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Abstract

The spatial aspect of political-economic transformation in the former Soviet Union - including the relations between new independent states and the center-region relations within national borders – has a heavy impact on the quality of institutions comprising the economic order. The paper discusses how the interaction between the development of large business groups and changes in the spatial organization of power within the framework of the Russian federalism and the post-Soviet integration influenced the changes of economic institutions. In the 1990s the interests of big business contributed to the fragmentation of both internal market in Russia and international markets in the CIS and therefore to the general disorganization problem. Since 1998 development of interregional corporations supported the re-integration of the Russian market. Since 2000 the investment expansion of Russian business plays an important role for the integration "from bellow" in the post-Soviet space. Yet even in this case the impact on the quality of institutions is ambiguous: integration of markets influences the power relations between different levels of government in Russia and between different governments in the CIS. Moreover, it intensifies the processes of institutional competition, which have an ambiguous effect on the development of institutions because of the "demand for bad institutions" problem.

Keywords:

Russian Federation, CIS, transformation, spatial organization of power, bad institutions

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Big Business and Quality of Institutions in the Post-Soviet Space: Spatial Aspects

1. Introduction

The main challenge of the economic transformation in the post-Soviet space[1] -for both theoretical and practical issues – is the complexity of relations between different aspects of what is called "triple transition" (Offe, 1991): transformation of economic order, of political order and development of new independent states. In fact, the latter aspect could be even placed in a broader context. The problem is not only the development of new institutions on the state level; it also comprises the changes in the international political and economic relations (in fact, the very existence of this level is a result of the transformation process and the collapse of the Soviet Union) and the relations between national and subnational authorities (in particular, within the framework of federalism, like in Russia; however, the issue seems to be relevant for other countries like Ukraine as well): in what follows I am going to refer to this complex network of relations as "spatial order of authority". So, it is likely that in order to understand the driving forces behind the development of the economic order it is necessary to study how to changes in political and spatial order influence the quality of economic institutions.

From the point of view of the spatial organization of authority two aspects should be considered. First, the allocation of power between different levels of governance and the structure of international relations are important factors influencing the governmental reform policies through both changes of constraints and of economic incentives (Oleinik, 2006). Second, the existence of barriers between jurisdictions can both limit the interregional and international exchange and therefore have an impact on economic development or facilitate the trade and investment relations. In the last case it does not only influence the economic performance directly; it is also a

[1] This paper defines the post-Soviet space as twelve former Soviet republics, which are currently members of the Commonwealth of Independent States (CIS).

factor of strengthening the institutional competition between jurisdictions, which also has an impact on the behavior of the governments. However, the development of the spatial order of authority also depends on multiple non-governmental actors, in particular private business, which partly appears as a result of economic reforms.

This paper aims to study the interrelations between the spatial order of authority in the post-Soviet space and the development of big business. It focuses on two particular cases: the development of the Russian Federalism and the international economic integration within the frameworks of the CIS and two related projects: Eurasian Economic Community and Common Economic Space. In fact, although this is rarely recognized, these two processes (the development of the Russian federalism as a process of permanent re-designing the power relations between regions (for the theoretical framework of process-oriented analysis of federalism see Feld, 2007) and the post-Soviet integration) seem to be an interesting case of comparison. First, both systems of institutions developed in a similar economic framework and faced similar problems. Second, they appeared simultaneously as two different attempts to cope with the dissolution of the Soviet Union. In fact, in the early 1990s both independence of new states and stability of Russian Federation with its secessionist republics were questionable: put it differently, it was not obvious, that Belarus will remain a separate state while Tatarstan will be part of the Russian Federation. Third, at least in Russia until recently (probably 2004-2005) the policy towards the CIS countries and the regions of the Russian Federation was developed according to the common framework; the situation seems to have changed only after the "orange revolution in Ukraine".

Both Russian federalism and the post-Soviet space experienced similar development in the early 1990s: the weakening of the central authority in Russia led to the fragmentation and disintegration of internal market, and failure of the integration project resulted in increasing barriers for trade and investments in the CIS. At the latter stage the situation from the point of view of the interaction of local markets changed: Russian market evolved towards higher integration, and in the CIS investments of Russian enterprises and business networks supported the active process of "regionalization from bellow". However, the results of development of the spatial orders of authority in these two systems are completely different: while

Russia, after a period of decentralization evolved to a highly centralized federation, the CIS and further regions, in spite of several re-integration attempts and active Russian policy, developed to vague and weak unions without any impact. So, this difference is also an interesting puzzle, which is worth studying.

The paper is organized as follows. The next section discusses the fragmentation of the markets in the post-Soviet space and in Russia and the impact of private businesses on this process. The third section deals with the integration of markets through activities of large corporations. The fourth section deals with the indirect impact of market integration on the governmental policy and also discusses the potential differences between the development paths of two institutional systems. The fifth section focuses on institutional competition as result of market integration and on its ambiguous effects. The last section concludes.

2. Disintegration of markets and the big business

The first half of the 1990s was marked by the strong process of disorganization (Blanchard and Cremer, 1997) in the post-Soviet countries: the dissolution of economic ties existing in the Soviet Union alongside with absence of market institutions in the society supported the fragmentation of economic activity and contributed to the recession. Although the organization of “old” ties resulted not from evolutionary process of market competition, but from centralized planning in an autarky and therefore was obviously inefficient, the emergence of new network of business relations required time and effort; the “institutional interregnum” therefore became a period of economic decline. A crucial element of disintegration was the deficit of law (multiple loopholes in the existing legislation and poor enforcement of property rights and contracts) and the deficit of trust (preventing the development of informal institutions as alternatives to the absent formal legal framework). Finally, the demonetization and economy of arrears also supported the fragmentation of economic activity.

A significant part of the overall fragmentation process was the geographical fragmentation of the internal market of the Russian Federation. There is a large literature on integration of the Russian market based mostly on analysis of the “law of single price”, which should hold in an integrated market.[2] The empirical results show that in 1994-2000 only 36% of Russian regions were integrated with the national market, and 44% moved towards integration. Until 1994 the disintegration trend dominated; although it was replaced by a certain integration trend later on, the degree of integration still remained extremely low. The disintegration was strongly influenced by the geographical distance, the dominance of organized crime in individual regions and economic development before the reforms. The internal policies of regional governors were important: the so-called “red bellow” region with Communist governors was significantly less integrated in the Russian market than the rest of the country. Surprisingly, the international and internal integration of Russian regions were negatively correlated.

An important factor for the geographical fragmentation was the “provincial protectionism” practiced by the majority of Russian regions. On the one hand, Russian Federation after 1994 had formally a highly centralized structure with relatively limited authorities allocated to regions according to the constitutions. However, regional governments were actively involved in both bilateral bargaining with the federal center resulting in the system of power sharing treaties and in unilateral devolution activity. Many influential regions were quite successful in developing their own “loyal” business groups under control of local governors. From this point of view, interests of these business groups often contributed to the development of regional protectionism. First, regional governments practiced direct controls for the interregional trade and factor movement to maintain local monopolies (Kolomak, 2005). Second, the “regional protectionism” also included the “protection” of local “loyal” business groups from federal legislation. For example, regional enterprises were able to accumulate significant tax arrears and to avoid federal taxation due to support of the regional governors (Cai and Treisman, 2004; Ponomareva and Zhuravskaya, 2004; Plekhanov, 2006). In fact, regions were able to capture local tax authorities and seem to be much more active in collecting regional taxes than the federal ones (Libman and Feld, 2007). In several cases regions also

[2] The evolution of internal market (dis)integration in Russia is well documented in Gluschenko (2002; 2002a; 2004; 2004a; 2004b; 2004c; 2006; 2007); Berkowitz and DeLong (1999; 2001; 2005); Gluschenko and Koneva (2004); Gluschenko and Kulighina (2006); Gluschenko and Klimich (2007) and Kopsidis (2000).

protected their enterprises from hostile takeovers and bankruptcies (which have an important disciplining function in a market economy).

Besides the fragmentation of the markets, there were further negative implications of the regional protectionism for the institutional development. Because of the limited formal authorities of the regional governments, in many cases the protection took form of the involvement of regional business of semi-legal activity running against federal legislation, but informally “supported” by the regions. Therefore the regional protectionism often increased the share of shadow economy activities in the Russian Federation, supporting the development and the broadening of respective practices in the business community.

What was the impact of the federal big business on the fragmentation of economic space? In Russia the first wave of development of large business groups on the federal level started in 1994-1995 through the process of privatization. Private banks were able to establish significant industrial holdings with Russian-wide presence. However, this “first wave” or “regional expansion” did not really support the market integration. First, most business groups developed as relatively vague conglomerates without internal ties between businesses; a clear strategy of development was absent. Hence, the interest towards reducing the barriers for the interregional trade was limited. Moreover, the bargaining power of business groups was still relatively weak, and their ability to use federal center as an instrument of protection against local governors was also limited because of extreme weakness of the federation. In fact, several business groups, although formally with an interregional presence, focused on establishment and support of regional monopolies, e.g. in petroleum sphere (Eskindarov, 1999). The crisis of 1998 ruined the majority of banking groups and was used by regional authorities to initiate a wave of bankruptcies of assets controlled by large business groups and to re-integrate them into regional holdings. Therefore the federal business groups were not successful (and, actually, not willing) to support the re-integration of the economic space (Zubarevich, 2005). The state-owned business groups, although present in all regions, were weakly governed and hardly controlled by the federal government, therefore also unable to prevent the fragmentation of markets.

The fragmentation of the trade and economic relations within the FSU seems to be an obvious outcome of the dissolution of the Soviet Union. The empirical evidence shows that the development of new borders indeed had a significant impact on the trade patterns (Djankov and Freud, 2002) and that the problems for cross-border trade within the CIS contributed to the economic decline (Bevan et al., 2001; Linn, 2004). The integration attempts within the framework of the CIS and later of individual regional integration groups turned to the "ink on paper" integration quite fast. The majority of legal acts of the integration groups were not implemented. Countries ignored regional trade agreements and introduced unilateral protectionist measures (actually, it is true also for Russia, in spite of its attempts to support the regional integration). Even the most "loyal" partner of Russia, Belarus, introduced significant barriers for Russian goods (e.g. restrictions on share of foreign production in retail trade). The formal attempts to support the integration "on the enterprise level" like the establishment of "transnational financial-industrial groups" – communities of enterprises organized through the top-down approach – were also unsuccessful.

The reasons for the failure of the formal post-Soviet integration include a variety of factors (Libman, 2007). However, a significant element influencing the problems of regional integration in the 1990s was the position of Russian business. The trade between post-Soviet countries was mostly organized through two main channels: the informal semi-legal and illegal trade, mostly carried out through small and medium-size businesses and vast intermediation networks, and trade of large business groups, usually maintaining a quasimonopoly position due to the technological specifics of their counterparts. The intermediaries obviously have a vested interest in the existence of trade barriers, since they gain exactly from being able to find loopholes in protectionist borders; but also the large technological quasimonopolists seem to have benefited from the specific structure of trade between post-Soviet countries (Yevstigneev, 1997). Finally, most post-Soviet countries in the 1990s experienced the development of powerful business groups based on privileged relations to national governments (with only view exceptions where no large-scale privatization and liberalization was implemented). Even a delay in economic reforms was effectively used by business groups to gain from "informal" privatization with its intransparent channels and high corruption (Ukraine is the a good example of this process). Obviously, the attempts to gain control for assets and markets required the protection from abroad, and therefore made the full-scale economic integration impossible.

To conclude, fragmentation of both Russian internal market and economic relations between the CIS countries resulted to an important extend from the protectionist measures of governments, which were influenced by the interests of emerging regional business groups. Therefore business interests contributed to degradation of economic institutions in the post-Soviet space.

3. Integration of markets and the big business

The statistical evidence presented above suggests, that the fragmentation of the Russian market went down towards the end of the 1990s. After a period of disorganization the spatial integration of local markets became more important. At the same time, position of large business groups changed dramatically after 1998. Since the cheap income opportunities through acquiring federal bonds disappeared, business groups had to seek new opportunities of growth and expansion, which were connected with regional presence. Economic growth increased relative power of business groups vis-à-vis regional governments. The internal logic of development of business groups changed: many of them moved from conglomerates to vertically integrated production networks (Galukhina and Pappe, 2006), therefore receiving a vested interest in the reintegration of markets. Moreover, private business was able to gain support of the federal government, which became increasingly important after 2000. The public corporations in the field of infrastructure already present in most Russian regions became more active and therefore also influenced significantly the regional policy. These changes also influenced both bargaining position of business groups vis-à-vis local governments and their desire to support economic integration of the Russian regions. In the early 2000s many regional administrations in Russia were directly or indirectly controlled by the interregional business groups (Orttung, 2004). In fact, after 2000 businesses tried to “compensate” the loss of power on the federal level by increasing their impact on the regional level. It is possible to argue, that large business became a driving force of re-integration of Russian internal market.

The impact of business was important in two aspects. First, the business activity of regional groups was important for the development of interregional trade networks and therefore to the increasing interdependence of markets. The supply chains between different regions were created or re-established. Second, however, the impact of businesses on regional governments was important. New interregional business structures supported the lowering of protectionist borders between Russian regions. The empirical evidence (Guriev et al., 2007) suggests that regions where interregional corporations were the main lobbyists exhibited a lower degree of protectionism. The reasons are straightforward: integrated production of business groups was often located in different regions, and therefore regional protectionism on the markets increased the costs. Moreover, regions with strong business influence became less prone to enter the conflicts with the federal center (Speckhardt, 2004). On the one hand, business groups were interested in relative stability of their position, which could be challenged in case of conflict of elites: the property rights in Russia still remain a function of political support rather than of the law. On the other hand, business often used federal center as instrument to oppose local elites and the associated business groups. The result was a significantly lower degree of regional protectionism and of conflicts between regions and the federal center as a consequence of expansion of large business.

The regional expansion of Russian business and the exhaustion of available assets in Russian regions also supported a new trend in the development of the post-Soviet space – the international expansion of Russian corporations. In particular, Russian business was especially active in the post-Soviet space. Although the top-down integration initiatives remained as inefficient as in the 1990s, the post-Soviet space therefore experienced an active process of bottom-up integration, or regionalization. This combination has already been observed in other regions of the world. For example, in South East Asia the regional integration was driven by the investments of Japanese corporations and transnational Chinese business networks. Similar forces were at work in the post-Soviet space: since they are by far less known than the problem of integration of internal Russian market, some empirical facts should be probably presented.

On the one hand, the permanent migration from the post-Soviet states to Russia caused by conflicts and wars (typical for the 1990s) was replaced by the regular work migration. The business networks organized by migrants resemble similar processes in East Asia. On the other hand, the investment activity skyrocketed. While in 2000 the overall Russian investments in the CIS (according to the date of the Russian official statistical authority) accounted for about US$ 130 mln., in 2006 it made out US$ 4,128 mln. One should be aware of the fact, that in 2006 the structure of Russian investments in the CIS changed significantly as compared to the previous years due to large investment inflow in Ukraine. In 2006 this country was also the main recipient of Russian investments worldwide. CIS accounts for about 26.6% of the total Russian foreign investment stock. There are, however, good reasons to believe, that even these optimistic figures systematically underestimate the Russian investment activity in the CIS. The origin of investments can often be hardly identified correctly; moreover, the statistical authorities often not properly record investment flows because of use of offshore companies and intermediaries, shadow schemes (which did not play an important role for Russia's investment activity in industrialized countries) and differences in statistical procedures of different countries. According to a study by Crane, Peterson and Oliker (2005), foreign investments from the offshore jurisdictions, which could be "suspect" of having Russian origin, exceeded formally registered Russian investments in Ukraine by more than 200%. In 2000-2004 Kazakhstan's estimate of Russian investments in this republic exceeded the Russian data by more than three times. Hence, alternative estimates of investment activity could be helpful. According to the UNCTAD databank on M&A and MMBA International Business Association, mergers and acquisitions in the CIS made out about one half of the total number of the M&A deals of Russian businesses in 2000s.

The main industries where Russian FDI is concentrated are telecom and oil and gas sector. The latter seems to be an evident goal of Russian businesses, since oil and gas corporations play the dominant role in Russia's economic structure and, hence, have potential needed to be actively involved in investment activity abroad. Moreover, this field remains heavily influenced by political factors. On the contrary, Russian Big Three telecom companies' involvement in the CIS seems to be mostly driven by purely economic considerations, while Russian investors currently control the dominant share of the mobile service providers market in the CIS. It is worth noticing, that Russian big business constitutes only one segment of the overall Russia's investment activity in the CIS (moreover, it is only the most "visible" part of the overall investment activity). Other main actors include wealthy individuals and small companies without significant presence in Russia, but with important role in the CIS, as well as ethnic networks.[3] Investments of

To conclude, after 1998 Russia and after 2000 the post-Soviet space became a field of active expansion of Russian business groups. In Russia they were able to re-integrate the national market by both establishing commercial links between local markets and lobbying lower regional protection. In the CIS, however, the situation was different: the regionalization was not followed by formal regional economic integration. Two questions remain unanswered: first, how does this re-integration process influence the quality of institutions? And second, what are the reasons for differences between the CIS and Russia? The next section examines these two issues in greater detail.

4. Political centralization, power relations and integration of markets

The development of the market integration represents only one side of the transformation of the Russian economy and politics since the late 1990s. Another aspect was the increasing political centralization and strengthening the federal center vis-à-vis regions. One of the first acts of the new president was to regain control over the federal political structures in regions (what was called "strengthening the vertical of power"): in 2000 seven new federal districts were established, where presidential representatives (mostly with a background in the military or security service) obtained the right to oversee the selection and placement of personnel in local branches of federal authorities (Ross, 2003). Furthermore, regional governors lost a significant part of their influence because of institutional changes (like the reform of the upper chamber of the Russian parliament, the Federal Council, or the right of the president to remove a governor from his office; see Hyde, 2001) accompanied by a strong public support for the new president. Whether this process was able to change completely the informal power relations of the Russian federalism is questionable

[3] Crane, Peterson and Oliker (2005), Vahtra (2005) and Libman (2007) provide a detailed account of the main actors of the Russian FDI activity in the CIS.

(Chebankova, 2005; 2007); however, the fact of increasing centralization in Russia after 2000 is beyond any doubts.

The activity of business groups fighting regional protectionism and opposing conflicts in the federation-region relations seem to have been instrumental for this re-centralization. To a certain extend, they limited the readiness of regional governments to oppose the centralization trends and created incentives for supporting the new policy of the federal government. However, while the market integration seems to be a process associated with increasing quality of institutions, the political centralization is much more ambiguous. In fact, whether the regions or the center are more prone to rent-seeking is an old debate in public economics: one could trace it back to Madison with his idea of "dilution" of influence of powerful local interest groups on the local level and Montesquieu, who considered the centralization a process of loosing public control over governments. The current empirical literature on Russia is also: Desai et al. (2005) show, that there is a positive relation between some specific indicators of economic performance of the regions and the retention of taxes in Russia; but Haaparanta and Juurikkala (2007) claim that in municipalities with higher local fiscal autonomy firms pay higher bribes. In Russia, as the experience of the late 2000s shows, the recentralization was instrumental for the overall concentration of political power in the country, which finally resulted into re-nationalization trend and reform blockade.

While in Russia market integration and re-centralization seem to be interconnected, in the CIS the process was different: although Russian corporations significantly increased their presence in the post-Soviet economies in the 2000s, the attempts of Russia to increase its political influence in the region were completely unsuccessful. The experience of Russia's interventions into the political process in the post-Soviet countries is usually dismal for Russia, and the formal institutions of the post-Soviet integration remain as inefficient, as they were. What is the driving force behind this difference? One possible explanation is related to the structure of market access property rights. The idea of market access rights (MAR) was developed by Herrmann-Pillath (2005) and can be used to describe the process of regional economic integration as exchange in MAR, which individual countries posses. An MAR defines the right of an enterprise to sell goods or make investments in a respective country. This right is granted by the government, which therefore possesses property rights on MAR. However, usually MAR are granted not to specific enterprises, but to a group of businesses – often all businesses of a particular foreign country. Therefore the MARs can be exchanged and traded between countries “possessing” them. The development of this market is crucial for the success of the integration process. A similar exchange takes place if the internal centralization is considered: individual regions through the regional protectionism measures obtained the right to allow some enterprises to make business in their jurisdiction, and could exchange the MAR against other benefits or MARs from other regions, but quite often also from the central government.

However, the nature of the property rights on MAR of new independent states and of local governments in Russia was completely different: while the members of the CIS received formally recognized property rights on MAR based on their internationally recognized sovereignty, Russian regions could “capture” informal property rights on MAR, based on the power relations with different central agencies. As noted above, the formal structure of the Russian federalism has been highly centralized since 1994. The advantages of regions were based on informal controls like tax auditing and tax collection or use of money surrogates in order to organize payments to the regional budget. Obviously, the informal property rights were much more sensitive to the changes of the power structure in the political system and therefore vanished when power constellation changed. On the contrary, formal property rights on MAR, based on international law, happened to be more stable much more stable. In fact, one of view issues the authoritarian and semi-authoritarian regimes are able to agree is the protection of their “property rights” on control of their countries. In Africa the “stability of the borders” was the main point of consensus of the organization of the international relations, protecting local authoritarian regimes. Similar processes could have been present in the community of semi-authoritarian states of the post-Soviet world.

5. Institutional competition in the post-Soviet space

The integration of markets is an important factor not only facilitating exchange and business relations, but also strengthening institutional competition. This problem seems to be especially interesting from the point of view of the post-Soviet space, where vivid regionalization from bellow is combined with absent integration from above. In the theory of institutional competition it is normally assumed, that the preferences of individuals are given and that private actors prefer institutions with lower transaction costs, which are defined as "efficient" institutions. The theoretical literature on the government-business relations in the post-Soviet space is to a certain extend ambiguous, whether this demand really exists.

A widespread point of view is that the problems of economic reforms in the 1990s were caused by low demand for efficient institutions by emerging private business. Generally speaking, three explanations apply. The first argument proceeds from the fact, that the post-Soviet economic systems were characterized by extreme concentration of property. Sonin (2003) and Polishchuk and Savvateev (2004) demonstrate that the demand for weak protection of property rights may result from inequality in the society. More rich and powerful agents can invest in a private protection system. Under a deficit of public protection, rich agents can gain from redistribution due to improper protection of property rights, because they have a significant advantage over the weaker agents. That's why they become natural opponents in improvement in public protection of property rights. Guriev and Sonin (2007) place this discussion in a political economic setting and show that weaker protection of property rights also results from bargaining between the non-democratic government and the "oligarchs".

If formal property rights are absent, the economy turns in the endless redistribution cycle and permanent power conflicts between different groups of interest (which exists in the most CIS countries either in a "hidden form" of in states with higher concentration of state power like Russia or Central Asia or more open in countries like Ukraine (Valasek, 2007), where elements of political competition are more pronounced). Economic effects of presence of multiple power groups in society competing for dominance can be disastrous, as the literature on the "voracity effect" shows (Lane and Tornell, 1996; Tornell and Lane, 1999). Even if inequality is ignored, Hellman (1998) and Polterovich (1999) describe a situation of partial reforms in transition economies, when incumbent actors, receiving special rents from non-completion of reform process, support the stability of inefficient institutions.

Braguinsky and Myerson (2007, 2007a) discuss the problems of stable asset stripping equilibrium in an economy with oligarchic property rights and high risk.

The second argument focuses on the issue of learning costs. Any individual compares his sunk costs in learning the structure and the functioning of the old institutions and the adaptation to the old “rules of the game” (e.g. bribes, licenses etc) with the advantages of the new rules. It is possible, that the sunk cost will be higher, than the gains, and individuals decide not to change the status quo, or, at least, not to invest in political activity to improve the situation. In that way the path dependence strengthens the effects of other factors inducing demand for “bad” institutions. For an entrepreneur preference for old institutions could be connected with competitiveness. In a bureaucratic environment with high market entry barriers, the first mover has important advantages, because he has already passed the bureaucratic environments. He prefers any worsening of institutional environment (e.g. higher entry barriers), because they prevent him from newcomers in the market.

The third explanation is related to the deficit of trust in the post-Soviet world. f individuals have always suspected their government, any change of institutional environment is considered to be worse than the existing equilibrium. In this situation individuals support existing, and not better institutions. In case of institutional competition environment “exit” is a reaction on any institutional changes, and not on worsening institutional environment in terms of transaction costs. The ability of the government to attract mobile factors of production by changing institutional environment is reduced; a better way to prevent “exit” is to maintain the existing institutional balance, even if it is not optimal (and is perceived as not optimal by people). Other point is, that in case of low trust investments and labor migration are consciously organized via informal channels (to avoid government’s attention) and thus lead to support of less efficient institutions of the shadow economy as an untended result. The governmental attempts to limit the expansion of shadow economy with softening the restrictive regulations do not improve the situation because people do not believe in reforms; coercive measures against the informal sector make the formal institutions even less appropriate for the private actors and only support the expansion of the shadow economy (i.e. formal outcomes of institutional competition support illicit economic activities).

One could probably claim, that the existence of demand for bad institutions is currently mostly accepted by the studies of the post-Soviet world. A more difficult problem is whether the situation changed after the initial stage of transition, and, after initial accumulation of wealth, corporations are more interested in protection of property rights and reduction of transaction costs. Following Greif and Latin (2004), the question is whether the mechanisms described above were not only self-enforcing (i.e. constituted an equilibrium), but also self-reinforcing (increased the range of parameters for their stability). On the one hand, accumulation of wealth, even if it follows from redistribution, increases the demand for property rights, thus making this mechanism not self-reinforcing. But on the other hand, the redistributive networks can include broad groups of population and become intransparent, hence increasing demand for redistribution. The same is true for the learning costs: the longer an institution exists, the higher the costs of its transformation are. Different post-Soviet countries were characterized by different constellations of costs and advantages of different institutional environments.

As institutional competition replaces supply-side monopoly on market for institutions by competitive order, the demand-side factors become more important. Therefore institutional competition shifts the market power to the demand side on the market for institutions. Hence, the “shift of demand” from “bad institutions” to “good institutions” is crucial for the evaluation of the effects of institutional competition. The situation is, however, more difficult. Institutional competition is associated with internationalisation of business activity, which has several distinct effects. On the one hand, the “exit” of efficient companies can strengthen the “voice” of inefficient companies. After most efficient companies leave the country, the remaining inefficient ones become the main income source for politicians and bureaucrats (legally and illegally) and get a larger impact on the politic decisions. A crucial issue is of course how rents for the government are generated. If “exit” reduces rents, the governments are likely to change their attitude towards institutional reforms. If, however, rents are relatively independent of “exit” (what is especially true for resource-abundant economies, like those of the CIS, see Gandhi and Przeworski (2006) for a similar analysis), the “exit” is ignored and effects of institutional competition are insignificant. Finally, the costs of “exit” can be correlated differently with preferences for institutions (for example, at an early stage more mobile companies can be exactly intermediaries enjoying the main benefits of “transition rents”). Moreover, an inefficient equilibrium resulting from the open economy includes asset striping, large capital flight (or “exit”) and low quality of institutions. The same individuals, who use the “exit” option to secure their wealth gained from assets in the jurisdictional with law quality of institutions, support with their “voice” option the “bad” institutions (see Mummert, Mummert, 2000). Given the asymmetry of the post-Soviet institutional competition, where Russian companies (more or less directly depending upon resource rents) dominate, one can hardly expect positive effects from this direction.

The second argument implies that the corporations use their investments as an instrument to transfer knowledge and better practices. It is an often point mentioned that the multinationals export their national models of regulation to the new locations of their industries and stores. For example, the business strategies of multinationals in respect to different national standards in their host countries can represent the original “national” model derived from “varieties of capitalism” reproduced abroad via corporate culture, management appointment system, incentives etc. (Pauly and Reich, 1997) Once again, asymmetric structure of the CIS is of central importance. The major “promising” factor from the post-Soviet investments is that the Russian economy mostly demonstrates better institutional performance, than the rest of the CIS.[4] Hence, asymmetric structure of institutional competition is likely to ensure higher quality of institutions. There are only few exceptions. Kazakhstan has formally implemented many “second-generation” reforms, which still fail in Russia (power utilities liberalization, amnesty of capital, reforms of communal sphere, banking, pensions system etc.). However, exactly Kazakhstan is the second important source of FDI in the CIS (following Russia). Armenia is also a certain exception with extraordinary good institutional performance. Kyrgyz Republic used to be the leader of institutional reforms in the early 1990s, but later demonstrated a worse performance. However, in many cases Russia is more advanced, than the rest of the CIS, and therefore Russian corporations act as an instrument of import of more efficient institutions. There is evidence (mostly based on discussion with CIS and Russian managers) that Russian assets often prove to be more efficient, than owned

[4] By the way, similar problems of demand for bad institutions occur in the Russian investments in Baltic states, where this “benefit of institutional advantage” of Russia is, of course, not present. See Zashev, 2004, 2007

by local or even international corporations (cf. Crane, Peterson and Oliker, 2005). The simple correlation approach suggests that Russian businesses invest in countries with lower “institutional distance” from Russia and with higher institutional quality (Libman, 2007). A large problem is, however, that the relative institutional advancements of Russia are not given: assuming low success of catching up reforms, other countries of the CIS can achieve higher institutional quality. In this case the asymmetry is going to make a negative influence on the link between institutional competition and quality of institutions.

Anecdotal evidence suggests, that demand for bad institutions can exist in the post-Soviet institutional competition. First of all, as Russian corporations have significant experience in working with “shadow” schemes, it continues using this experience abroad and thus “export” inefficient institutions or applies their experience of intransparent institutional systems as a competitive advantage. Russian businesses ability to act in a very instable legal environment is often pointed out by the observers. Obviously, they use this opportunity, thus “switching on” the self-enforcement mechanism of an institutional trap. There are many cases of intransparent “shadow” investment schemes used by the Russian corporations in the post-Soviet world. May be the most notorious is the case of two Gazprom subsidiaries in Ukraine Eural TransGas and (since 2004) RosUkrEnergo established to resell the gas of Turkmenistan. It is officially incorporated in Switzerland with 50% of the shares under the control of Gazprom and 50% represented by a nominal shareholder Raiffeisen Investment without any clear information as to who could own the shares (the assessment vary from organized crime to different political groups in Ukrainian and Russian elite and Gazprom or Naftogaz Ukraine officials). After the gas war in Ukraine, RosUkrEnergo received privileged rights of gas supply to Ukraine and partly to Europe.

The Ukrainian case is the most notorious, but not unique example of demand for bad institutions. It looks like these inefficient schemes are often even preferred by the Russian investors. For example, the second public tender on the large Ukrainian metallurgical plant Kryvorozhstal in 2005 is often considered as one of the seldom examples of completely transparent privatisation in the CIS. Russian investors, although very interested in the plants and active during the former tenders, rejected to participate. On the other hand, the business activity of Russian corporations in “unrecognised republics” Transdniestria and Abkhasia also shows that the Russian corporations do not hesitate working in semi-legal environment. Replacement of Russian business practices in the CIS discussed above also has a double effect. On the one hand, they may be superior to what exists in the post-Soviet world, as discussed above. On the other hand, however, the model exported is also an example of the “institutional trap”. For example, in their fight over Kyrgyz telecom asset BiTel Russian and Kazakh investors (and later Russian companies VympelCom and MTS) resulted into seizure of the company’s headquarters by an armed group in police uniform, which rejected to follow the orders of the minister of internal affairs (in the post-Soviet world directly in charge for the police).

Most arguments for the interjurisdictional competition in the CIS apply also for the interjurisdictional competition between Russian regions. However, the market integration in Russia also supports a very specific form of institutional competition. As demonstrated above, unlike the CIS, the market integration in Russia is strongly interrelated with the development of political centralization. Therefore the institutional competition usually takes place at informal level, i.e. is related to “hidden” policies and rules established by the regional governments. Most post-Soviet countries face the problem of permanently increasing corruption. Corruption has a double effect on institutional competition. On the one hand, it is likely to increase the benefits for the governments from attracting capital and economic growth (Allen et al., 2006). From this point of view corruption is just an additional tax (price of institutions), which reduces to the marginal benefits of institutions in turn of the competition process. This effect seems to be present e.g. in the competition between Indian states. But, given the fact, that the actors of institutional competition are mostly not abstract “governments”, but individual agencies and administrations, it is likely, that the competition takes form of “protection” of privileged enterprises from rivalry agencies, which leads to overall decline in taxation and underproduction of public goods (Yakovlev, 2006). From this point of view the market integration creates an additional incentive for regional protectionism, which is in fact disturbing the functioning of the market integration, i.e. market integration is not self-reinforcing in terms of Greif and Latin! The question how the system is going to evolve in the future remains open.

6. Conclusion

The aim of the paper was to understand the impact of big business on the development of the spatial order of authority in the two institutional systems in the post-Soviet space: Russian federalism and the post-Soviet integration – and their impact on the quality of institutions. From the point of view of impact of big business on spatial organization of authority, there are also clear similarities between the Russian federalism and the post-Soviet space in the beginning of reforms and differences at the later stage. Although in the 1990s the business interests contributed to the segmentation of both Russian internal market (in form of the provincial protectionism) and the post-Soviet economic space (in form of “quasiintegration”), since 1998 the situation changed for the Russian Federation and since 2000 for the CIS. The development of interregional business groups was instrumental for the reintegration of the Russian economic space; currently the expansion of Russian corporations in the CIS is important for the regionalization in this area.

While the institutional impact of business interests supporting fragmentation of the economic space is obviously negative (and indeed contributes to the disorganization as an important source of economic problems for the post-Soviet countries), the re-integration is ambiguous: in Russia, removing the inefficiencies of the early stage of transition it also indirectly supports the political centralization and increasing rent-seeking. In the CIS the situation is different, reflecting different structure of market accession property rights: the informal property rights in Russia were much more instable from the point of view of changes of power relations than formal MARs set in the CIS. Another aspect of market integration is intensified institutional competition. Although the theory considers this process an efficient instrument of increasing the quality of institutions by controlling Leviathans, in the post-Soviet space the relation seems to be more complex because of the demand for bad institutions and “hidden” forms of competition in a centralized federation. Table 1 summarized the main features of development of both institutional systems and their impact on quality of institutions.

Table 1: Development of the Russian internal market and post-Soviet economic space compared

	Russian internal market	Post-Soviet economic space
Role of the business groups in the 1990s	Support of fragmentation through regional protectionism	Support of fragmentation by technological quasi-monopolies
Market accession property rights	Informal (by the regional authorities)	Formal (by the new independent states)
Role of business groups in the 2000s	Start of regional expansion in 1998; support of re-integration through economic activity and lobbying against regional protectionism	Start of international expansion in 2000; regionalization from bellow
Outcomes for the spatial order of authority	Re-centralization of the Russian Federation	Failure of attempts of economic integration from above
Outcomes for the quality of institutions	Advantages of re-integration vs. disadvantages of re-centralization and possible disadvantages of institutional competition in presence of corruption	Advantages of re-integration vs. possible disadvantages of institutional competition in presence of demand for bad institutions

To conclude, the impact of big business on the quality of institutions through the channel of changes of spatial order of authority was ambiguous, however, there are good reasons to believe that there have been many problems associated with this aspect of institutional development of the post-Soviet countries. It is worth questioning, whether an institutional system of the Russian federalism and of the post-Soviet integration limiting negative effects and supporting positive effects through market integration could be designed and implemented – yet the latter issue crucially depends on the overall political development and economic reforms in the post-Soviet world.

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