pressing firms to increase the proportion of the vouchers used to buy shares for workers under the second variant (instead of using cash or ploughed-back profits).

The government encouraged the formation of investment funds to play the role of intermediary and encourage the concentration of shareholdings. Citizens can invest their vouchers in these funds, or the funds can buy vouchers for cash. However, influential investment funds have been slow to emerge. There are now 550 funds in operation, with about 15% of the vouchers in circulation. Many funds were set up by industrial enterprises, with a view to pooling the vouchers of their employees. A major problem is that 80% of commercial banks are excluded from creating such funds by the rule which bars any organization with more than 25% state ownership. This is in contrast to Czechoslovakia, where banks have played a key role in the privatization program by concentrating ownership through investment funds controlled by them. Another barrier is a Eltsin decree of 21 May 1993 which confined the funds to investing in shares, preventing them from engaging in other transactions (such
as real estate) which they were using to generate cash income, enabling them to buy up vouchers. The funds are also hampered by a lack of clear legislation defining their rights (eg they cannot issue long-term securities).  

These restrictions mean that most of the funds buying up vouchers are seeking a quick profit through speculative resale (eg to plant managers), with a heavy emphasis on asset stripping (selling off equipment such as trucks, stocks of materials and land). There have also been some scandals involving funds such as the Revansch group, whose directors bought up 20% of all the vouchers issued in St. Petersburg before absconding. On 5 April Chelyabinsk council suspended the region's voucher auctions, since according to council chairman P. Sumin 'People were bringing vouchers in suitcases to buy the property of Cheliabinsk province. Our people were being deprived of their rights.' As of May the largest fund (Pervyi investitsionnyi) controlled less than 2% of the total number of vouchers. Again, this contrasts with Czechoslovakia, where the funds took 72% of all vouchers, with 40% in the hands of the five biggest funds.

The cash value of the voucher fell to R4,000 ($4) by March 1993, but has since recovered to R10,000 ($10). The relatively low price of the vouchers can be explained partly by the slow pace at which firm assets have been put up for voucher auction (slow relative to the pool of vouchers in circulation), and by the fact that outside shareholders will clearly find it very difficult to have any influence over the insiders who control the majority of shares in these firms.

The only auctions generating really high prices are those with scope for asset stripping - such as firms with valuable real estate in downtown Moscow. In the majority of cases the only people interested in acquiring shares for the long haul are the current management and/or workers. There have been only a handful of cases of foreign firms being involved. For example, a Swedish firm bought 43% of the Baltika drinks manufacturer in Petersburg,
and Philip Morris bought 49% of the Krasnodar Tobacco Factory for $60 mn.37 The shares of Baltika, whose nominal price at the auction was R70, were later being sold at R7000.38 There are an equal number of cases where deals are delayed or collapse at the eleventh hour (eg Ligget Myers in Moscow, Otis Elevators in St. Petersburg).39

On the basis of the current ruble/dollar exchange rate and the current market price for vouchers, Boycko, Shleiffer and Vishny estimate the implied dollar value of the entire Soviet industrial sector to be a mere $5-10 billion, with capital assets per worker valued at a paltry $100 (compared to $100,000 in the USA).40 It is clearly absurd to suggest that capital productivity in Russia is 1,000 times less than in the USA, if only when one considers that capital flight from Russia last year amounted to $15-20 billion. The most valuable Russian factory according to these calculations is the Zil auto works, which comes in at $15 mn, while Uralmash is $4mn, the Bratsk aluminum works is $3.6 mn and the Volgograd Tractor Works $570,000!

Privatization and the oil industry

The fiercest political controversy has been that surrounding the ownership of the oil and gas industry - which generates about 70% of Russia's export earnings.41 In December 1991 Eltsin blocked moves to privatize the oil industry into the hands of the new corporations which arose out of the former Soviet ministries - and their allies in municipal councils. Since then the government has been locked in a political stand-off with regional interests in West Siberia who want more direct access to the proceeds from oil and gas exports.

The reformers lost a crucial battle at the end of May 1992, when Eltsin fired the Minister of Fuel Energy, Vladimir Lopukhin ('the only Gaidar man heading a sectoral ministry'). Lopukhin proposed to include oil and gas in the privatization program by
creating independent holding companies, and was accused of pursuing policies favoring the private firm Menatep (whose head, Khodorkovski, was deputy minister). Lopukhin was replaced by Viktor Chernomyrdin, the former head of Gazprom and Rosneftegaz (the corporations which inherited the operations of the former union ministries). In August 1992 Eltsin issued a decree formally exempting the oil and gas sector from the privatization program. The creation of holding companies has proceeded, but the controlling packet of shares remains in the hands of the ministry. 42 Chernomyrdin went on in December 1992 to replace Gaidar as prime minister.

1993 saw little progress in the privatization of the oil sector, although in September 1993 the industry agreed in principle to issue 20% of its share capital for vouchers. Foreign investors are keen to get involved, but want to see a clarification of ownership rights and export regulations before getting further involved. Thus far only a few pilot projects are under way with foreign participation, such as the $300 mn Polar Lights project in Arkhangelsk. 43

A similar pattern occurs in several other sensitive sectors, such as gold mining. As of June, in the gold province of Magadan there had not been a single privatization, and mining activity was concentrated in the hands of a 43-firm holding company. 44

The impact on the behavior of privatizing enterprises

The managers of state-owned enterprises are showing considerable resilience and not a little entrepreneurial spirit. New evidence from Poland suggests that hard budget constraints can induce state firm managers to become profit seekers even without formal privatization. 45 The counter-argument would be that their enthusiasm for profits can partly be attributed to their expectation that privatization is imminent, and a desire to build up a good track record for their future owners. Similarly, evidence from China suggests that private firms do best in those
cities where state firms are also enjoying output growth.\textsuperscript{46} Studies of new business start-ups in Russia similarly suggest that most new entrepreneurs tend to originate within state firms and/or continue to rely heavily on trading with them as supplier and customer.\textsuperscript{47}

There is some evidence that Russian state firms are also starting to respond to price signals - such as a positive correlation between change in output and change in relative sectoral prices.\textsuperscript{48} Most Russian managers are motivated by the survival instinct: a desire 'to preserve the work collective'.\textsuperscript{49} The managers' priorities are jobs, wages and housing, in that order. Given the changing economic environment, most of them recognize that to survive they will have to respond to market signals. At the same time, managers find few concrete market opportunities coming their way. According to one survey, about one third of state firms have been able to seek out new suppliers and customers.\textsuperscript{50} Among the factors inclining a firm to become more market oriented were the following:

- form of ownership (but it is too early to say whether privatization will make a difference);
- degree of monopoly power (the more monopoly, the less market-like behavior);
- place in technology chain (closer to consumer, or to exports means more market orientation);
- dependence on imports (this stimulated market behavior in the form of a desperate search for replacements);
- variety of output (more variety, more market behavior);
- burden of social spending (strongly inhibits market behavior, because of the financial strain).

The key criteria for predicting the economic success of state firms in the transition period would seem to be access to dollar credits; access to ruble credits and access to foreign markets. Privatization has provided another set of opportunities
for firms to seek ways to survive - by allying themselves with more profitable firms, or conversely by cutting themselves off from lossmakers. There seem to be almost as many ways to respond to the challenge of privatization as there are firms entering the program, and contingent factors far outweigh the formal process of ownership transfer.51

Progress in small privatization

The most successful field for privatization has been the small-scale retail sector, the administration of which was entirely delegated to municipal authorities under a December 1991 decree. (The federal government merely takes 20% of the proceeds.) The small privatization program covers firms with fewer than 200 workers and less than R1 mn book value as of 1 January 1992.

By August 1993 some 70,000 shops, cafes and service outlets had been privatized by auction or direct sale, raising R450 bn.52 This represents perhaps 30% of the total number of outlets and 60% of all shops. Moscow and St. Petersburg became the leaders in the small privatization drive.53

Distribution of objects by the type of buyer, %:

<table>
<thead>
<tr>
<th>Type of Sale</th>
<th>Worker</th>
<th>Legal person</th>
<th>Physical person</th>
</tr>
</thead>
<tbody>
<tr>
<td>trade</td>
<td>69.6</td>
<td>22.7</td>
<td>7.7</td>
</tr>
<tr>
<td>catering</td>
<td>70.1</td>
<td>21.8</td>
<td>8.0</td>
</tr>
<tr>
<td>services</td>
<td>82.2</td>
<td>22.3</td>
<td>12.3</td>
</tr>
</tbody>
</table>

Distribution of objects by types of sale, %:

<table>
<thead>
<tr>
<th>Type of Sale</th>
<th>Tender</th>
<th>Auction</th>
<th>Lease</th>
<th>Transformation into JSC</th>
</tr>
</thead>
<tbody>
<tr>
<td>trade</td>
<td>35.0</td>
<td>13.6</td>
<td>39.5</td>
<td>10.9</td>
</tr>
<tr>
<td>catering</td>
<td>25.9</td>
<td>15.8</td>
<td>40.4</td>
<td>17.9</td>
</tr>
<tr>
<td>services</td>
<td>45.9</td>
<td>9.1</td>
<td>34.0</td>
<td>11.0</td>
</tr>
</tbody>
</table>
As these tables show, two thirds of the shops, cafes and service outlets have been purchased by their current workers, mostly through leasing or closed tenders rather than open auctions.54

Prices are often very low, although on the negative side in many cases the new leaseholders are obliged to continue maintaining the 'profile' of the store (eg a bakery must continue selling bread). Many commentators complain that standards of service have not significantly improved after privatization.55 Unfortunately, the cumbersome and inefficient wholesale and transport network is being privatized at a much slower rate.

There has also been steady progress with the privatization of housing. 6 million apartments have been privatized (17% of the total) - mostly by being given free of charge to the sitting tenants.56 However, maintenance and utilities remain the responsibility of municipal authorities - and the fees charged go nowhere near to covering the costs.

The main impetus for the expansion of the small privatization program came from model projects set up by the International Finance Corporation (an arm of the World Bank, paid for by USAID) in Nizhnii Novgorod and Volgograd, beginning in March 1992.57 In Novgorod, the IFC persuaded the local GKI to sell the firms free of debts, while in Volgograd the firms were sold as a 'going concern' (ie with the old debt obligations).58

As for small business start ups, by March 1993 there were 950,000 new entrepreneurs registered - 200,000 private, 400,000 partnerships (tovarishestva), 150,000 cooperatives, and 12,000 'concerns' and other legal forms.59 They employed a total 16 mn people (22% of the workforce), of which 4 mn were in the private sector per se. In the manufacturing and construction sector, most of these new entities had spun off from state firms. They typically take their skilled personnel and equipment from the state firm, which also rents space to them, sells them supplies and buys their output.
Evaluation

The main criterion for judging the success of the program at present seems to be the simple numerical score - how many firms have been privatized, how many vouchers invested. Larger questions such as are new owners emerging, and are they having an impact on the operations of the plants, are dismissed as premature. At a press conference in August 1993, for example, Chubais declined to provide a single example of a privatized firm which he considers a success story. Critics also argue that the emphasis on the voucher program is keeping other capital sources (including foreigners) out of privatization. Another major problem with privatization is that firms are shedding social services and local soviets cannot afford to maintain them.

Leaving aside the privatization of small shops, in only a very few cases has privatization achieved its avowed goal of putting new owners in control of enterprises. The process is better described as 'commercialization' than 'privatization', since what it involves is the conversion of state-owned and centrally planned enterprises into profit-seeking, legally independent companies, owned and controlled by their former managers and workers.

This process is obscured by the bewildering variety of legal forms now in existence, from holding companies owned by their members to firms in which a majority of shares are formally held by the work force. The latter has been the predominant form of privatization thanks to the voucher method - contrary to the intentions of those who introduced the scheme.

What of the political goals of the privatization program? The proponents of the scheme are now claiming that privatization has successfully built a constituency of support for reform, and has been partly responsible for Eltsin's victory in the 25 April referendum. They also argue that privatization can claim at least
partial credit for the depoliticization of Russian industrial enterprises - while conceding that allocation of credits is still a highly politicized process.

However, one may question whether these political gains can really be attributed to the privatization program. The crucial tests of Eltsin's popularity - his electoral victory as President in May 1991, his defiance of the August 1991 coup - predate the launching of the privatization program. And the real depoliticization of Russian enterprises came long before the 1992 law on privatization. The erosion of central authority set in at least as early as 1983, when worker collectives were given the right to elect directors. The 1987 Law on the State Enterprise repealed this right, but went on to grant considerable autonomy to state firms, which they eagerly took advantage of amid the mounting economic chaos of 1990 and 1991. The break-up of the central USSR ministries in the fall of 1991 was the final blow, but long before then local managers with the tacit cooperation of their workforces had established de facto control over their factories. Thus one can argue that there has been a systematic pattern of managers seeking autonomy from outside control, and if they have merely utilized the privatization program to consolidate their autonomy. If this is true, then it has worrying implications for the impact of privatization, since managers will not be very amenable to seeing control flowing into the hands of new outside investors.

It is nevertheless true that the privatization program has enjoyed considerable public support - no small achievement in a land of massive public alienation from political institutions. However, a June 1993 poll showed that while 69% approved of the idea of small private firms, only 27% favored large private firms - and only 13% approved large private firms owned by foreigners. 

The economic transformation of Russia is proving to be a slow and painful process - more slow, and more painful, than anybody predicted. Nevertheless, it is moving forward - and steps
towards the legal definition of property rights, even if they are enjoyed by the managers and workers, should be a positive step towards a market economy.

On the other side, one could argue that focusing the government’s scarce political and administrative resources on privatization has diverted attention away from other more pressing problems, such as the stabilization program, or the acute need to resurrect some sort of payments system with the neighbouring successor states. One can argue that the impact on GNP of the collapse of inter-state trade has been far more devastating than the putative efficiency gains expected from the privatization program.
NOTES


2. For a review of all the ownership laws, see Fonda reforma, ‘Annotatsiya osnovnykh zakonodatel’stva i normativnykh aktov po privatizatsii v RF.’, Delovoi mir, 9 July 1992, p. 6.

3. A. Aslund, Systemic Change and Stabilization in Russia, Royal Institute of International Affairs, 1993.


10. According to two surveys of 55 firms cited in Boycko et al, op. cit., p. 29, managers controlled 17% of total shares, compared to workers 53%, NPF 16% and outsiders 14%.


15. For the example of Aeroflot, see O. Bolmatova, 'Plan aktsionirovaniya Aeroflota vyzyvaet spory', Finansovye izvestiya, 30 April 1993, p. 2.


20. Several Western observers have supported the idea of channelling the bulk of Western aid into the privatization program - R. Frydman and A. Rapaczynski, Structure of Assistance for Russia, manuscript, 1993.

21. The initial criteria are listed in a December 1992 paper prepared for GKI by M. Boycko, A. Shleifer and R. Vishny Voucher Privatization. The more streamlined criterion of political feasibility is the focus of their October 1993 paper, op. cit.


34. Ostankino television, 6 April 1993.


43. See the article by the head of Conoco, C. Nicandros, ‘Russian oil, Western Investment’, The World Today October 1993, pp. 186-89.


51. See for example the four fascinating case studies in P. Biziukov, V. Borisov, S. Clarke and P. Fairbrother, The Privatization of Industrial Enterprises in Russia: Four Case Studies, manuscript, July 1993. See also S. Clarke, ‘Privatization and the development of capitalism in Russia’, New Left Review, 196, November 1992, pp. 3-27.


60. For example, in his speech to the Seventh Congress Prime Minister Egor Gaidar noted that small privatization was falling behind the plan ‘but in volume it will be fulfilled for 1992’ ie. 40,000 units. Ostankino television, 2 December 1993.
