博士論文（要約）

Doctoral Thesis (Abridged)

From market to the state: the politics of state ownership in Russia and Kazakhstan

（市場から国家へ：ロシアとカザフスタンにおける国有の政治）

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Abstract

Why are some leaders in authoritarian regimes motivated to increase state control over the key sectors of the economy, driving out the private sector? Informed by the scholarly discussion regarding the rise of state capitalism in the developing world, this dissertation provides a fresh perspective on the political logic of nationalistic economic policies in authoritarian regimes. It takes an authoritarian power politics in economic policymaking as a framework and explains why the necessity of maintaining political power and stability in authoritarian regimes breeds increased state control in critical sectors of the economy and how these motives ultimately shape an economically inefficient, yet politically stable economic system.

Based on a detailed and in-depth analysis of statist inclinations in the post-Soviet economies of Russia and Kazakhstan under presidents Vladimir Putin and Nursultan Nazarbayev, the dissertation argues that the rise of statist economic policies in these countries since 2000 does not stem from either the policies of economic modernization under the auspices of developmental state or internal fighting between domestic factions over the property, as usually argued in the literature. Instead, this dissertation argues that an amalgam of such policies constitutes a new political-economic order in post-Soviet Russia and Kazakhstan, a distinct type of *authoritarian state capitalism*, whose emergence can be best explained by the irreconcilable nature of the tension between the social forces brought by liberal reforms during the 1990s and the necessity of consolidating and sustaining authoritarian regimes by the new rulers. Put simply, by bringing the state control to crucial sectors of the economy, the rulers in Russia and Kazakhstan aimed to tame the political behavior of emerging social groups with a financial basis to challenge the power possibly. In addition, a rise in state control also enabled the regime to increase its financial ability to distribute the spoils to patronage programs.

Acknowledgements

This research was made possible owing to the continuous support of many people over the past few years. First, I owe a significant debt of gratitude to my supervisors, Professor Nobuhiro Hiwatari and Akio Takahara along with the members of dissertation committee for their continuous support and forbearance until the completion of this dissertation. Their constructive criticism and sharp comments helped me raise the bar higher and their unwavering diligence and benevolence have been encouraging.

I also would like to thank Professor Richard Westra for guiding me through unexplored gates of political science in the first place and cultivating a critical perspective in my mind. I am also particularly grateful to the faculty and staff members in GSDM at The University of Tokyo for financial and moral support throughout my doctoral years at GraSPP. I also owe an intellectual debt to Professor Laruelle Marlene and Henry Hale at IERES, George Washington University, Washington DC, for their kindhearted invitation to Washington DC and thought-provoking discussions.

Lastly, immense indebtedness goes to my brothers, Sherzod, Bunyod, and Dilshod and close friends in Japan as well as my wife Leila and daughter Sumayya, whose wholehearted encouragement and moral support were the source of my inspiration to complete my degree.

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Acronyms

CBR - Central Bank of Russia

ENRC - Eurasian Natural Resources Corporation

KGB – Secret Service of Former Soviet Union

KMG – KazMunaiGaz

NOC – National Oil Company

RSPP – Russian Union of Industrialists and Entreprenuers

SME – Small and Medium sized Enterprise

SOE – State-owned Enterprise

IOCs - International Oil Companies

SK - Samruk Kazyna

SWF – Sovereign Wealth Fund

TWG - Trans World Group

VEB - Vnesheconombank

VTB - Vneshnotargobank

Chapter 1. Introduction

This dissertation uses the economic policies of Russia and Kazakhstan under the presidents Vladimir Putin and Nursultan Nazarbayev that favor increasing state control and ownership in certain sectors of the economy as case studies to investigate why personalist autocrats attempt to install control over highly lucrative sectors of the economy and what kind of political, economic order such decisions bring about. Taking an authoritarian power politics in economic policymaking as a framework, the dissertation argues that the chaotic transitions to liberal market economies after the collapse of the Soviet Union produced various economic actors in Russia and Kazakhstan with financial resources to challenge the new leaders and capture the state. The need to consolidate power in the face of challengers and further sustain the regime with resources incentivized the president Putin and Nazarbayev to bring state control over the key sectors. In its analysis, the dissertation will attempt to dissect this key hypothesis.

1.1 The economic liberalization and return of state control in the post-Soviet area

The collapse of the Soviet Union and the crumbling economy it commanded for decades forced the post-Soviet countries to find a new type of economic system that balanced the interaction between state and market.[1] Exhausted by the deformities of the Soviet economy for years, the emerging countries embraced market economics for their development. Although the cornerstones of this transition - economic liberalization in different dimensions - varied among them in speed and scope, Russia and Kazakhstan showed a sincere interest in transforming their economies towards market mechanisms for the allocation of resources. Boris Yeltsin's famously declared statement, "the task that I have set before the government is to make the reforms irreversible" could epitomize their passion for reform.[2] As Table 1 shows, the scores of transition indicators in both Russia and Kazakhstan substantially improved regarding the depth of policy reforms in price liberalization, open trade, enterprise restructuring, and institution building, putting them as top reformers among former Soviet republics like Ukraine and Belarus.

[1] Yelena Kalyuzhnova, "The Kazak Soviet Socialist Republic in the USSR," in *The Kazakstani Economy: Independence and Transition*, ed. Yelena Kalyuzhnova, University of Reading European and International Studies (London: Palgrave Macmillan UK, 1998), 3–13, https://doi.org/10.1007/978-1-349-14430-3_1.

[2] Timothy Frye, "Original Sin, Good Works, and Property Rights in Russia," *World Politics* 58, no. 4 (July 2006): 479, https://doi.org/10.1353/wp.2007.0007.

The critical reform among everything was *destatization,* the attempt to abolish state ownership through different means of privatization. By the end of the 1990s, the private sector share in GDP accounted for 70% and 60% in Russia and Kazakhstan in 1999, respectively.[3] With the help of privatization, which is usually associated with the emergence of so-called oligarchic "financial-industrial groups," the most assets, even in unlikely sectors such as energy and metals, were transferred to private hands, though in dubious fashion. In Russia, for instance, so-called oligarchs dominated the largest industrial sectors by early 2000. In particular, their share in oil sales accounted for 72%, while ferrous and non-ferrous metals accounted for 78% and 92%, respectively.[4] The only sectors in which the state preserved its control were so-called natural monopolies like pipelines, natural gas, and energy.

Table 1. EBRD transition indicators of former Soviet Union counties, 1991-2000

	Kazakhstan		Poland		Russia		Ukraine	
	1991	1998	1991	1998	1991	1998	1991	1998
Price liberalization	1.0	3.0	3.0	3.3	1.0	2.7	1.0	3.0
Small-scale privatization	1.0	4.0	3.0	4.3	1.0	4.0	1.0	3.3
Large scale privatization	1.0	3.0	2.0	3.3	1.0	3.3	1.0	2.3
Enterprise reform	1.0	2.0	2.0	3.0	1.0	2.0	1.0	2.0
Banking sector reform	1.0	2.3	2.0	3.3	1.0	2.0	1.0	2.0

Note: Indicators are measured on a scale of 1 to 4.33, with pluses and minuses

Source: EBRD (2000)

The same was true in Kazakhstan, where external shocks following the Soviet collapse produced adverse economic outcomes.[5] In the face of possible failure due to these external shocks, the leadership of Kazakhstan adopted a rapid reform strategy to construct a market-oriented economy. Emphasizing an "economy first, politics second approach," President

[3] EBRD, "Transition Report 2000 Employment, Skills and Transition," 2000.

[4] Gabriel Di Bella, Oksana Dynnikova, and Mr Slavi T. Slavov, *The Russian State's Size and Its Footprint: Have They Increased?* (International Monetary Fund, 2019), 10–12.

[5] Martha Brill Olcott, *Kazakhstan: Unfulfilled Promise* (Carnegie Endowment, 2010), 131.

Nazarbayev said, “the market is a democracy based on rigorous financial accountability.”[6] To construct marketization, the leadership opted for neoliberal policies in the framework of price and trade liberalization, private ownership, and privatization, and reducing the state's role in the economy. Being broke, the government had no option but to engage with the international community so that it could attract international companies and foreign investment. Desperate for cash amidst the crumbling economy, the government sold many of its formerly state-owned enterprises to international investors. In the oil sector, Kazakhstan’s price sharing agreement with large multinational companies accounted for 86% of the total oil production.

Table 2. Privatization of major companies in Kazakhstan by 2000

Major companies	Sector	Buyer	Basis, value%
Shymkent oil refinery	Refinery	Vitol Munay	94%
GAO Yuzhneftegaz	Oil	Hurricane Hydrocarbons	89.5%
Karazhanbasmunai	Oil	Triton – Vuko Energy Group	94.5%
Mangistaumunaigaz	Oil	Central Asian Petroleum	65%
Aktyubinskmunaigaz	Oil	(CNPC)	60%
Uzen Oil Fields	Oil	(CNPC)	60%
Tengiz	Oil field	Mobil	50%

Source: Pomfret (2005)

However, interestingly, starting from early 2000, the more or less liberal economies of both Russia and Kazakhstan marked an abrupt break from their commitment to *destatization*. The return of the state activism in economic governance and its control over the critical sectors of the economy gained substantial strength with the start of the new century in 2000. In other words, economic nationalism through various takeovers has become a notable process in both the Russian and Kazakhstani economies. The increasing state intervention and control coincided with Putin’s second presidency during 2004-to 2008. In the economy it was manifested in

[6] Ariel Cohen, *Kazakhstan: The Road to Independence. Energy Policy and the Birth of a Nation* (Silk Road Studies Program, Institute for Security and Development Policy, 2008), 21.

several instruments through which state extended its hand over influential sectors of economy. Namely, it included major acquisitions of companies by the state and consolidation of state ownership in strategic industries, banks & media, the creation of vertically integrated state corporations and various investment funds and slowing down of privatization. Following hostile takeovers, the share of SOE's in total Russian market capitalization increased from 24% to 40% from 2004 to 2007.[7] As of 2014 their share in total market capitalization accounts for 39%, the highest in OECD countries whose public sector varies between 3% to 10%. Such intimidating state control was also observed in finance, as can be seen in table 3, where the state banks gradually replaced the private banks and increased their share in the banking assets from 40% in 2000 to 60% in 2010. An essential part in the statist shift was the genesis of "state corporations" in Russia, a unique type of state companies that were formed to consolidate state-owned assets in heavy industries, that Putin invented to help strengthen the state power and control in industry.

Table 3. Market share of top-ranking banks in Russia, 2011

Name	Ownership	Market share, percent of	
		Total assets	Profits
Sberbank	State-owned	25.9	37.9
VTB Group	State-owned	17.1	6.4
VTB	State-owned	*9.8*	*2.5*
Bank Moskovy	State-owned	*3.2*	*0.7*
Gazprombank	State-owned	5.8	4.6
Rosselkhozbank	State-owned	3.5	0.2
Alfa-Bank	Domestic private	2.3	1.3
UniCredit Bank	Foreign controlled	2.1	2.0
Rosbank	Foreign controlled	1.5	1.0

[7] Alexander Abramov, Alexander Radygin, and Maria Chernova, "State-Owned Enterprises in the Russian Market: Ownership Structure and Their Role in the Economy," *Russian Journal of Economics* 3, no. 1 (March 1, 2017): 10, https://doi.org/10.1016/j.ruje.2017.02.001.

Source: Vernikov (2012)

A similar move to increase state control in the economy was observed in Kazakhstan after t the oil price boom during early 2000. Taking this opportunity to alter the unfavorable results of his liberalization efforts, President Nazarbayev started to fortify the national oil company, KazMunaiGaz, to acquire a greater share in industry amid stronger international presence of oil companies.[8] Over the years, KazMunaiGaz became state's important instrument for devouring several private oil companies in the face of mounting political challenge against President Nazarbayev. The strong presence of state also spread to the banking sector after the financial crisis in 2008 where the state had to bail out majority of banks. As a result, by 2010 the large part of the economy was de facto brought into a single state holding company, Samruk-Kazyna, whose extensive profile of companies made up half of the economy.[9] Figure 1 can indicate the spread of state control in both countries.

Figure 1.

Yet the irony is that the state control over the strategic industries did not signify a complete ebb of liberal market principles in either country. In Russia, this can be epitomized in the reform package of the Gref Program which was initiated after Putin came to power to fix the lingering tax issues and improve the business environment.[10] Furthermore, in both countries there are still a host of successful private companies that operate in such crucial sectors as oil, metallurgy, and banking. At the same time, both governments have carried out liberal reforms in the arena of tax, corporate governance, and rule of law so that they earn higher liberalization scores and attract investment from outside. Figure 2 below succinctly summarizes the chronicles of transition describe above.

Figure 2. The chronicle of the transition from market economy to state capitalism in Russia

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[8] Paul Domjan and Matt Stone, "A Comparative Study of Resource Nationalism in Russia and Kazakhstan 2004–2008," *Europe-Asia Studies* 62, no. 1 (2010): 35–62.

[9] Richard Pomfret, *The Central Asian Economies in the Twenty-First Century: Paving a New Silk Road* (Princeton University Press, 2019), 88–91.

[10] Anders Åslund, "Russia's Economic Transformation under Putin," *Eurasian Geography and Economics* 45, no. 6 (September 1, 2004): 402–4, https://doi.org/10.2747/1538-7216.45.6.397.

1.2 The research questions and the significance of the dissertation

As described above, these changes regarding *re-statization*, the rise of the state as an important factor in economic governance, in both Russia and Kazakhstan in fact insinuated a new era in their political economic history that presents an excellent opportunity to examine their root causes. In understanding the reasons behind the emergence of new political-economic order with the state taking an assertive role in economy, this dissertation asks the following questions: *what explains the leaders' motivation to increase the state control over key sectors of the economy? What does this tell us about the overall politico-economic order in these countries?* Reflecting these changes, several scholars have attempted to explore the nature of the ensuing economic systems under the label of state-led capitalism. Yet, the existing arguments still leave a gap in explaining why the political leadership opted for state activism and control in their economic governance.[11] Particularly lacking is an inquiry that takes into account the distinct character of the political regimes in these countries in explaining the abrupt shift to statist control over key sectors of the economy.

Taking an authoritarian power politics in economic policymaking as a framework, this dissertation aims to explain why the logic of political power and the necessity of stability in authoritarian regimes aspires to achieve breeds an increased state control in key sectors of

[11] David Lane, "From Chaotic to State-Led Capitalism," *New Political Economy* 13, no. 2 (June 1, 2008): 177–84, https://doi.org/10.1080/13563460802018505.

economy and how these motives end up shaping an economically inefficient yet politically stable economic system. In the empirical realm, taking the case studies of authoritarian Russia and Kazakhstan, it seeks to explain the political reasons behind the rise of state control in certain sectors of economy and the peculiar type of state-led capitalism that emerged following a brief period of economic liberalization.

The focus of this dissertation pertains to some of the important issues related to the subject of both regime studies and area studies of post-communist transition after the independence. As for its theoretical considerations, the dissertation topic is interested in understanding the economic logic of authoritarian regimes as these regimes are prone to be different from democracies in terms of the exercise of power, political challenges, and constraints. An analysis of how autocrats make economic decisions and why they use the mixture of state control and free market mechanisms is important to understanding not only the way that autocracies exercise political power, but also the way they adopt to the developments in the global economy. Such analysis is also crucial for understanding the pathways through which contemporary authoritarian regimes can resist the global calls for capitalist democracies.[12]

In terms of public policy, this dissertation has practical importance in explaining two important questions: First, it attempts to shed light on why attempts to build liberal market economies does not always materialize in the post-Soviet authoritarian regimes, but rather end up forming a state capitalist model with the state taking up an active and important role. For this purpose, the dissertation takes an account of how the more or less liberal economies that emerged in Russia and Kazakhstan following independence were gradually replaced by statism in certain areas deemed as strategic and how this emergent system, dubbed as state capitalism, works at the expense of genuine market forces. Specifically, it chronicles the major events that led to the emergence of important state companies/corporations, funds, and state banks. It also analyzes how the emergence of these establishments produced a new equilibrium in state-business interactions of these countries in recent years. Second, it attempts to understand what implications the gradual change toward statism in Russia and Kazakhstan over time bear on an overall process of marketization in transition countries. It specifically explains how political

[12] Raymond Hinnebusch, "Authoritarian Persistence, Democratization Theory and the Middle East: An Overview and Critique," *Democratization* 13, no. 3 (June 1, 2006): 373–95, https://doi.org/10.1080/13510340600579243.

regimes carry out the economic reforms and although doing so, why they always come up with economically inefficient but politically important outcomes.

1.3 The main argument and the scope of theoretical framework

What explains leaders' motivations to increase state control over the economy that ultimately results in state capitalism? The main argument of this dissertation is that leaders' political exigencies to consolidate power and maintain political stability against the rise of an oligarchic economy gives rise to state control over the economy and a distinct form of state capitalism. In this dissertation, such an economic system is described as *authoritarian state capitalism* where the private market actors operate alongside the state's political prerogatives in strategic sectors of the economy. The scope of this theory expounds the mechanisms in which such dictatorial state capitalism emerged personalized authoritarian regimes in Russia and Kazakhstan and how it compares to the distinct type of state capitalism in China.

The underlying assumption that guides the theoretical foundation of this dissertation is that personalist dictators always aim to maintain power and ensure political survival. The objective of dictatorial regimes is not limited to mere political survival but can include such grandiose rhetoric as national greatness and competitive economies. However, the latter objectives usually serve as one of the tools to further the main objective of political survival. Consolidation of political power and its subsequent exercise necessitate the dictator's control over economic resources. Access to a continuous stream of economic resources empowers the political life of dictator in different ways. Economic resources give a dictator the means to increase his bargaining power vis-à-vis another ruling elite in the early phase of his rule. Access to resources gives him substantial control over appointments to the state apparatus through which he can install loyalists into important positions and launch agencies to pursue goals not shared by the rest of the elite. With this increased power, the ruler redirects his concern to neutralizing an influential elite with autonomous political and economic power.[13] The consolidation of power finally opens a way for the dictator to personalize power, which in turn increases his prerogative of undertaking more interventionist economic policies. Such policies help him share the spoils with a new coalition that includes the cooperative elite, submissive

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[13] Marc Morjé Howard and Philip G. Roessler, "Liberalizing Electoral Outcomes in Competitive Authoritarian Regimes," *American Journal of Political Science* 50, no. 2 (2006): 365–81, https://doi.org/10.1111/j.1540-5907.2006.00189.x

oligarchs, and supportive people. The combination of these changes culminates in a dictatorial-oligarchic economy in which political power is personalized in the hands of one person, while economic governance is dominated by the active state that serves the regime survival.

1.3.1 The contrasting patterns: variations in state capitalism

What is the scope of this theoretical framework? How does this theory apply to case studies of Russia and Kazakhstan and how does it compare to China's version of state capitalism? The dissertation found that due to the irreconcilable tension between social forces brought about by early liberal economic reforms and the necessity of consolidating power and extending survival, both Putin and Nazarbayev created state capitalist systems that manifested state ownership of strategic assets. As analyzed throughout this dissertation, this process was similar in both states.

Liberalization and the radical privatization of key industries in both Russia and Kazakhstan following the breakup of the Soviet Union resulted in the concentration of important economic assets, especially in the energy sector where assets came to be held by the oligarchic class, and multinational companies in Russia and Kazakhstan. Vladimir Putin and Nursultan Nazarbayev saw the emerging pluralist politico-economic system as breeding ground for political opposition by oligarchs whose political engagement was deemed to generate political chaos. This created an opening for autocratic ascendency for presidents who began to consolidate power and stabilize the regime through centralization and targeted repression. The logic of power consolidation and subsequent regime survival then required both presidents to conduct asset expropriations and limited state intervention.

Following the consolidation of power, Putin and Nazarbayev both effectively personalized the political system, further increasing their autocratic discretion over political and economic policymaking. Such personalized political systems brought structural changes to existing economic arrangements in Russia and Kazakhstan. While the liberal market economy previously involved the interplay between fair market forces and benign state regulation, dictatorial state capitalism brought the state control over certain strategic sectors and allowed only limited *market freedom* for regime loyalists, foreign companies, and small businesses. The new political economy that emerged under the personalist regimes of Putin and Nazarbayev featured what this dissertation describes as *authoritarian state capitalism* with a dualistic nature. In this new politico-economic order, the state emerged as an active manager and owner of

strategic economic assets through targeted expropriations for supposedly "economic modernization" purposes, while the rest of the economic sectors, deemed not strategic, became open to market forces.

Within this scope, the theoretical framework in this dissertation presents a marked contrast between the version of state capitalism that emerged in the post-Soviet countries under the conditions described above and state capitalism in China that followed a quite distinct historical path. The rise of dictatorial state capitalism in the post-Soviet Russia and Kazakhstan is closely related to the radical privatization of key industries and political instability. In stark contrast, the Chinese version of state capitalism was engineered as a political necessity of maintaining legitimacy and encouraging economic growth. The regime gradually shed its grip over the economy and introduced markets without resorting to radical policies that could destabilize its power. Political leaders' foresight in anticipating the emergence of new economic and political forces that radical market reforms would bring helped them to politically refine the contents of state capitalism out of the decrepit socialist economy.

In addition to the conditions under which the state capitalism emerges, the scope of theory in this dissertation touches upon the *nature* of the state capitalism in different political contexts. This means that differences related to the nature of regime coalitions in authoritarian regimes produce different types of state capitalist economies. Despite Russia, Kazakhstan, and China all featuring authoritarian political systems whose sole priority is to maintain political survival through various means, regime coalitions in these autocracies tend to be formed from various groups. Based on this reasoning, autocratic state capitalism in Russia and Kazakhstan presents two versions: *crony-style* and *family-dominated*. Crony-style state capitalism in Russia features an economic system in which powerful friends and cronies of Putin dominate the major sectors of economy through a uniquely designed state-private partnership. Taking advantage of positions at the state companies and living off government contracts, political elites and crony oligarchs have been able to generate massive personal wealth and transformed the Russian economy into a kleptocracy.

In contrast, state capitalism in Kazakhstan is a *family-dominated* version in which the extended family members of Nazarbayev dominates major sectors of economy. Strategic sectors of the economy such as the oil and gas industry were concentrated under a single entity that has been governed as a family business over the years. By comparison, the political system in China

features a single-party regime in which the political rule is institutionalized around the party and the power is shared among broader coalition. Such institutional differences in authoritarian rule in China produced *party-state capitalism*. It is built around collective party leadership which maintains a balanced interaction among such objectives as top-down political control over strategic sectors, a bottom-up competitive market economy, and the integration to global economy. Each chapter provides a detailed analysis into the nature of these economic systems.

1.3.2 Value-added: putting theory in the context of existing literature

The idiosyncratic feature of this dissertation lies in the fact that it combines two related but diverse fields, political economy, and regime analysis, in its original theoretical approach and methodology. In terms of political economy, the originality of this research comes from its intent to break with the existing literature in offering a nuanced analysis of state capitalism. The existing literature scrutinizes state capitalism as an opposite of the liberalist status quo by focusing on major economies and thus neglecting diversity in case selection. A trajectory of the scholastic interest in state capitalism took two divergent routes following the 2008 financial crisis: the works of liberal-inspired critiques who warned of the threats posed by state capitalism and the works of policy-oriented observers who dealt with the institutional underpinnings of the system. However, neither did a fair job of explaining the role of political structures and power relations behind the rise of such systems. By connecting the way that political power works in three distinct authoritarian regimes with their economic systems, the research will fill a gap in the existing literature.

The political nature of economic systems in post-Soviet countries also led to a resurgence of scholarly works by area experts. Yet in explaining the rise of state intervention in Russia and Kazakhstan under their respective authoritarian rulers, these scholars either focused on ruler's personal preferences for economic modernization or infighting among domestic factions for assets. When it comes to China, scholars took a whole different approach, seeing China's state capitalism as a communist legacy and making it hard to conduct a comparative analysis with other countries. In short, area scholars also failed to take into account the economic structures and political environments in which these authoritarian leaders make important decisions. Thus, by bringing structural analysis of these political systems into the equation, this dissertation offers a novel explanation of an important phenomenon that should be of interest to scholars.

This dissertation also provides a novel explanation of the mechanisms through which state capitalism functions. In explaining the workings of state-capitalist economies, scholars exclusively focused on state-owned enterprises or sovereign wealth funds. Yet, by omitting an analysis of private sector activity, especially that of oligarchic big businesses that operate alongside the state companies, it is impossible to understand how the state-market interaction produces a coherent state capitalist economy. Hence, in considering both big and small private businesses along with state dominant sectors into a holistic view, this dissertation produces a fine theorization of the dualistic nature of state capitalism and adds a new dimension to the discussion. Such dualistic analysis will enable us to better understand the puzzling existence of liberal principles of market economies in non-democratic capitalist systems, including a freer business environment conducive to private ownership and foreign investment and their political rationale.

In terms of regime analysis, the findings of this dissertation contribute to theoretical debates on the rise of personalized politics in both authoritarian countries and in weakening democracies witnessed throughout the world. Its analysis produces new insights on how "strongman" politics is emerging in backsliding democracies such as Turkey, Russia, and Hungary, with important implications for promoting free governments and open economies. Its analysis dispels a widely held assumption that all authoritarian countries, regardless of type, function in a similar context with similar logics and hence produce similar political and economic outcomes. By connecting specific attributes of personalist regimes to statist economic outcomes, this dissertation advances our understanding that the personal configuration of power, survival strategies and economic structure peculiar to some personalist regimes produce different incentive structures and thus different patterns of decision making conducive to state control. This means that an autocrat in a personalist regime who faces a similar incentive structure tends to put more control over the economy than other regime types. Such analysis of resource asymmetries is currently relevant to the world affairs in terms of explaining why some autocracies rarely face popular uprisings or are resilient in the face of domestic challenges, and what kind of political outcomes such contestations produce. What this tells us is that personalist autocrats tend to have an upper hand vis-a-vis elite coalitions and civil society due to their monopoly over economic resources, which will limit the opposition's capacity to organize and challenge the regime. In other words, it is likely that popular political contentions in personalist

regimes with resource monopolies produce different outcomes that are less conducive to democratization, as opposed to party-based or military regimes, although rigorous empirical research remain essential to establishing causal connections. Overall, through its novel findings, the timely research of this dissertation is expected to make a significant impact on theories of state-market interactions, the politics of economic decision making in authoritarian contexts, and the political economy of post-communist area studies.

1.4 Methodology: Russia and Kazakhstan as case studies

The dissertation mainly takes a quantitative approach in its methodology, putting a thorough focus on small-N studies of two countries. Using two post-Soviet countries, Russia, and Kazakhstan, as case studies, the dissertation analyzes the statist policies that their autocratic leaders pursued in such state sectors as oil, gas, metallurgy, mining, and finance with a special emphasis on state-owned companies (SOE). In contrast to the sectors that the tstate has important presence, the dissertation also explores conditions and rules of such market sectors, such as manufacturing and retail, in which small entrepreneurs run their businesses. The analysis that the dissertation conducts is mainly built on the extant studies on the post-Soviet political economies as well as official statements, briefings, and reports. It also utilizes semi-structured interviews conducted in Washington DC with government officials, area experts, and civil society groups.

The political economy of state control and ownership in Russia and Kazakhstan is the primary focus of this dissertation. Russia and Kazakhstan constitute an appropriate and salient case for investigating the rise of state control and subsequent resurgence of state-led capitalism. First, Russia and Kazakhstan provide two of the most similar cases in understanding the reasons behind the rise of economic system with active state control and ownership. What makes the selection of these countries for this dissertation worthwhile is the similar economic outcomes that resulted after political consolidation of power by their presidents. The similarity of outcomes invites questions as to why this might be the case, providing grounds for potential answers. Similar outcomes in both countries strengthens the process-tracing in unpacking the precise causal chain between the rise of state control and the exercise of political power in personalist authoritarian regimes. Second, as relatively under-studied countries with state-led capitalist economies, the cases of Russia and Kazakhstan can provide new explanatory power

to the “substantively important” cases such as China.[14] Focusing on the rise of state capitalist economies in the post-Soviet area enables us to gain advantage in developing new theories.

1.5 The roadmap of the dissertation

The dissertation proceeds as follows: The first part of chapter 2 will propose a theoretical framework of statist control in post-Soviet countries, bringing the nature of political regime into the equation. It develops the lead hypothesis regarding the rise of state intervention and control in the current economic system in Russia and Kazakhstan. Analyzing how politics in personalist regime types play out regarding acquisition and exercise of power, the chapter discusses the way in which structural considerations affect the autocrat’s economic decisions regarding the expropriation and state control over economy. The insights in the chapter serve as the guiding framework on which the case studies will be based.

Having revisited the core arguments, the second part of chapter 2 then analyzes the gist of the extant studies with the causal linkage they establish to explain the intersection of politics and economics. To do so, the chapter introduces pioneering studies regarding the rise of state involvement in the liberal economies in the developing world, which came to be known as *state capitalism*. Then it will proceed to scrutinize the diverging views regarding the *shape* of political economic order in post-Soviet Russia and Kazakhstan since the collapse of Soviet Union. Finally, extending on the subsection, the chapter provides an in-depth analysis of existing debates on the rise of statist control in commanding heights of Russia and Kazakhstan under three categories and provide reasons as to why they fail to take the nature of regime into consideration.

Chapter 3 then proceeds with applying the theoretical framework to the case studies of Russia and Kazakhstan. The chapter divides into 2 sections: 1) a comprehensive analysis of Russian political economy from 1986 to 2018 under three presidents, Mikhail Gorbachev, Yeltsin, and Putin and 2) the political economy of Kazakhstan from 1991 to 2016 under the President Nazarbayev. The chapter discusses how the historical account of political and

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[14] Gary Goertz and James Mahoney, “Concepts and Measurement: Ontology and Epistemology,” 172, accessed August 13, 2021, https://journals.sagepub.com/doi/full/10.1177/0539018412437108?casa_token=kzTNz10O6ToAAAAA%3AeWXYhV1DOm-eN8XD0gUxJr5k84jzoiWHVha_cC2C2A4lICFgWK3khNSC6NDcSRzTEUxHI_Dz8PIrug

economic transition in both Russia and Kazakhstan paved a way to the emergence of new politico-economic system. The chapter then proceeds to analyze the emergence of new political and economic order under new presidents, Vladimir Putin and Nursultan Nazarbayev through three stages: 1) the consolidation of power and creation of markets, 2) the personalization of power and creation of dualistic capitalism and 3) the embedded nature of emerging soft version of personalistic cult in both countries.

Throughout chapter 4 and chapter 5, the dissertation provides in-detail analyses of how the state and market sectors operate in the dualistic capitalism in Russia and Kazakhstan. Specifically, chapter 4 examines the rise of state control and asset consolidation in several strategic sectors of Russia and Kazakhstan, including hydrocarbon, heavy industries, and finance, with a particular focus on the specific companies deemed national champions. The chapter argues that the control over the state sector helps the regime maintain its stability through three important mechanisms: 1) a provision of revenue and economic growth necessary for the regime to stay in power, 2) a provision of necessary patronage for the ruling coalition, including the political elite, while controlling the emergence of new wealth centers and 3) an avoidance of economic crisis that threatens the regime collapse. Similarly, chapter 5 discusses the existing market sectors in two countries, emphasizing the oligarchic businesses in metallurgy and mining and small businesses in retail and manufacturing. The chapter argues that oligarchs in both economies have played an intermediary role between the state sector and market economy, achieving a *modus vivendi* whereby complete loyalty and service to the state's objectives grant state support and voice access to the policy decisions.

Finally, chapter 6 concludes the dissertation with a detailed summary of findings, drawing theoretical and policy implications. The final chapter also provides a concise comparative discussion of how state-capitalist systems in Russia and Kazakhstan share similarities and differences with the Chinese state capitalism, suggesting avenues for further research.

Chapter 2. A theoretical framework and literature review: the political economy of post-Soviet Russia and Kazakhstan

"Life in a dictatorial elite is thus insecure, dangerous, and frightening."

(How dictatorship works, Barbara Geddes, etc.)

What explains leaders' motivations to increase the state's control over key sectors of the economy? What was the reason behind the rise of statist control in the economies of Russia and Kazakhstan after a brief preclude of economic liberalization? This chapter lays out the analytical framework of the dissertation to answer these questions. It argues that the rise of state intervention and control in the current economic system in Russia and Kazakhstan is inherently connected to and thus can be best explained by the nature of their *personalized authoritarian regimes:* the insecurities of establishing a personal dictatorship and the logic of power relations that play out in this regime. In fact, the coexistence and codependency of the economic and political order in these countries are particularly salient as both orders developed at the same time after the collapse of the Soviet system. In the second part, the chapter will analyze the gist of the extant studies with their causal linkage. The chapter examines existing arguments regarding the nature of the political economies that emerged in post-Soviet space along with the root causes. It then briefly demonstrates why the current arguments fall short of adequately explaining the resurgence of state control.

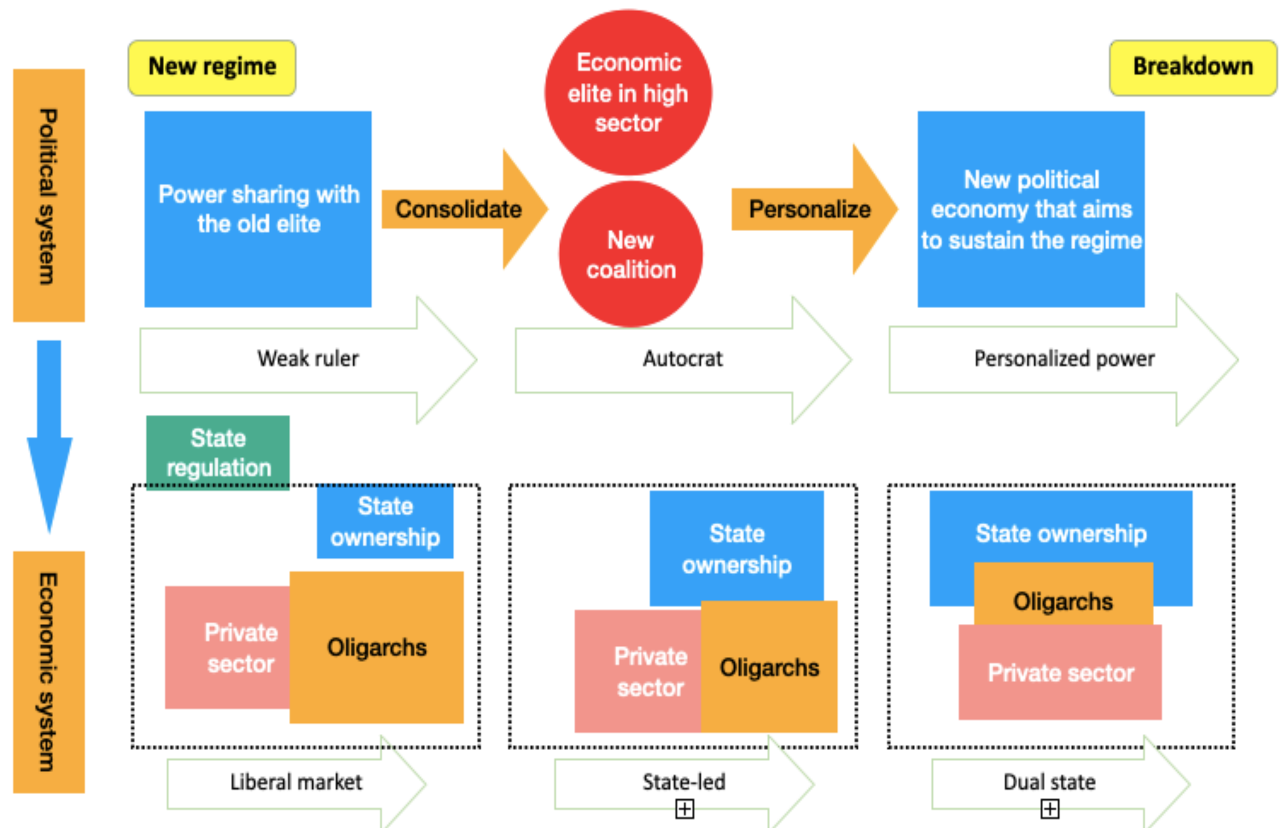
2.1 Main hypotheses: the pattern of economic decision-making and state control in personalist authoritarian regimes

To understand the rise of state control in the post-Soviet area, existing theories emphasize the personal preferences of autocratic presidents to bring developmentalism and economic modernization where the state became the principal agent.[15] However, breaking with this explanation, this dissertation invokes the discussion of *structural analysis* of authoritarian regimes to understand the political logic of economic decision-making regarding state control

[15] Anna Lowry, "Russia's Post-Neoliberal Development Strategy and High-Technology Considerations," in *Authoritarian Modernization in Russia,* edited by Vladimir Gelman, 1st Edition (London: Routledge, 2016).

and ownership in Russia and Kazakhstan. To put it differently, this dissertation argues that understanding the nature of economic decisions made by autocrats regarding state intervention and control, means replacing the *personal preferences* of autocrats with the *context of political systems* in which such decisions are made.

Figure 3. The interaction of political and economic order in personalist authoritarian regimes



Source: author's own depiction.

The political systems in Russia and Kazakhstan can be defined as *personalized authoritarian regimes*.[16] Unlike other regimes, political power in personalized power systems

[16] Rico Isaacs and Sarah Whitmore, "The Limited Agency and Life-Cycles of Personalized Dominant Parties in the Post-Soviet Space: The Cases of United Russia and Nur Otan," *Democratization* 21, no. 4 (June 7, 2014): 699–721, https://doi.org/10.1080/13510347.2013.768616; Andrea Kendall-Taylor, Erica Frantz, and Joseph Wright, "The Global Rise of Personalized Politics: It's Not Just Dictators Anymore," *The Washington Quarterly* 40, no. 1 (January 2, 2017): 7–19, https://doi.org/10.1080/0163660X.2017.1302735.

is usually concentrated in a single ruler's hand rather than in a collectively run institution.[17] The structural differences in the acquisition and exercise of power in personalist autocracies impact how autocrats make important economic decisions regarding state control and expropriations. Based on this reasoning, this dissertation argues that the rise of state control in the current economic system in Russia and Kazakhstan is inherently connected to and thus can be best explained by the nature of their personalized authoritarian regimes and the logic of power relations that play out in this regime. Linked to this argument, the dissertation hypothesizes that *the rise of state control in certain sectors of the economy (A) and subsequently emerging state-capitalist systems in Russia and Kazakhstan (B) came into being due to the irreconcilable tension between the social forces that early liberal economic reforms brought and the necessity of maintaining political survival in authoritarian regimes in these countries.* The lead hypothesis of the dissertation will be thoroughly developed as two separate yet interconnected hypotheses that constitute the theoretical framework of this dissertation.

Hypothesis (A): the rise of state control in commanding heights. The first part of the hypothesis follows the assumption that when an autocrat considers making an important economic decision that might affect the fate of the regime, he first prioritizes the *political dimension* of that decision. The defining feature of the political dimension of economic decisions in authoritarian regimes is whether it affects the autocrat's ability to maintain political power and extend his survival. Based on this reasoning, autocrats are "likely to reject outright any alternative that poses potentially very high political costs, even if that same alternative also yields potentially high benefits on other dimensions."[18]

However, the mere fact that all autocrats are concerned about their survival explains very little about how the political dimension works in economic decision making in different authoritarian regimes. Thus, it is imperative to identify and analyze the contents of the *political dimension*, that is, decision-making logics and contexts specific to personalist authoritarian regimes, and link them to certain economic outcomes. For this, the dissertation builds on the existing studies which argue that different types of authoritarian regimes present different

[17] Farid Guliyev, "Personal Rule, Neopatrimonialism, and Regime Typologies: Integrating Dahlian and Weberian Approaches to Regime Studies," *Democratization* 18, no. 3 (2011): 575–601.

[18] Alex Mintz, "How Do Leaders Make Decisions? A Poliheuristic Perspective," *Journal of Conflict Resolution* 48, no. 1 (February 1, 2004): 7, https://doi.org/10.1177/0022002703261056.

combinations of ruling coalitions, institutional arrangements, and governance strategies.[19] This is because the institutional configurations affect the incentives of political leaders. Based on this reasoning, this dissertation argues that the characteristics of economic decision making in personalist dictatorships depend not on some abstract nature of autocratic behavior or economic benefit of the decision, but on important structural factors that constitute political dimension of decisions in personalist decisions regimes. These structural factors – 1) the institutional configuration of power, 2) the nature of the regime coalition and its strategies of survival, and 3) the economic structure of the industries - produce strong motives for a dictator to pursue interventionist economic policies that favor heavy state control.

1) The personal configuration of power in personalist regimes. To understand why some personalist dictatorships, advance economic policies that favor state control over essential resources, we need to unravel the power acquisition, internal structure, and logic of power in such authoritarian regimes.[20] The idea is that the incumbent leader's decisions regarding expropriation and allocation of revenues are both *necessitated* and *facilitated* by the internal structure and logic of power specific to personalist authoritarian regimes. While a dictator's acquisition and consolidation of power require the control of resource rents in the early stage of regime, the personalization of power in a later stage *facilitates* such decisions.

First, an interesting dilemma that ensues the dictatorship in the early stage between an autocrat and the elite coalition that helped him to seize power creates an incentive for an autocrat to put control over the economic resources. As briefly described above, an aspiring personalist-autocrat in a regime faces a desire to consolidate the power at the expense of weakening the existing elite that helped him seize power.[21] And his ability to do so in the presence of weak institutions gives him an incentive to cut the ruling coalition, including the influence of existing

[19] Alejandro Bonvecchi and Emilia Simison, "Legislative Institutions and Performance in Authoritarian Regimes," *Comparative Politics* 49, no. 4 (2017): 521–39; Natasha M. Ezrow and Erica Frantz, *Dictators and Dictatorships: Understanding Authoritarian Regimes and Their Leaders* (Bloomsbury Publishing USA, 2011).
[20] Beatriz Magaloni, *Voting for Autocracy: Hegemonic Party Survival and Its Demise in Mexico*, Cambridge Studies in Comparative Politics (Cambridge: Cambridge University Press, 2006), https://doi.org/10.1017/CBO9780511510274.
[21] Michael Albertus and Victor Menaldo, "If You're Against Them You're with Us: The Effect of Expropriation on Autocratic Survival," *Comparative Political Studies* 45, no. 8 (August 1, 2012): 973–1003, https://doi.org/10.1177/0010414011428593.

oligarchs, and centralize the power by taking immediate command of all important financial and administrative resources in the state.

Furthermore, the ensuing control over the economic resources will give the dictator an upper hand over regime elites or economic powerholders who might challenge the regime. This enables him to resist pressures to create power-sharing arrangements with regime insiders that might constrain his power.[22] At the same time, complete control over economic resources grants the new autocrat with agenda-setting power regarding policy-making and distributive decisions. Access to state revenues also gives the dictator substantial control over appointments to state offices, which he can use to bring loyalists into decision-making positions and create state agencies to pursue goals not shared by the rest of the seizure group.[23] In other words, controlling the economy through expropriating assets of the former elite gives positive signaling to the new coalition members that the dictator prefers them over the former power brokers.

Easy access to economic resources also helps the dictator deal with the structural insecurity that the personalist regime faces regarding both internal and external environments. The personalist regime is susceptible to such external factors as sanctions and global financial turbulence – these resources increase his ability to deal with them. Party-based or military regime types typically counter these challenges through elite cohesion and institutions. At the same time, the oppositional forces in these regimes have the power to prevent the elite from instituting total control over the entire economy. However, in a personalist regime, the threat is so dire that it gives the dictator an incentive to act rather harshly in controlling the economic means.

The arbitrary and interventionist nature of economic policies, including sudden expropriation, is further amplified by the internal structure of personalist regimes after consolidation of powers. Comparative regimes research has long confirmed that autocrats' decision-making is strongly influenced by whether they rule mainly at their discretion or face institutional constraints to their rule, or *veto players*, from a powerful party or military.[24] As

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[22] Matthew D. Fails, "Oil Income and the Personalization of Autocratic Politics," *Political Science Research and Methods* 8, no. 4 (October 2020): 772–79, https://doi.org/10.1017/psrm.2019.14.
[23] Barbara Geddes, Joseph Wright, and Erica Frantz, *How Dictatorships Work: Power, Personalization, and Collapse* (Cambridge University Press, 2018), 74–76.
[24] Jessica L. Weeks, "Strongmen and Straw Men: Authoritarian Regimes and the Initiation of International Conflict," *American Political Science Review* 106, no. 2 (May 2012): 326–47, https://doi.org/10.1017/S0003055412000111.w

mentioned above, personalist dictatorships, unlike party-based or military regimes, enjoy highly centralized governance in which a single veto player (as opposed to multiple veto players with the same standing in party or military regimes) has enormous power concentrated at hand.[25] Geddes argues that the institutional feature that distinguishes personalist regimes from others is that "although personalist regimes have parties and militaries, these organizations have not become sufficiently developed or autonomous to prevent the leader from taking personal control of policy decisions and selection of regime personnel."[26] This will grant him complete control, ad hoc discretion, and flexibility over economic decisions like intervention, expropriation, and allocation that he deploys to extend his political survival.

In the face of an autocrat's dominance over state structures and the absence of power-sharing arrangements, institutions like parties or the military can exercise very little independent power. They cannot exert decisional constraints on the dictator. The same is true for societal opposition: the personalist regime is an infertile land for resistance to emerge and challenge the regime. Some coalitions, including regime insiders and economic oligarchs, tend to show signs of conflicting interests. However, they lack coordination mechanisms that constrain their ability to claim their share of rents in the economy. Succinctly stated, the lack of decisional constraints and institutionalized opposition in a personal dictatorship can allow the dictator to pursue arbitrary economic policies for the sake of survival for several reasons. First, neither the elite nor the mass populace in personalist regimes has institutionalized mechanisms and channels to either influence the policy choice or punish the dictator in case of policy failure. Second, elites in personalist regimes tend to be very much dependent on the personal autocrat and become sycophants "who tell the leader what he wants to hear, which suggest that personalist regimes may be the least likely to calculate the consequences of the policy."[27] Due to the characteristics of weak coalitions, the personalist regimes do not need to have "the formal governing coalitions between organized state and social interests or the collective bargaining over core public policies that characterize corporatism."[28] In short, the environment of weak institutional

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[25] Simon Hug and George Tsebelis, "Veto Players and Referendums Around the World," *Journal of Theoretical Politics* 14, no. 4 (2002).
[26] *Paradigms and Sandcastles*, 53, accessed May 9, 2018, https://www.press.umich.edu/11907.
[27] Mark Peceny and Caroline C. Beer, "Peaceful Parties and Puzzling Personalists," *American Political Science Review* 97, no. 2 (May 2003): 340, https://doi.org/10.1017/S0003055403000716.
[28] Michael Bratton and Nicholas van de Walle, *Democratic Experiments in Africa: Regime Transitions in Comparative Perspective* (Cambridge University Press, 1997), 65.

constraints provides an autocrat with "opportunities for personal enrichment and power that are unavailable to leaders in other political systems" through arbitrary expropriations and interventionist economic policies.[29]

In contrast, in regimes with coherent party institutions or military structures, term limits or regularized turnover of rulers and consultative councils usually direct the course that economic policies take. The rules that govern the decision making in these regimes are based on the logic that "an institutional division of decision-making power helps reduce the risk of arbitrary policy action."[30] Here, the veto player is collective leadership organized around an institution rather than a single individual whose consent is required to make decisions. Unlike unrestrained power in personalist regimes, the policy on the economic resources in party-based and military regimes will either be constrained by considerations of maintaining party supremacy or corporate coherence. Also, the power-sharing arrangement organized around the party or military structures can credibly deliver a threat of collective action and act as a constraining power over the ruler's policy discretion. Due to the constraining power of the elite, the dictator in a non-personalist regime is obliged to create a binding institution that curbs his ability to expropriate and guarantee investment stability.

In sum, these nuances in rules governing decision-making in personalist authoritarian regimes can have important implications for economic policymaking on the access to oil rents and their allocation. Due to the lack of institutional oversight, decisional constraints, and centralization of power, policymaking will be extremely discretionary, giving the autocrat a better opportunity to expropriate economic resources and keep them under his private control.

2) The nature of the ruling coalition and strategies of regime survival. The decision to maximize discretionary power over economic resources may come because of the ruler's strategy to retain power in the face of insecurity.[31] As mentioned above, the important point to acknowledge is the ultimate priority of authoritarian regimes, regardless of their types, to maintain power and eliminate all the threats that put its monopoly on power in jeopardy. The

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[29] Weeks, "Strongmen and Straw Men."
[30] Andrew MacIntyre, *The Power of Institutions: Political Architecture and Governance* (Cornell University Press, 2018), 21.
[31] Scott Gehlbach and Philip Keefer, "Investment without Democracy: Ruling-Party Institutionalization and Credible Commitment in Autocracies," *Journal of Comparative Economics* 39, no. 2 (June 1, 2011): 123–39, https://doi.org/10.1016/j.jce.2011.04.002.

strategies for containing these threats shape dictator's economic decisions concerning rent expropriation and its allocation. These threats usually come from two sources; the problem of authoritarian control, the one that comes from a broad mass over which the autocrat rules, and second is the problem of authoritarian power-sharing, the problem that stems from the elite with whom the autocrat controls the mass.

In general, the dictator has two strategies to manage these threats: loyalty/support through cooptation and patronage and repression through coercive means.[32] The dictator's strategy for survival against the threat depends on the size of the support group that the ruler relies on.[33] In Bueno de Mesquita et al.'s (2003) model, the personalist dictatorships are interested in having a small winning coalition and larger selectorate than other regime types because doing so helps the dictator manage a small number of elites to accumulate much larger stockpiles of resources for survival.[34] So, the scholarly consensus maintains that to secure the loyalty of a small elite circle while deterring the possible threats they pose, autocratic leaders pursue patron-clientelist policies that emphasize sufficient benefit to winning coalition so that they stay supportive of the incumbent and do not defect.[35] The same is true for the selectorate or the general populace, to whom the regime needs to deliver the provision of selective public goods from time to time to manage their desires.

The fact that personalist dictators are induced to choose strategies of survival that emphasize doling out patronage to both winning coalition and the selectorate through the combination of both private and public goods "provide incentives for the ruler to implement highly interventionist economic policies aimed at extracting rents."[36] In turn, the state allocation

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[32] Ronald Wintrobe, *The Political Economy of Dictatorship* (Cambridge University Press, 2000), 20–30; Jennifer Gandhi and Adam Przeworski, "Cooperation, Cooptation, and Rebellion under Dictatorships," *Economics & Politics* 18, no. 1 (2006): 1–26.
[33] Mark Peceny and Christopher K Butler, "The Conflict Behavior of Authoritarian Regimes," *International Politics* 41, no. 4 (December 1, 2004): 565–81, https://doi.org/10.1057/palgrave.ip.8800093.
[34] Bruce Bueno De Mesquita et al., "Policy Failure and Political Survival: The Contribution of Political Institutions," *Journal of Conflict Resolution* 43, no. 2 (April 1, 1999): 147–61, https://doi.org/10.1177/0022002799043002002.
[35] Joseph Wright and Abel Escribà-Folch, "Authoritarian Institutions and Regime Survival: Transitions to Democracy and Subsequent Autocracy," *British Journal of Political Science* 42 (April 1, 2012): 283–309, https://doi.org/10.1017/S0007123411000317.
[36] Abel Escribà-Folch, "Repression, Political Threats, and Survival under Autocracy," *International Political Science Review* 34, no. 5 (November 1, 2013): 543–60, https://doi.org/10.1177/0192512113488259.

of resources through interventionist policies promotes “the consolidation of weak and loosely integrated regimes, create social bases of support for those regimes, penalize and marginalize opponents of the status quo, and give regimes some claim to legitimacy.”[37] In other words, regime’s decision to allocate state resources in the form of private and public goods through state patronage is “inseparable from and shaped by broader strategies of domestic political consolidation and control”: it is an essential component of a *system of political control*.[38] The evidence attests to this claim; “the rate of government consumption as a share of DGP (a proxy for patronage distribution) are higher in personalist dictatorship than in other forms of authoritarianism.”[39] We can observe the specific ways in which the regime promotes decisions regarding state intervention and resource allocation through the clientelistic practices of the following actors whose support the dictator needs.

The regime elite - securing loyalty and preventing defections. The important group that influences the direction of the economic arrangement in personal dictatorship is the regime insiders with whom an autocrat runs the country. Even though the regime elite stays loyal to the autocrat, they possess a potential seed of destruction to the regime through defection if the autocrat fails to manage the distribution of spoils and economic rents.[40] In other words, as Brough and Kimenyi emphasized, “to keep the coalition intact, the dictator must distribute benefits to the coalition.”[41] Here, the dictators utilize patron-client networks for the distribution of rents and benefits, in which the patron provides material rewards to the clients in return for political support. However, such clientelistic practices act as a system of political control for the dictator in the regime. Regulating access to state resources on an *ad hoc* basis, patron-client relations assist the dictator in alleviating the threat and securing the loyalty of the elite.[42]

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[37] Catherine Boone, “The Making of a Rentier Class: Wealth Accumulation and Political Control in Senegal,” *The Journal of Development Studies* 26, no. 3 (April 1, 1990): 428, https://doi.org/10.1080/00220389008422163.
[38] Boone, “The Making of a Rentier Class.”
[39] Erica Frantz et al., “Personalization of Power and Repression in Dictatorships,” *The Journal of Politics*, December 10, 2019, https://doi.org/10.1086/706049.
[40] Ora John Reuter and David Szakonyi, “Elite Defection under Autocracy: Evidence from Russia,” *American Political Science Review* 113, no. 2 (May 2019): 552–68, https://doi.org/10.1017/S0003055419000030.
[41] Wayne T. Brough and Mwangi S. Kimenyi, “On the Inefficient Extraction of Rents by Dictators,” *Public Choice* 48, no. 1 (1986): 46.
[42] Gandhi and Przeworski, “Cooperation, Cooptation, and Rebellion under Dictatorships.”

The appropriation of rents can usually be generated by extensive state intervention in the markets. State-controlled markets, state monopolies, market regulations, and delegating control over state-owned enterprises (SOEs) in key industries constitute the key patronage goods that the dictator uses to reward the loyal supporters.[43] Access to such spoils and rents from the control of those companies co-opts the elite, induces a strong norm of loyalty to the incumbent leader, and ensures his stability.[44] The dictator's cronies and family members, under his auspices, usually run the public funds freely and establish profit-oriented state monopolies and SOEs. For instance, dictatorships in Latin America throughout the 1930s and 1980s adopted the practice of "military entrepreneurship" through ownership, management, or stockholding of economic enterprises.[45] The use of state power regarding the decision of intervention and allocation of economic resources creates a political class in personalist regimes. Dominant actors who derive their power stem from access to state resources and involvement in rentier activities.

Apart from maintaining the dominance of the ruling class vis-a-vis the independent capitalist class and their political cohesion, patron-client relations also serve the reciprocal interests of both individual elite and dictator. For the elite, exercising control over state monopolies and SOEs in key economic resources provides an area of turf for personal enrichment, enabling them to cultivate their patronage networks to increase their influence in the policy-making process. For a dictator, the appointment of a small elite to SOEs in important sectors provides a *channel* to monitor the activities of the elite and contain their ambitions when necessary.[46] In short, the exercise of political power and its stability in a personalist regime rests on the selective allocation of state resources to the regime elite in various forms. This creates a powerful incentive for a dictator to bring an extensive regulation of economic activity "through

[43] Robert Bates, *Markets and States in Tropical Africa* (University of California Press, 2014).
[44] Alexander Baturo and Johan A. Elkink, "Dynamics of Regime Personalization and Patron–Client Networks in Russia, 1999–2014," *Post-Soviet Affairs* 32, no. 1 (January 2, 2016): 75–98, https://doi.org/10.1080/1060586X.2015.1032532.
[45] Kristina Mani, "Militares Empresarios: Approaches to Studying the Military as an Economic Actor," *Bulletin of Latin American Research* 30, no. 2 (2011): 183–97, https://doi.org/10.1111/j.1470-9856.2010.00445.x.
[46] Anders Aslund, *Russia's Crony Capitalism* (New Haven: Yale University Press, 2019).

which the incumbent elite gained control over a wide range of monopolies and economic rents."[47]

The people - managing the popular desire and countering the rebellion. Along with the regime elite, the need to manage desires and garner public support gives a dictator certain incentive to promote state interventionist policies in the economy. Although regime comparativists argue that the people may threaten rebellion against all types of autocracies, the magnitude of that threat varies in different regime types.[48] In a personalist regime, the risk is higher as the people have fewer resources in representation in the policy. This is backed by empirical evidence showing that personalist regimes usually break down in the face of popular uprisings.[49] Thus, to secure the people's legitimate support, the regime relies on "authoritarian bargaining": buying-off certain constituents of the population through the allocation of public goods, economic transfers, and manipulating redistributive policies concerning inequality.

However, for redistributive policies (subsidies, price controls, welfare benefits, employment, and public projects) to effectively fend off the popular rebellion, the autocrats need to establish a stable stream of economic rents and revenue to state coffers. Such redistributive transfers are usually channeled through state-controlled companies in natural resource-rich countries. Another reason for an autocrat's yearning for control over economic resources is his concern with the economic performance upon which the "pact" between the regime and people is built. Bad economic performance by sudden recession, inflation, or currency collapse may deny the regime important resources needed to maintain the population's support, destroying the pact, and leaving the regime vulnerable to defection.[50] This gives the dictator an utmost incentive to control the strategic sectors and hence the fate of the economic performance. In short, it is fair to assume that such an analysis of dictators' bargaining "implies

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[47] Bratton and Walle, *Democratic Experiments in Africa*, 66.
[48] Ezrow and Frantz, *Dictators and Dictatorships*.
[49] Barbara Geddes, Joseph Wright, and Erica Frantz, "Autocratic Breakdown and Regime Transitions: A New Data Set," *Perspectives on Politics* 12, no. 2 (June 2014): 313–31, https://doi.org/10.1017/S1537592714000851.
[50] Valerie J. Bunce and Sharon L. Wolchik, *Defeating Authoritarian Leaders in Postcommunist Countries* (Cambridge University Press, 2011), 49.

a link between redistributive policies and political control and tradeoffs between the two in explaining autocratic decision-making."[51]

The oligarchs - curbing independent economic power and co-opting to the statist economic order. Another important group that dictator takes into consideration when making economic decisions is the *oligarchs*, the existing capitalist class, who can potentially pose a real threat to the regime. This is mostly because "autocrats and would-be autocrats encountered resistance to their pretensions among those engaged in commerce" because free business activity independent of the regime tends to subvert autocracy and encourage political self-rule.[52] Also, the capitalist class is usually a potential source of opposition to the power and the demand for open politics. They tend to translate their autonomous economic power into a political one, as many historical accounts demonstrate.[53] Yet, such a vital force can present itself as beneficial for regime stability: the dictator can tap into the "entrepreneurial spirit" of the capitalist class to generate rents efficiently and channel the outcome of such spirit into contributing to the cause of regime stability.[54] In other words, it is sometimes in dictators' interest not to destroy the existing capitalist class, but rather accept them as "junior partners" who receive important properties as "concessionary" property from the regime to stay loyal and committed to its causes.[55] A critical aspect of such cooperation is the dictator's rent maximization effort. Another one is that oligarchic businesses can help the regime achieve economic growth, modernization, and social policies, which is crucial for maintaining performance legitimacy and social stability. In return for their contribution to the regime causes, the oligarchs can also benefit from the state's interventionist policies, such as protectionist measures and subsidized credits.[56]

However, such a state-business alliance does not always prove benign; oligarchs might develop some degree of autonomy and sufficient financial capacity to challenge the regime.

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[51] Raj M. Desai, Anders Olofsgård, and Tarik M. Yousef, "The Logic of Authoritarian Bargains," *Economics & Politics* 21, no. 1 (2009): 6, https://doi.org/10.1111/j.1468-0343.2008.00337.x.
[52] M. Steven Fish, *Democracy Derailed in Russia: The Failure of Open Politics* (Cambridge University Press, 2005), 157.
[53] Charles Tilly, *Coercion, Capital, and European States: AD 990 - 1992* (Wiley, 1993).
[54] Gandhi and Przeworski, "Cooperation, Cooptation, and Rebellion under Dictatorships."
[55] Gerald M. Easter, *Capital, Coercion, and Postcommunist States* (Ithaca, NY: Cornell University Press, 2012).
[56] Hootan Shambayati, "The Rentier State, Interest Groups, and the Paradox of Autonomy: State and Business in Turkey and Iran," *Comparative Politics* 26, no. 3 (1994): 307–31, https://doi.org/10.2307/422114.

Therefore, the dictator makes sure that "junior partners" are subject to stringent state control through ready-made instruments designed to prevent state capture. One of those instruments that enable the regime to have a higher bargaining power vis-a-vis business is the state's direct control over capital through market regulation, domestic credit, outright ownership, and financial autonomy. The state's autonomy and direct control over capital are usually higher in countries with *rentier* economies where the external rents from natural resources free the state from being dependent on the cooperation of domestic businesses to generate a surplus.[57] Control of capital and financial autonomy also helps the dictator dampen the corporate influence that the capitalist class might exert and undercut their ability to organize politically and challenge the regime. Another instrument is selective punishment through the expropriation of assets that an autocrat can deliver if an oligarch sticks his neck out too far. Kang describes this asymmetrical style of state-business relations as top-down predation in which regimes "take advantage of a dispersed and weak business sector…pursue outright expropriation…solicit "donations" from a businessman who in turn are either "shaken down" by the regime or who volunteer bribes in return for favors and employ other means as well."[58]

In short, although the property-owning oligarchs in personalist regimes are allowed space to operate in key sectors, they are under political surveillance and coerced to embed themselves in the structure of "authoritarian capitalism," giving unconditional loyalty to the dictator. This is based on the understanding that when they try to avoid being not accountable to the ruler's network or help establish his economic clout, they make themselves the enemy of the regime and a possible threat to the system who may be targeted for possible elimination. Thus, oligarchic business groups in personalist regimes with capital control do not represent any independent power capable of exerting corporatist demands but instead act as a collaborating actor to the "rentier class" of the regime that helps sustain its statist economic order.

3) The nature of the predominant economic sector. The leader's policy preferences regarding the intervention and control can also stem from the nature of the predominant

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[57] Kiren Aziz Chaudhry, "Economic Liberalization and the Lineages of the Rentier State," *Comparative Politics* 27, no. 1 (1994): 1–25, https://doi.org/10.2307/422215.
[58] David C. Kang, *Crony Capitalism: Corruption and Development in South Korea and the Philippines*, Cambridge Studies in Comparative Politics (Cambridge: Cambridge University Press, 2002), 16, https://doi.org/10.1017/CBO9780511606175.

economic sector that structures the country's political economy.[59] Scholars argue whether the wealth comes such "unearned" income as oil rents, minerals extractions and foreign aid or a productive economy.[60] As Shafer claims, "different sectors generate different resources and distribute them in distinctive, politically salient ways…generate different patterns of societal actors with sectorally determined interests, resources, and capacities for collective action."[61] Therefore, the politics of state ownership in post-Soviet personalist regimes can be shaped by the sectoral characteristics of hydrocarbon sectors in Russia and Kazakhstan and much of their heavy manufacturing.

If so, this begs the question of the implications of those specific *sectors* for regime survival. My hypothesis regarding the sectoral analysis builds on the work of Shafer, who defines a sector as "a type of economic activity" (extractive industries like mining and hydrocarbon, production, and agriculture) whose constitution can be explained by a distinctive combination of four core variables: capital intensity, the extent of economies of scale, production flexibility and asset flexibility. Based on these factors, we can construct two ideal sectors with each on the different poles: *high sector* and *low sector*.

Industrial production in high sectors in economies like Russia and Kazakhstan is very capital intensive and characterized by a high degree of asset specificity and economies of scale.[62] This means that companies in these high sectors tend to be geographically concentrated and more specialized in their production technology, facility, and infrastructure. Also, these sectors tend to feature a high barrier to entry and exit and limited competition with a small number of large companies that ready the ground for oligopolies. In the extractive industry of many personalist regimes, high sectors are best epitomized by the oil and gas sectors. By

[59] Professor Daron Acemoglu, Daron Acemoglu, and James A. Robinson, *Economic Origins of Dictatorship and Democracy* (Cambridge University Press, 2006).
[60] Kevin M. Morrison, "Oil, Nontax Revenue, and the Redistributional Foundations of Regime Stability," *International Organization* 63, no. 1 (January 2009): 107–38, https://doi.org/10.1017/S0020818309090043; Terry Lynn Karl, *The Paradox of Plenty*, *The Paradox of Plenty* (University of California Press, 1997), https://www.degruyter.com/document/doi/10.1525/9780520918696/html.
[61] D. Michael Shafer, *Winners and Losers: How Sectors Shape the Developmental Prospects of States*, Cornell Studies in Political Economy (Ithaca, NY: Cornell University Press, 1994), 5.
[62] William Tompson, "Back to the Future? Thoughts on the Political Economy of Expanding State Ownership in Russia," in *Institutions, Ideas and Leadership in Russian Politics*, ed. Julie Newton and William Tompson, St Antony's Series (London: Palgrave Macmillan UK, 2010), 67–87, https://doi.org/10.1057/9780230282940_4.

contrast, low production sectors have very low capital intensity and economies of scale. Many small-size firms in low sectors do not require specific assets and capital and are subject to a high market competition where there is no barrier to entry and exit.

What do these specific features of sectors tell us about the dictator's propensity to control them? First, high sectors yield monopoly rents that the regimes can easily tap into in order to provide a "material underpinning" for its stability. The hydrocarbon, oil, and gas sector are a typical example of the high sector that scholars associate with an endurance of authoritarian regimes and a personalization of power.[63] With state coffers full following the oil bonanza, personalist authoritarian regimes have the financial capacity to deal with the potential threats from regime insiders and the general public by distributing more rents in employment, lucrative contracts, and business subsidies on low-priced fuels. At the same time, the negative performance of the hydrocarbon sector, when the boom is over and the bust comes, might put the regime in economic jeopardy, too, since this sector tends to dominate the state's main revenue stream and export earnings.

Another reason for the regime's distaste regarding private ownership in high sectors is concerned with the fear of the economic power and influence that high sectors tend to present to oligarchs. Their massive size and asset specificity put them in a demanding position vis-a-vis state through which "they are likely to attempt to influence government policy… wield political influence."[64] Due to their small number, collective action is less of a problem for their ability to organize. Thus, in the case of a weak regulatory, institutional environment, personalist regimes find the fear of exploitation and capture by those private owners very threatening to their policy autonomy and flexibility.[65] Also, the sectoral competition and conflicts that may arise among them could destabilize the regime, as the "kompromat wars" in Russia among oligarchs demonstrated during wild capitalism. In the face of private and foreign ownership concerns, state ownership becomes the only feasible option.[66]

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[63] Fails, "Oil Income and the Personalization of Autocratic Politics."
[64] Kang, *Crony Capitalism*, 13.
[65] Philip Hanson, "The Russian Economic Puzzle: Going Forwards, Backwards or Sideways?" *International Affairs* 83, no. 5 (September 1, 2007): 869–89, https://doi.org/10.1111/j.1468-2346.2007.00660.x.
[66] KIREN AZIZ CHAUDHRY, "The Myths of the Market and the Common History of Late Developers," *Politics & Society* 21, no. 3 (September 1, 1993): 245–74, https://doi.org/10.1177/0032329293021003002.

In sum, the structure of specific sectors in personalist regimes affects the dictator's decision regarding ownership. High sectors increase his preference to bring heavier control in the form of state ownership. At the same time, the dominance of high sectors discourages the dictator from adopting an institutional environment that requires cooperation with domestic business to generate a domestic surplus. As Wright puts it, personalist regimes, compared to other regime types, "do not have the same incentive to establish binding legislatures because they are more dependent on sources of "unearned" income such as natural resource rents and foreign aid and less dependent on investment in the productive economy."[67]

Hypothesis (B): the emergence of state capitalism as political-economic order. It is fair to argue that economic decisions are subjected to political calculations in personalist regimes based on the previous discussion. As mentioned, several structural factors peculiar to personalist regimes bring a new *political order* that shapes autocrats' decision making with matters like resource expropriation and allocation. A political order that aims to maintain state control over certain sectors while allowing some economic progress provides a building block for the distinctive *economic order* in these regimes. An economic order with a two-tier objective is defined and controlled by political organization in personalist regimes and can be characterized as dictatorial *state capitalism* with a dualistic character. In such political-economic order, the state asserts its right to oversee the strategic *state sectors* of *the* economy through prerogative interference and ownership. At the same time, a bulk of private businesses operate in the *market sector*.

A dualistic economy involves two favored sectors based on two factors: 1) the importance of the sectors to the regime in terms of material and social benefit and 2) the level of threat that they pose to the regime. This distinction then assumes that each sector in a dualistic economy produces different rules and is subject to varying modes of decision-making.[68] A useful analogy can be found in numerous works regarding political decision-making in Russia.[69] The concept of a dual economy is seen as a useful description of production and business organization

[67] Joseph Wright, "Do Authoritarian Institutions Constrain? How Legislatures Affect Economic Growth and Investment," *American Journal of Political Science* 52, no. 2 (2008): 323, https://doi.org/10.1111/j.1540-5907.2008.00315.x.
[68] Hanson, "The Russian Economic Puzzle."
[69] Richard Sakwa, "The Dual State in Russia," *Post-Soviet Affairs* 26, no. 3 (July 1, 2010): 185–206, https://doi.org/10.2747/1060-586X.26.3.185.

aspects that existed in several developing countries. Almost all proponents of the dual-economy concept seem to find an asymmetry in two separate sectors within one country.

The state sector comprises important industries such as oil, gas, and heavy industries that lie in the *economy's core* and are "strategically" important to the regime due to the revenue, export earnings, and employment they provide.[70] Such sectors are subject to the control of the regime. The prevailing rule for this sector is not market; the political calculations of the leader rather than economic efficiency dictate the decision-making and the rationale behind commercial operations of state-controlled companies in state sectors and their interaction with private business. Limited access to some strategic and nonstrategic sectors might be granted to private business on the basis of loyalty to the regime. In the post-Soviet terrain, such a private sector that lies in the vicinity of the state sector constitutes a corrupt *oligarchic* business, which the case studies will explore more deeply. The private sector's operation in such sectors is supposed to benefit the stability of the regime and by no means compromise the interests of the regime. However, some of these sectors are still subject to weak property rights and the prerogative interferences of the state.[71] To advance and protect their interest, the businesspeople in or around the state sector attempt to establish close ties with the high-ranking officials, the autocrat himself, or the ruling family. In other words, "linkage to the state and to the government bureaucracy, rather than to the market, was the main source of accumulation."[72]

The most important tools that regimes employ in the state sector include "national oil (and gas) corporations (NOCs), other state-owned enterprises (SOEs), privately owned national champions, and sovereign wealth funds (SWFs)."[73] Refraining from daily control, governments use direct or indirect tools and measures to manage strategic sectors of the economy. They also take advantage of capitalist institutions such as stock markets and embrace globalization as long as it serves vested politico-economic interests.

The market sector, or *periphery* economy, by contrast, is made of private businesses in the economy second-tier sectors of the economy such as manufacturing, construction, or retail

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[70] Martin C. Spechler, Joachim Ahrens, and Herman Willem Hoen, *State Capitalism in Eurasia* (London: World Scientific, 2017), 55.
[71] Richard Sakwa, *The Quality of Freedom: Putin, Khodorkovsky, and the Yukos Affair* (Oxford: Oxford University Press, 2009), https://kar.kent.ac.uk/24621/
[72] Shambayati, "The Rentier State, Interest Groups, and the Paradox of Autonomy," 321.
[73] Ian Bremmer, *The End of the Free Market: Who Wins the War between States and Corporations?* (United States: Penguin Publishing Group, 2010), 54.

that has free barriers for entry to almost anyone. However, the proximity to the governing elite gives some privilege in their functioning.[74] A group of business owners in the market sector can function in a bazaar economy, where entrepreneurs are identified "not so much by the kind of business they engage in as by the way they do business." Some of these business owners are petty capitalists who are regulated by local market forces; that is, "strong competition and prices, rather than personal ties, become the key coordination mechanism and incentives."[75]

The business activities in *the bazaar economy do not involve strict state intervention, unlike th*e state sector. Except for matters like taxation, political considerations do not prevail in the periphery provided that they do not cross a certain political threshold. In that sense, they can maintain their economic positions and keep their economic resources out of state control. This will give them a certain level of financial independence and the formation of their organization. Sometimes, as was the case in Iran during the late 1970s, the state can't tap into the immense wealth accumulated in the bazaar economy because of the deficiencies of the extractive apparatus due to the oil rent. In other cases, the regime considers the financial autonomy businesses enjoy in the market sector to be a deliberate co-optation strategy directed against the people's power. An infamous color revolution in Kyrgyzstan organized by wealthy businessmen in the bazaar economy in 2005 can epitomize the immense cost that the regimes might incur when they become reckless in harassing the business owners.[76]

Overall, the dualistic mode of state capitalist economy, which characterizes the economic order prevalent in many personalist regimes, includes the following traits:

- The complete dominance of the state over so-called strategic sectors of the economy, such as oil, gas, and minerals
- Political calculations rather than economic efficiency dictate the rationale behind the commercial operations of the state in these or other related sectors and its interaction with private business

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[74] Neil Robinson, "Economic and Political Hybridity: Patrimonial Capitalism in the Post-Soviet Sphere," *Journal of Eurasian Studies* 4, no. 2 (July 1, 2013): 136–45, https://doi.org/10.1016/j.euras.2013.03.003.
[75] Shambayati, "The Rentier State, Interest Groups, and the Paradox of Autonomy," 322.
[76] Scott B. Radnitz, *Weapons of the Wealthy: Predatory Regimes and Elite-Led Protests in Central Asia, Weapons of the Wealthy* (Cornell University Press, 2012), 103–30, https://null/view/title/527329.

- Limited access to some strategic and non-strategic sectors might be granted to the private businesses on the condition of loyalty to the regime
- However, some of these sectors are still subject to prerogative interference by the state
- Yet, second-tier sectors of the economy, such as manufacturing, construction, or retail, are open for the entry of private business, although the proximity to the governing elite gives some privilege in their functioning
- However, the increased role of the state coexists with the commitment to liberal economic principles and does not inhibit other reforms ongoing in different spheres, especially in finance.

The figure below provides a simplistic view of how the political and economic order emerges in personalist authoritarian regimes.

In conclusion, this section aims to provide an answer to the question of why the autocrats feel compelled to increase the state control vis-a-vis the private business. Through the framework discussed, it becomes clear that the first and foremost reason is the autocrat's need to consolidate and maintain power in the face of potential challenges. To achieve this goal, regime elites ensure that they have access to a stable revenue source, whose distribution the leader can then maintain the support of his patronage and manage the popular desires. An equally important priority is to get necessary cooperation with, but also unconditional loyalty from, the property-owning class to prevent the emergence of any independent power base with the substantial financial resource. The establishment of this equidistance might sometimes require the forceful redistribution of their property through different means of acquisition, as the case studies demonstrate. The framework also indicates that such a personalized regime breeds a typical economic order, a state capitalist economy that hosts two distinct actors.

2.2 The existing views on the political economy of capitalism in contemporary Russia and Kazakhstan

For the scholars in the first strand, understanding the political economies in contemporary Russia and Kazakhstan can hardly make sense without analysis of informal arrangements ubiquitous in the state system. Yet for other scholars, the nature of economic structures, especially a huge natural resource endowment and the way wealth is created and distributed, are important determinants in shaping Russia and Kazakhstan's political and economic

institutions. Given the sheer size of the hydrocarbon sector in the economy, with oil and gas together constituting 25% of the GDP and 50% of government revenue in 2008, scholars demonstrate that Russia under Putin has become a carbon-based political economy, dubbed a *petrostate* or *petronation,* awash with petrodollars which facilitated Putin's ambition to regain global superpower status and consolidate authoritarian power at home.[77] As for Kazakhstan scholars have also long recognized the importance of oil as the blood in the political and economic life in the country due to the wealth it generates.[78] The regime's trajectory in the wake of independence and its subsequent consolidation under the fist of President Nazarbayev is hence intrinsically linked to economic development in which hydrocarbon reserves played a substantial role.[79]

Table 4. Existing debates on the rise of state control in Russia and Kazakhstan

An argument	The state control	The reasoning
1. Strong state, strong economy	A way to maintain stable economic activity	A strong state is to stabilize the economy by bringing order and protecting the property
2. Economic development through *etatization*	A way to facilitate the economic modernization through active industrial policy	A strong state is an active agent of economic modernization in the global economy
3. State as a domain for factional struggle	A domain for acquiring personal wealth	State and the wealth that comes from it are subject to the internal fighting by various elite groups

Over the years, scholars attempted to present an account of political economies in post-Soviet Russia and Kazakhstan under the framework of varieties of capitalism. Yet such undertaking led to the contention that murky ways of state involvement in the economies of post-Soviet countries defy a simple "liberal vs. coordinated" dichotomy of market capitalism

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[77] Peter Rutland, "Petronation? Oil, Gas, and National Identity in Russia," *Post-Soviet Affairs* 31, no. 1 (January 2, 2015): 66–89; Marshall I. Goldman, *Petrostate: Putin, Power, and the New Russia* (Oxford University Press, 2008).
[78] Wojciech Ostrowski, *Politics and Oil in Kazakhstan* (London: Routledge, 2009).
[79] Martha Brill Olcott, *Kazakhstan: Unfulfilled Promise* (Carnegie Endowment, 2010): 130.

and necessitates bringing political factors into the equation.[80] As a result, diverse literature emerged dedicated to the formation of post-Soviet political and economic order in Russia and Kazakhstan, which is fraught with such catchy depictions as *kleptocratic or crony capitalism, petrostate/rentier state,* and different manifestations of *political capitalism*.

Skeptical of the politically charged nature of these descriptions, scholars observe that the recent rise of state intervention in economic management and ownership brought a new political-economic order in contemporary Russia and Kazakhstan, dubbed s*tate capitalism*, that deserves special scrutiny. In transforming from "chaotic capitalism" to state-led capitalism, states became the main player in the economy for the ongoing struggle for property and manage a significant production means, controlling strategic industries and subordinating the private business to its will.[81] As a result, a successfully functioning market economy in Russia would go down the path of state capitalism or state corporatism under Putin's rule to the extent that the nationalization of the means of production was the only distinction that separated Russia from the Soviet economy. In the case of Kazakhstan, Spechler argues that the current political and economic order under Nazarbayev's rule features state capitalism in dual-track form, in which "a state-driven, modern, and export-oriented core sector …coexists with a smaller, usually less advanced private sector".[82]

Such analyses regarding the comeback of state control following initial attempts at liberalization beg an interesting question that has intrigued a sizeable group of scholars: why were political leaders suddenly motivated to increase state intervention and control in key sectors of the economy after first driving towards liberalization? Answering this quandary requires going beyond simple explanations of the nature of statist political economies in these countries and elucidating the reasons behind the question. Scholars who presented diverging views regarding the reasons behind the rise of state control can be categorized into three groups: 1) presidents' statist preference to maintain order and economic stability, 2) economic nationalism or states as an agent of economic development and modernization, and 3) states as

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[80] David Lane, "From Chaotic to State-Led Capitalism," *New Political Economy* 13, no. 2 (June 1, 2008): 177–84

[81] Andrew Scott Barnes, *Owning Russia: The Struggle Over Factories, Farms, and Power* (Cornell University Press, 2006).

[82] Spechler, Ahrens, and Hoen, *State Capitalism in Eurasia*, 8.

a domain to reign for different factions fighting with each other. The summary of arguments is given in figure 3 above.

A strong state, a strong economy. In the first strand, scholars maintain that the necessity of bringing the state control over the economy is closely associated with the longing of both President Putin and Nazarbayev to build a strong and capable state that could maintain domestic order and bring macroeconomic stability and balance state-business relations.[83] This makes perfect sense in the case of Russia in the "damned 1990s," where an unsighted neoliberal project of creating markets without solid institutional support was marked by the dismantling of the central authority, collapse of the state's fiscal capacity, and corruption of political society.[84] These economic reforms bred a group of oligarchs at the federal level, who successfully penetrated in the corridors of power through clientelist ties and captured the state, privatizing its functions to the extent that the national markets were discreetly carved up among them.[85] All these ailments piled up over the years, culminating in the financial crisis in 1998 that left the Russian economy in ruins.

Against this backdrop Putin's palpable response right after coming to power was to re-design orderly capitalism through refurbished Moscow Consensus that entailed bringing back "*the visible hand*," a strong state, in charge of fixing the botched transition so that it could enforce the rules of the game for a market economy, creating the necessary condition for economic development through the rule of law, property rights, tax system, and corporate governance.[86] Such a dire need for a stronger state found nationalistic and liberal spectrum in the country.[87]

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[83] Chris Miller, *Putinomics: Power and Money in Resurgent Russia* (University of North Carolina Press, 2018); Anders Åslund, *Russia's Capitalist Revolution: Why Market Reform Succeeded and Democracy Failed* (Peterson Institute, 2007), 213.

[84] Daniel J McCarthy, Sheila M Puffer, and Alexander I Naumov, "Russia's Retreat to Statization and the Implications for Business," *Journal of World Business* 35, no. 3 (July 1, 2000): 256–74

[85] Piotr Dutkiewicz and Dmitri Trenin, *Russia: The Challenges of Transformation* (NYU Press, 2011), 18.

[86] John Willerton, Mikhail Beznosov, and Martin Carrier, "Addressing the Challenges of Russia's 'Failing State': The Legacy of Gorbachev and the Promise of Putin," *Demokratizatsiya: The Journal of Post-Soviet Democratization* 13, no. 2 (April 1, 2005): 219–40, https://doi.org/10.3200/DEMO.13.2.219-240.

[87] Thane Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia* (Harvard University Press, 2017), 250–57.

Apart from the state's renewed role in economic management, Putin's attempt to reconstruct the state, Sakwa argues, also meant "establishing institutions strong enough to prevent state capture by countering the power of the oligarchs."[88] This resulted in the emergence of "capitalism with a corporatist face" where the balance of power shifted in favor of the state ownership in state-business relations, with oligarchic groups being forced to become a subordinate actor through the policy of equidistance.[89] The logic of this new economic arrangement indeed required the taming of some oligarchs who tried to stick their necks out, as demonstrated in the arrest of Khodorkovsky and the nationalization of his oil company Yukos. At the same time, the increased state control through ownership in resource sector was meant to strengthen the weakened capacity of central authority and rebalance its positioning in effectively managing the resource rents vis-a-vis the regional and international actors, which would help reinstate Russia as a global power. In short, the ultimate end of Putin's statist intervention aimed at stabilizing the economy with conditions conducive to investment and disciplining the oligarchic groups.[90]

Of course, there is a widely recognized contention that the reconsolidation of the state under Putin was not all about the economic benefit. State reconstruction, it is argued, is intertwined with the consolidation of the regime, which was contingent on dire political priorities. The benign version of this priority, argued by Myant and Drahokoupil, reflected societal changes where the people's economic suffering surged a strong demand for a state capable of providing welfare.[91] Yet Putin's primary motive was to consolidate his regime and curb the ambitions of powerful oligarchs, as clearly manifested in the war on oligarchs and his move to centralize power under his administration through establishing a power vertical, marginalizing political opposition, and bringing former KGB officials into the new coalition.[92] Thus, under the pretext of developing state capacity, Putin was ruthless, Robinson asserts, in fortifying the state's revenue position and knit together the independent economic elite with the

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[88] Richard Sakwa, *Putin: Russia's Choice* (Routledge, 2007), 243.
[89] Philip Hanson and Elizabeth Teague, "Big Business and the State in Russia," *Europe-Asia Studies* 57, no. 5 (July 1, 2005): 657–80
[90] Domjan and Stone, "A Comparative Study of Resource Nationalism in Russia and Kazakhstan 2004–2008."
[91] Martin Myant and Jan Drahokoupil, *Transition Economies: Political Economy in Russia, Eastern Europe, and Central Asia*, 1 edition (Hoboken, NJ: Wiley, 2010).
[92] Stephen K. Wegren and Dale R. Herspring, *After Putin's Russia: Past Imperfect, Future Uncertain* (Rowman & Littlefield Publishers, 2009), 168.

capacity to challenge him under the presidency by ensuring the state control over what he calls "state-supporting and internationalized" sectors of the economy.[93]

In stark contrast, during the late 1990s, Kazakhstan maintained consistent economic and social stability amid its ethnic diversity, thanks to the presence of a relatively stable state inherited from the Soviets. Nevertheless, for the president Nursultan Nazarbayev, the long-time admirer of Lee Kuan Yew's Singapore as a vision for industrial Kazakhstan, an economically stable state, "is particularly important to ensure the country's accelerated economic growth and effective economic planning in terms of existing macroeconomic and institutional conditions."[94]

The idea of an economically well-balanced state with the roles it should assume finds its pedigree in the repercussions of the privatization policy adopted during the transition. This was when Kazakhstan's government, on the brink of collapse, had to massively sell off the important oil reserves to foreign companies.[95] Over time, however, upon realizing the dire consequences that dependency of the state budget on multinational oil companies and their oil export might bring, President Nazarbayev launched a policy of economic nationalism that aimed at enhancing the state's control over natural resources to maximize the profits from the surge in energy prices.[96] Though such nationalistic policy is usually regarded as inherently political control, scholars argue that the reasons behind the resource nationalism in Kazakhstan are less about politics; "it focuses on economic growth and development as a basis for strengthening the political legitimacy of the ruling elite."[97]

The modernization through etatization. A second strand of scholarship emphasizes that presidents' longing for the state expansion is their commitment to catch up with the developed world through establishing a developmental state that helps "redistribute wealth from

[93] Neil Robinson, *The Political Economy of Russia* (Rowman & Littlefield, 2012), 39.
[94] Roza Nurgozhayeva, "State Ownership in Terms of Transition: Curse or Blessing," *Cornell International Law Journal* 50, no. 1 (2017): 59.
[95] Pamela Blackmon, *In the Shadow of Russia: Reform in Kazakhstan and Uzbekistan*, Eurasian Political Economy and Public Policy Studies Series (East Lansing: Michigan State University Press, 2011).
[96] Serik Orazgaliyev, "State Intervention in Kazakhstan's Energy Sector: Nationalization or Participation?" *Journal of Eurasian Studies* 9, no. 2 (July 1, 2018): 143–51, https://doi.org/10.1016/j.euras.2018.06.001.
[97] Domjan and Stone, "A Comparative Study of Resource Nationalism in Russia and Kazakhstan 2004–2008," 36.

consumption to investment and extract and allocate resources as the state required."[98] The impetus for industrial modernization stems from the failure of neoliberal marketization in the post-Soviet countries sped up de-industrialization and "*resourcialization*", thus giving rise to an economic "*involution*". In this process, the economy erodes its very productive foundation.[99] Agreeing with the point, Lane asserts that the ills of neoliberal reform gave rise to "chaotic capitalism," under which the state is rendered unable to direct the necessary accumulation of capital and effective coordination of the economy because the chaos results in elite disunity and instability.[100] In short, the Russian economy, captive to a set of detrimental and inherent disadvantages, could never develop "without a state structure and state policies" that can compensate for those disadvantages. Thus, the argument goes, the reliance on the state and its strong power is not only a realistic approach for Russia to coordinate market-state interaction and develop its industrial capacity but also plays a legitimate role in bringing employment and social welfare.[101]

Building on this reasoning, Tsygankov argues that Putin promoted a vision of "neo-mercantilism" in which the state plays a dominant role and "reserve(s) the ability to shape economic outcomes independently of market forces by controlling key resources, coordinating the activities of main internal players, and assisting the country in finding its niche in the global economy."[102] Yet state power should also synthesize the market economy and adopt the state-private partnership to make the development possible. This vision also justifies Putin's doctrinal rejection of market-based development; he wrote in his dissertation that "a contemporary strategy for rational use of the resources cannot be based on the possibility of the market alone." Additionally, the increased state control of assets, Barner argues, is informed by Putin's understanding of the international order, both political and economic, which consists of three important parts; the state should help the private sector to develop the economy, states and not

[98] Andrei P. Tsygankov, *The Strong State in Russia: Development and Crisis* (Oxford University Press, 2014), 117.
[99] Dutkiewicz and Trenin, *Russia*; Michael Burawoy, "The State and Economic Involution: Russia through a China Lens," *World Development* 24, no. 6 (June 1, 1996): 1105–17, https://doi.org/10.1016/0305-750X(96)00022-8.
[100] Lane, "From Chaotic to State-Led Capitalism."
[101] Allen C. Lynch, "Roots of Russia's Economic Dilemmas: Liberal Economics and Illiberal Geography," *Europe-Asia Studies* 54, no. 1 (January 2002): 45, https://doi.org/10.1080/09668130120098223.
[102] Tsygankov, *The Strong State in Russia*, 117.

firms are the competitors in the international economy, and control over natural resources are an important mechanism of international influence.[103]

In this context, increasing state control over rents is better not only for producing funds for the government to reestablish the country's industrial base but also for reasserting the state's global influence. As the ruling elite justified, this would be achieved by creating "national champions," the state-owned companies like gas and oil giants Gazprom and Rosneft, capable of successfully competing in the world market.[104] At the same time, the state's re-nationalization efforts in this process is considered to be a necessary condition for the state to become an "active corporate partner with private investors to ameliorate costs associated with substantial hold-up due to the propensity of oligarchs and local bureaucracy to divert wealth."[105]

There is indeed a political side of the story that intertwines with the economic aims. The state's assertiveness, Tompson argues, helps the elite counter the possible influence that relatively large private companies might create to defend their interests.[106] Given the nature of the industrial structure of Russia, which tends to produce high concentration of ownership of industrial assets, these companies might pose a greater danger to the developmental vision once they start meddling in politics. Thus, it makes more sense for the state to tighten its grip on commanding heights of the economy to pursue its developmental objectives through direct control rather than indirect methods such as regulation and taxation. In short, there is a scholarly consensus that a genuine inspiration for advancing developmental state vision, which purely aims at restructuring the society and modernizing the economy in Russia, guided leaders' reasoning that they, a "trusted few," needed to change the structure of power in Russia so that they can advance a new model of political economy in Russia.[107] The state became the dominant player, and its main instrument was control over strategic resources.

The need for increased state involvement in the economy that can bring economic modernization is a common argument among the scholarly circles on the Kazakhstani

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[103] Barnes, *Owning Russia*, 219.
[104] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 250.
[105] N. Vanteeva, "The Re-Emerging Role of the State in Contemporary Russia," *Transition Studies Review* 19 (September 2012): 27.
[106] Tompson, "Back to the Future?"
[107] Dutkiewicz and Trenin, *Russia*, 50.

economy.[108] This is the release of the blueprint, Strategy 2030, which outlines Nazarbayev's statist-cum-liberal developmental vision that aims to achieve diversification and modernization of the economy through government-induced incentives, similar to the economic policies of Asian developmental states. His development is also mirrored in his annual address to the people in 2008, where he said: "We should continue our strategic focus on Kazakhstan's industrialization, on our joining the community of the world's 50 most competitive nations and on forming a select group of 30 corporate leaders to advise on these goals".

Without active state involvement, the domestic entrepreneur class can never play a substantial role in financing the industrialization and diversification of the oil-dependent economy. Several important organizations, including Samruk-Kazyna, a sovereign wealth fund modeled after similar organizations in Singapore and Malaysia, are designed to facilitate such a developmental vision. According to Nurgozhayeva, such a well-designed state asset management system like Samruk-Kazyna is vital to ensure efficient channeling and allocating an accumulated foreign exchange in the economy. Similarly, Kalyuzhova also maintains that administrations in Russia and Kazakhstan introduced wealth funds as special financial vehicles to "substitute for the actions of private actors by directing credit for industrial development and investment" because of the underdeveloped and structurally skewed nature of private financial sectors.[109] In short, the primary aim of the wealth funds, the National Fund of Kazakhstan, and the *Samruk-Kazyna* are to help the policymakers achieve industrialization and economic diversification while providing socio-economic and political stability and control.

State as a domain for the struggle over the property. Finally, there is an argument which contends that the issue of bringing state control over strategic sectors reflects the ongoing fighting over property among different factions managed, sometimes with constraints, by presidents.[110] The intensity of the battle over property became particularly salient in Russia after Putin came to power when state capture by oligarchs transformed into the business capture by the expanded power of the state that individual bureaucrats have used. In fact, the Russian elite

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[108] Joachim Ahrens and Manuel Stark, "Emulating Developmental States? The Institutional Foundations of Economic Transition in Kazakhstan," *Critique Internationale* No 63, no. 2 (n.d.): 95–110.
[109] Yelena Kalyuzhnova and Christian, A Nygaard, "Special Vehicles of State Intervention in Russia and Kazakhstan," *Comparative Economic Studies* 53, no. 1 (March 1, 2011): 58, https://doi.org/10.1057/ces.2010.26.
[110] Sakwa, *Putin*, 250.

groups tend to have different views on two major economic issues: "the scale of state participation in the economy and the role of large private business in the political process."[111] In the Kremlin, major policy outcomes, including those regarding the direction of the economy, whether a strong state or the private business should be the agent of economic modernization, are believed to happen among three major factions that *even* limit the president's direct control: liberals or reformers, *siloviki,* and technocrats.[112] Such a debate between the representatives of such groups, statists, and liberals, regarding the role of the state versus the market in Russia is well documented by Miller, Aslund and Gustafson.[113]

There appears to be a scholarly consensus that the *siloviki,* the members of coercive organs of the state, is the group that pursues economic nationalism and seeks increased state control over key economic sectors, in contrast to the liberals who prefer market liberalization and private actors in economic management.[114] According to this line of argument, there is a built-in tension between these two groups regarding the prioritization of political control and economic liberalism.[115] The rise of ex-KGB officer Putin as president and the subsequent increase in oil prices then presented an opportunity for the *siloviki* faction to renew the position vis-a-vis oligarchs' domination and take back their strength in the political and economic life of the country.[116] Thus, they stood behind the attack to nationalize the private companies in key economic sectors, including successful oil company Yukos and still hold the belief that such moves could put Russia along the path of "bureaucratic capitalism" in which the newly established state-controlled companies could be used as channels to extract the rents. In that sense, the strategic takeovers seemingly guided for economic development are "re-privatization"

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[111] Alexander Auzan, "Revolutions and Evolutions in Russia: In Search of a Solution to the Path Dependence Problem," *Russian Journal of Economics* 3, no. 4 (December 1, 2017): 342, https://doi.org/10.1016/j.ruje.2017.12.002.
[112] Ian Bremmer and Samuel Charap, "The Siloviki in Putin's Russia: Who They Are and What They Want," *The Washington Quarterly* 30, no. 1 (January 1, 2007): 83–92, https://doi.org/10.1162/wash.2006-07.30.1.83.
[113] Chris Miller, *Putinomics: Power and Money in Resurgent Russia* (University of North Carolina Press, 2018); Anders Aslund, *Russia's Crony Capitalism* (Yale University Press, 2019); Thane Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia* (Harvard University Press, 2017).
[114] Richard Sakwa, *The Crisis of Russian Democracy: The Dual State, Factionalism and the Medvedev Succession* (Cambridge University Press, 2010), 131.
[115] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 234.
[116] Åslund, *Russia's Capitalist Revolution*.

or redistribution of property: it is not the state but particular members in the political elite that, controlling the state structures, really "own" these companies.[117] Such concern is well expressed by liberal critic Boris Nemtsov, who said, "it is offensive that under Putin the state has taken on the role of plunderer and racketeer with an appetite that grows with each successive conquest."[118]

Such internal disputes over the state assets among various factions, scholars claim, highlight the nature of the regime in Kazakhstan. According to Peyrouse, the regime in Kazakhstan functions as a typical patronal system in which several circles enclose their economic domains with a prerogative, though they are subject to struggle; the president and his entourage are called family, who have important stakes in lucrative sectors such as natural resources, media, and banking, the oligarchs with important involvement in mining, the technocratic and regional elites, who act as intermediaries in the bureaucracy.[119] Similarly, Satpaev characterizes those factions as family, the inner circle, the outer circle, and the distant circle.[120]

President Nazarbayev, in this system, is seen to mediate the conflicting interests of competing groups in acquiring resources associated with the state. Yet, the regime's stability is very fragile due to the difficulty of striking a balance among them. One famous example is the emerge of entrepreneurial opposition during early 2000s that grew dissatisfied with the family's growing stronghold with the claim that "the greatest threat to their economic well-being was the power of the ruling family to arbitrarily decide the fate of entrepreneurs and political players alike".[121] At the same time, such internal rift can also happen inside the family, which does not constitute a united group. Such rivalry is argued to have happened between two sons-in-law of president Nazarbayev, Aliyev and Kulibayev, whose interests in key sectors such oil, banking

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[117] Philip Hanson, "The Resistible Rise of State Control in the Russian Oil Industry," *Eurasian Geography and Economics* 50, no. 1 (January 1, 2009): 14–27, https://doi.org/10.2747/1539-7216.50.1.14.
[118] Åslund, *Russia's Capitalist Revolution*, 256.
[119] Sebastien Peyrouse, "The Kazakh Neopatrimonial Regime: Balancing Uncertainties among the Family, Oligarchs and Technocrats," *Demokratizatsiya* 20, no. 4 (September 22, 2012): 345–71.
[120] Dosym Satpaev, "An Analysis of the Internal Structure of Kazakhstan's Political Elite and an Assessment of Political Risk Levels," in *Empire, Islam, and Politics in Central Eurasia* ed. Uyama Tomohiko (Slavik Research Center, Hokkaido University, 2007): 283-300.
[121] Barbara Junisbai and Azamat Junisbai, "The Democratic Choice of Kazakhstan: A Case Study in Economic Liberalization, Intraelite Cleavage, and Political Opposition," *Demokratizatsiya; Washington* 13, no. 3 (Summer 2005): 382.

and media clashed with each other. In short, like Russian case, state control over the resources correspond to the predominance of the leading faction in the competing circle, which is the family. The summary of the debates over the rise of state capitalism in post-Soviet Russia and Kazakhstan is provided below.

2.3 Conclusion: how the framework contributes what the existing literature misses

The literature review above shows that scholars have attempted to establish arguments regarding the emergence and nature of political economy in post-Soviet countries after the state's comeback. Generally, the combination of arguments above suggests either a positive inkling of stronger state that was supposed to stabilize and develop the economy through an efficient rent management system or pessimistic view of the state as an intersection of wealth and power for vying groups. However, these accounts simply reduce the matter to a troubled relationship between the state and private business in mainly resource sectors, thus disregarding the overall nature of political dynamics taking place inside the regime.

The existing arguments fall short of the analyzing the timing of the state expansion; why did political elites see a necessity to impose state control after Putin came to power in Russia or after a long period of stability in Kazakhstan. Also, they do not give a clear explanation to the puzzle of why the tightening of state's grip on key sectors of economy did not completely thwart the presence of private companies in strategic core sectors. The puzzle here is that the nationalizations and state intervention in these countries did not necessarily mean the end of their commitment to the principles of liberal market. In short, the existing studies on post-Soviet politico-economic terrain do not consider the importance of domestic politics and political rationales that the political system can play in this process. This demonstrates the necessity of an alternative framework that can fasten the dynamics of political regimes and power relations in it to the changes in economic policies.

The alternative framework that this dissertation provides aims to remedy such oversimplified view through deriving theoretical insights from the intersection of politics and economy. In fact, in its analysis the framework of this dissertation speaks volumes to a missing link in the literature of comparative political economy regarding studies on the impact of politics on economic arrangements in non-democratic countries. In general, the scholars of comparative political economy have studied issues of dictatorship and state capitalism separately, thus leaving a major rift in the interaction between authoritarianism and economic arrangements. On

one hand, the problem with the literature on comparative authoritarianism has been its disregard of the importance of political economic foundation in regimes. Scholars seem to disregard the significance of economic policies and growth strategies in domestic economy that autocrats use to enhance national power. On the other hand, scholarship that focuses on the rise of state capitalism does not take into account the aspect of political power and regime survival in the analysis.

Over the past decade, the focus of scholarship in comparative dictatorship has been directed to the study of political institutions such as parties, elections, and legislatures that autocrats utilize to maintain power and distribute goods in the absence of power-sharing arrangements. Breaking from this tradition, the framework of this dissertation focuses on state-controlled economic resources and agents, including state-owned companies that authoritarian regimes utilize for their survival. In this analysis, the dissertation resonates well with the emerging field of non-institutional features of authoritarian rule.[122]

Along with its novel insight into the scholarship on dictatorship, the originality of this framework comes from its intent to break with the existing literature by offering a nuanced analysis of state capitalism. The existing literature scrutinizes state capitalism as a deformed version of the liberalist economic order by focusing on major economies and thus neglecting diversity in case selection.[123] Historically, state capitalism has usually been identified with a Soviet-style planned economy where the state acted as a behemoth-like corporation. The financial crisis in 2008 resurrected discussions of "bringing the state back in" again. After the crisis a new set of economic challengers emerged in the world, so-called BRICS (Brazil, Russia, India, China and South Africa), the nuanced policies of which led to a resurgence of scholarly debates on state capitalism.[124] Since then, a trajectory of the scholastic interest in state capitalism took two divergent routes: the works of liberalism-inspired critiques who warned against the threats state capitalism and the works of policy-oriented observers who dealt with the institutional underpinnings of the system. However, neither camp fairly explained the role

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[122] Thomas Pepinsky, "The Institutional Turn in Comparative Authoritarianism, British Journal of Political Science, Cambridge Core," *British Journal of Political Science* 44, no. 3 (2014): 631–53, https://doi.org/10.1017/S0007123413000021.
[123] Ian Bremmer, "State Capitalism Comes of Age," *Foreign Affairs*, 2009, 4, https://www.foreignaffairs.com/articles/united-states/2009-05-01/state-capitalism-comes-age.
[124] Ilias Alami and Adam D. Dixon, "The Strange Geographies of the 'New' State Capitalism," *Political Geography* 82 (October 1, 2020): 80, https://doi.org/10.1016/j.polgeo.2020.102237.

of political structures and power relations behind the rise of such systems. By connecting the way that political power works in personalist authoritarian regimes with their economic systems, the framework in this dissertation fills in this existing hole in this literature.

Apart from its break with the existing literature on the causes of the phenomenon, my framework also lies in the explanation of the mechanisms through which state capitalism functions. In explaining the workings of state-capitalist economies, scholars exclusively focused on state-owned enterprises or sovereign wealth funds.[125] Yet, omitting the analysis of private sector activity, especially that of oligarchic big businesses that operate alongside the state companies, we are unable to understand how state-market interaction produces a coherent state capitalist economy. Hence, bringing both big and small businesses in private sectors along with state dominant sectors into a holistic view, this research produces a fine theorization of the dualistic nature of state capitalism, which adds a new dimension to the discussion. Such dualistic analysis will enable us to better understand the puzzling existence of liberal principles of market economy in nondemocratic state capitalist systems, including a freer business environment conducive to private ownership and foreign investment and their political rationale.

[125] Richard Carney, *Authoritarian Capitalism Sovereign Wealth Funds and State-Owned Enterprises East Asia and Beyond* (Cambridge England; New York: Cambridge University Press, 2018), http://www.cambridge.org/gb/academic/subjects/politics-international-relations/political-economy/authoritarian-capitalism-sovereign-wealth-funds-and-state-owned-enterprises-east-asia-and-beyond.

Chapter 3: Political economy of personalist authoritarian regimes in Russia and Kazakhstan

The previous chapter introduced the dissertation's theoretical framework along with the literature review. The current chapter proceeds with applying the theoretical framework to the case studies of Russia and Kazakhstan. The chapter is divided into two subsections, a comprehensive analysis of Russian political economy from 1986 to 2018 under three presidents, Mikhail Gorbachev, Boris Yeltsin, and Vladimir Putin and the political economy of Kazakhstan from 1991 to 2016 under the President Nursultan Nazarbayev. The chapter discusses how the historical account of the political and economic transition in both Russia and Kazakhstan paved a way to the emergence of new politico-economic system. The chapter then proceeds with the analysis of the emergence of new political and economic order under new presidents, Vladimir Putin and Nursultan Nazarbayev, through three stages: the consolidation of power and creation of markets, the personalization of power and creation of dualistic capitalism, and the embedded nature of emerging soft personalistic cult in both countries.

3.1 The emergence of new political economy under Boris Yeltsin

It is with the onset of Gorbachev's democratizing reforms that Russia was for the first time in its modern history introduced to a different kind of political regime. In such a rigidly hierarchical system in which almost everyone had an incentive to stick to the status quo, the only change could come from the top leadership.[126] The primary rhetoric for change was to revitalize the economy and inject some open discussion and creativity into the ossified system without substantially altering the core communist principles, similar to China's reform.[127] The components of *perestroika* included *uskorenie* and later *glasnost*, the acceleration of industrial investment and technological progress, along with giving voice and access to information to the public that aimed to decentralize the decision-making and mobilize public support for the reforms.

When Boris Yeltsin, the first ostensibly democratic leader in Russia, inherited the old system, he was not an outsider to Gorbachev's reform initiatives. However, Gorbachev's indecisiveness for continuing his reform programs led Yeltsin to make a break and carve his

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[126] Michael McFaul, *Russia's Unfinished Revolution: Political Change from Gorbachev to Putin* (Cornell University Press, 2015).
[127] Chris Miller, *The Struggle to Save the Soviet Economy: Mikhail Gorbachev and the Collapse of the USSR* (UNC Press Books, 2016):60-90.

own path for reform. Sacked by the cliques in the Politburo, Yeltsin first became the chairman of the Russian parliament and then president of Russia in 1991. From that post, Yeltsin had to carry out three transformative tasks, which Offe calls as *triple transition;* design new political order and secure his grip on it, disband the tattered economy to launch a market transformation, and finally dissolve the Soviet Union and build new state institutions.[128]

Among these, the most challenging task before him was to make a complete transformation to capitalist order. The dire conditions that the economy found itself was highly a testament to the urgency of such reform. As mentioned earlier, Soviet economy was on the brink of collapse because of external debts and a huge budget deficit. By 1991, the deficit soared around 31% of GDP, as public expenditures had skyrocketed beyond control and union republics ceased to send their taxes.[129] Also, the rampant issuance of ruble credits by republics without coordination with the central bank led to massive hyperinflation, which was around 2,500% in 1992.[130] Partial liberalization of trade and idiosyncratic regulations of prices aggravated the market distortions. Lining up for chronic food shortages was order of the day. A rapid fall in economic output then led to the decline in state capacity, which could not maintain societal order. In short, Russia was struggling with multiple shocks.

Inspired by the example of Poland's liberalization, he was convinced that his grand design for the new economy, now known today as "big bang" or "shock therapy". Such transformation required a "jump to a market economy" at full speed through price decontrol, freeing markets, and privatization of enterprises.[131] In practice, the shock therapy was supposed to go ahead with required four interlocking wheels of "*marketization*"; stabilization, liberalization, privatization and institution building.[132] Now, with the majority of Congress authorizing "go-ahead" to his economic crusade, Yeltsin formed new government led by a Western-minded economist, Yegor Gaidar and his colleagues, including Anatoly Chubais, who were in turn advised by a few

[128] Claus Offe and Pierre Adler, "Capitalism by Democratic Design? Democratic Theory Facing the Triple Transition in East Central Europe," *Social Research* 71, no. 3 (2004): 501–28.
[129] Anders Åslund, *How Russia Became a Market Economy* (Brookings Institution, 1995).
[130] Anders Aslund, "Why Has Russia's Economic Transformation Been So Arduous?" Carnegie Endowment for International Peace, accessed May 6, 2019
[131] John Marangos, "A Political Economy Approach to the Neoclassical Model of Transition," *The American Journal of Economics and Sociology* 61, no. 1 (2002): 44.
[132] Shafiqul Islam and Michael Mandelbaum, *Making Markets: Economic Transformation in Eastern Europe and the Post-Soviet States* (Council on Foreign Relations Press, 1993), 20–25.

American experts. Now charged with everything, Yeltsin's economic reform path was, at least in theory, directed towards building market capitalism.

Another important element of big leap towards a market economy was to establish a decentralized form of property and ownership structure through privatizing enterprises. Such an "urgent and politically vulnerable" task was, in theory, necessary to form a stratum of a capitalist class who could not only degrade the influence of the old class through *depoliticization*, but also restructure the enterprise system with effective corporate governance so that they could provide revenue stream to state. It is because, according to the Western advisors, in Russia "political influence over economic life was the fundamental cause of economic inefficiency" and thus, "privatization fosters depoliticization because it robs politicians of control over firms." [133] The only problem, however, was the question of effectively implementing neatly formulated theory in practice given the structure of Soviet enterprises and the hostile political environment. In this regard, the major policy debate was concerned with how to carry out privatization and who would be the stakeholders.

Following extensive debates, the reformers unleashed the first round of privatization, dubbed as *mass privatization,* between 1992 to 1994. However, the transfer of ownership of large-scale enterprises to private hands scarred the Russian economy. [134] Although paper evidence showed the property transfers of 2,418 firms to the private hands in auctions, "many Russian shareholders were disappointed with the result of their participation in the voucher program and many workers felt frustrated to learn that the vast employee privileges did not empower them vis-a-vis the management".[135] Due to the design flaws which allowed a free transfer of vouchers, the managers de facto accumulated valuable blocks of shares at hand from workers and ordinary people, usually using a tactic of coercion and deceit. A random survey of 439 enterprises conducted by World Bank estimated that insiders dominated 84% of all non-state enterprises.[136] Such result, according to some scholars, came in due to the negligence to the fact that without proper incentive structure and infrastructure their program would extend

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[133] Maxim Boycko, Andrei Shleifer, and Robert Vishny, *Privatizing Russia* (MIT Press, 1997), 10–12.
[134] Thane Gustafson, *Capitalism Russian-Style* (Cambridge University Press, 1999), 42.
[135] Hilary Appel, "Voucher Privatisation in Russia: Structural Consequences and Mass Response in the Second Period of Reform," *Europe-Asia Studies* 49, no. 8 (December 1997): 1442, https://doi.org/10.1080/09668139708412508.
[136] "A Russian Puzzle What Makes the Russian Economic Transformation a Special Case," WIDER Working Papers (UNU-WIDER, 1996), 44, https://doi.org/10.22004/ag.econ.295322.

the spontaneous privatization by insider "*nomenklatura*" who preferred to engage in insider self-dealing and looting than productive investment.[137]

The second stage of privatization began in early 1995 with the government initiative to sell stakes in the most lucrative companies that were previously excluded from privatization in the hope of balancing the budget with some revenue. Yet, selling the stakes of such giants through privatization was politically difficult as the previous case demonstrated. The easy solution came when a group of politically connected bankers, Mikhail Khodorkovsky of Menatep Bank and Vladimir Potanin of Onexim Bank, came with the proposal to finance the budget deficit under "loans-for-shares" scheme.[138] The idea was simple; the banks would loan funds to the government for several years in exchange for its controlling stakes in key enterprises, especially in energy and mining, as collateral. Under the scheme, the government would auction the shares to whichever bank would loan to it and, in case of default, the creditors would sell the stakes at further auction.[139]

Yet, in practice the scheme barely worked; the government failed to repay, and auctions were rigged in favor of banks. As a result, a small group of nascent *oligarchs,* who had acquired their wealth in banking through favorable deals and theft from the government in early reform period, ended up buying the lucrative companies for astonishingly low prices.[140] For instance, Menatep Bank won around 78% of Yukos oil company which had the largest oil reserves, whose $450 million market capitalization reached $9 billion in two years.[141] Furthermore, the oligarchs grew in power through incorporating other enterprises, including 80% of national television and 70% of press to their emprise, they could exert more pressure on the state and dodge the public criticism. In short, due to dismal failure in design and negligence in implementation, massive privatization program in Russia produced fall in output in economy, cronyism and corruption in government and negative distributional consequences in society. As a result, ordinary Russian people came to associate the privatization with corruption, crime, and oligarchy and

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[137] Bernard Black, Reinier Kraakman, and Anna Tarassova, "Russian Privatization and Corporate Governance: What Went Wrong?" *Stanford Law Review* 52, no. 6 (2000): 1740–41, https://doi.org/10.2307/1229501.
[138] Richard Sakwa, "Putin and the Oligarchs," *New Political Economy* 13, no. 2 (June 1, 2008): 185–91, https://doi.org/10.1080/13563460802018513.
[139] Black, Kraakman, and Tarassova, "Russian Privatization and Corporate Governance," 1744.
[140] David E. Hoffman, *The Oligarchs: Wealth and Power in The New Russia* (PublicAffairs, 2011), 11–30.
[141] Sakwa, "Putin and the Oligarchs."

interchangeably use the word *prikhvatizatsiya* (grabbing) instead of *privatizatsiya* (privatization).[142] Worst of all, such disappointing views ultimately lent a popular base of legitimacy for the possibility of re-nationalization of some industries. Table 6 below can provide a view of how oligarchs came to concentrate their economic power in the economy.

Along with the battle that had broken out in economic front, Yeltsin had institutional chaos to deal with as well; the simultaneous agenda of designing political institutions for governing new Russian polity.[143] At first the experience of "too much political reform" and its subsequent failure over the past years led the leaders to follow the sequencing of economy first, politics second. Yet the question regarding what kind of rules should organize politics – democracy or dictatorship – stood in front of him to go ahead. Scholars usually divide the design of political institutions during Yeltsin era into two periods: the first republic in 1991-1993 transition and the second republic during 1993-1996. [144]

Few doubt that Yeltsin's avowed political aim was to construct a democratic Russia. Yet the problem he confronted was the legacy of the old system that was highly inauspicious to democratic rule. Although Yeltsin had a popular support as new president in 1991, his authority in new system was barely institutionalized and the political rules were ill-defined.[145] The president neither had a popular party to rest his power nor political machine to carry out his policies throughout the country. In addition, Russian society suffered a legacy of weak civil society characterized by popular apathy in political affairs. Thus, Russian politics in early transition years was confined to an elite circle who were located at two institutional loci of power; the newly created presidency packed with reformers and Russian Congress of People's Deputies (Duma) that hosted the representatives of old regime.[146]

The core of the issue, however, was that the balance of power between two institutions was not set clearly during the early institutional chaos. Although such ambiguity gave Yeltsin room to rule by issuing decrees and appointing personnel in an *ad-hoc* manner during the early

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[142] Marshall I. Goldman, *The Piratization of Russia: Russian Reform Goes Awry* (New York: Routledge, 2003).
[143] George W. Breslauer, *Gorbachev and Yeltsin as Leaders* (Cambridge University Press, 2002), 174.
[144] McFaul, *Russia's Unfinished Revolution*, 146.
[145] Colton Timothy J., "A Fresh Look at Semipresidentialism: The Russian Predicament," *Journal of Democracy* 16, no. 3 (2005): 118.
[146] Graeme Gill, *The Yeltsin Era* in Routledge Handbook of Russian Politics and Society, ed. Graeme Gill (New York: Routledge, 2011), 3–6, https://doi.org/10.4324/9780203804490.ch1.

period, over time unclear rules produced political uncertainty on whose voice should be heard on the political and economic design of the country.[147] The result was the years of stalemate and polarizing politics between reformist and restorationist groups at two institutions, which at last culminated in constitutional crisis and the death of Russia's budding but flawed democracy in 1993 when Yeltsin dismissed the Parliament, order the arrest of his opponents, and shelled the Parliament building.[148]

Yeltsin's subsequent victory, achieved by use of force, gave him a complete discretion to wipe the institutional slate clean and design a new institutional foundation of a second republic without any input by other independent political actors.[149] Although the new institutional arrangement later provided formal channels for political opposition, its deliberate design poisoned the fate of Russian democracy, opening a Pandora's Box for an irresistible path of unchecked personalist authoritarianism. First, the new constitution adopted a strong presidential system, or *super-presidentialism* with tremendous powers for the sake of promoting market reforms while the powerless legislative body remained under president's shadow.[150] Although Yeltsin had the means, he lacked the desire to use such power to suppress the opposition; his successor, Vladimir Putin would abuse it to eliminate opposition and consolidate his dictatorship.

The presidential election campaign of 1996 that had to define the fate of Russia provides a case for this intimate relationship around the "family" of Kremlin insiders headed by Yeltsin's daughter Tatyana Dyachenko and son-in-law Yumashev.[151] Out of the panic that Gennady Zyuganov, a communist front-runner, might win the presidential election in 1996 and expropriate assets privatized through dubious "loan-for-shares" scheme, the oligarchs mobilized their resources, money and media empire for Yeltsin's campaign to ensure his victory despite his debilitating health issues.[152] Following Yeltsin's hard-won victory, the oligarchs were rewarded with government perks and positions which they used to hijack the state to

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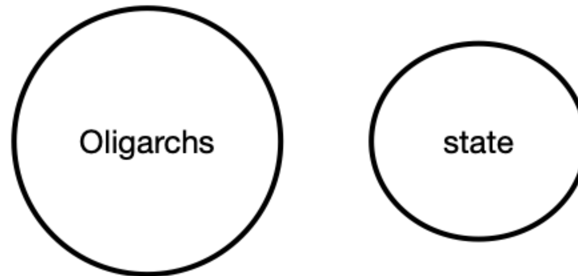
[147] Timothy J. Colton and Cindy Skach, "The Predicament of Semi-Presidentialism," *Democracies in Danger*, 2009, 121–36.
[148] David Kotz and Fred Weir, *Russia's Path from Gorbachev to Putin: The Demise of the Soviet System and the New Russia* (Routledge, 2007), 204.
[149] Joel M. Ostrow, *Politics in Russia: A Reader* (CQ Press, 2013), 38.
[150] McFaul, *Russia's Unfinished Revolution*, 209.
[151] Ostrow, *Politics in Russia*, 74.
[152] Lilia Shevtsova, *Russia--Lost in Transition: The Yeltsin and Putin Legacies* (Carnegie Endowment, 2007), 47–66.

facilitate their private interest, institutionalizing corruption and meshing private business with state administration. What then followed was the destruction of state institutions and chaotic division of property among a few people.

Figure 4. The power of oligarchs vis-à-vis the state in Russia



3.2 The rise of personalist authoritarianism and dualistic state capitalism under Vladimir Putin

Putin's ascendance to power is one of the most startling mysteries to many. Brought up in a city apartment and spending nearly fifteen years in Soviet KGB, he experienced a rapid rise through the city administration in St. Petersburg and federal government in Moscow.[153] No one would believe that a former KGB officer would change multiple positions, becoming head of the former KGB, prime minister and then, defying expectations, becoming president-elect within just three years. Over the next few years, he would emerge as the savior for Russians, providing stability and economic growth to the old house that the collective efforts of Gorbachev and Yeltsin almost destroyed. His meteoric rise to prominence out of thin air and his subsequent shakeup of the system left the many to ask, who is Mr. Putin and how did he manage to become ruler of the largest country of earth?

Putin's march to join the ranks of elite in Moscow started in 1996 when Sobchak lost the mayoral election. With the help of the networks of his former boss in Moscow, Putin quickly rose through multiple posts in two years – from deputy head for managing Kremlin property, deputy head for presidential administration, chief inspector for the federal bureaucracy and importantly the head of security service, the FSB. Then, on August 9, 1999, the ailing Yeltsin surprised the world when he announced Putin's candidacy to prime minister, proclaiming his ability to unite people and renew Great Russia. By that time, it was obvious that the "family",

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[153] Andrew Jack, *Inside Putin's Russia: Can There Be Reform without Democracy?* (Oxford University Press, 2005), 50–60.

the insider group of oligarchs and Yeltsin's associates, found themselves a suitable heir for the upcoming presidential election in June 2000.[154] Putin was a perfect candidate to safeguard family's interest and immunity from the winner-takes-all politics of Russia; a young, loyal, outsider and competent man who could be easily molded and trusted with the tacit agreement of the family.[155]

However, Putin would never win the presidency since, living always in shadows, he was hardly known to any one inside or outside Russia. The highly competitive terrain was dominated by formidable candidates like Yuri Luzkov, mayor of Moscow, Yevgenni Primakov, and Zhuganov who offered an appealing policy aimed at rooting out corruptions. Polls suggested that Putin only had 5% chance.[156] Afraid of losing the election, Yeltsin announced his early resignation and made Putin interim president, deliberately giving him an ample time to garner popular support. Thanks to the ongoing conflict in Chechnya, the mysterious bombings around Russia, and efforts of political technologists, Putin enjoyed all the media coverage controlled by oligarchs. His image of being tough, energetic, and dynamic leader who could unite the ailing Russian state against all enemies won him the election with 52 percent vote.

3.2.1 The formation of new regime, consolidation of power and creation of state-market nexus during early 2000s

After assuming power, the pressing question before Putin was how to solve the political and economic disorder left over from the previous regime while consolidating his grip on power. The political economic system of "Yeltsin's Russia" was the halfway house; the county was in a state of chaos as half-baked reforms severely weakened the economy, riddled the state with corruption, and exhausted the society with crime and inequality.[157] All the while a handful of oligarchs not only concentrated the important assets in their hands but also dominated the political process with their wealth and media empire. The regional governors, having long

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[154] Peter Reddaway, "Will Putin Be Able to Consolidate Power?" *Post-Soviet Affairs* 17, no. 1 (January 2001): 23–44, https://doi.org/10.1080/1060586X.2001.10641493.
[155] Peter Rutland, "Putin's Path to Power: Post-Soviet Affairs," *Post-Soviet Affairs* 16, no. 4 (2000): 319, https://www.tandfonline.com/doi/abs/10.1080/1060586X.2000.10641490?casa_token=lht6OBQ3oQkAAAAA:qvl1CfzNg9l_tAdaEk8DEbKgYKxxOLiV18nG7Ok2oFoVxWGeK1GatANvPYr-ReCFWYQzpeScsOcAeg.
[156] Daniel Treisman, *The Return: Russia's Journey from Gorbachev to Medvedev* (Simon and Schuster, 2011), 144.
[157] Daniel Treisman, "Russia Renewed," *Foreign Affairs* 81, no. 6 (2002): 58–72.

enjoyed autonomy "as much as they [could] swallow", easily defied the orders from Kremlin to share the revenues and ruled the regions as personal domain.[158] Meanwhile, the authority of ailing president Yeltsin was bleeding away with clashing interests of the competing clans in "anarcho-democratic" system.

Table 5.

Among these ills, a critical juncture that might have shaped Putin's political motivation towards the creation of a new politico-economic arrangement was the financial crisis of 1998. Some scholars indicate that the *ruble crisis* in 1998 was the fatal blow to the failed shock therapy reforms. Following the crisis, GDP per capita fell to around $3500, five times lower than average in other developed countries. The 1998-ruble crisis is thought to have provoked the eventual ascendency of personalized autocratic state capitalism under Putin. First, crisis became an opportunity for financial oligarchs and enabled the state to isolate its power from interests. In other words, the crisis weakened Yeltsin's authority and divided the political elite, creating conditions for political succession to be separated from economic interests. In the aftermath, Yeltsin had to find a political successor inside his administration and granted him extensive formal authority. Once Putin won the presidency, he simply completed the fallout of the 1998 financial crisis on politics in reclaiming his mandate to reassert centralized state authority.

Once in power, Putin was constrained by this legacy of political and economic order. Against this background he famously declared "Russia is in the midst of one of the most difficult periods in its history. For the first time in the past 200–300 years, it is facing a real threat of sliding into the second, and possibly even third echelon of world states."[159] The dire state of affairs made him realize that he had to accomplish three imminent tasks before him; to remedy the excesses of the revolutionary 90s, to adopt "political normalcy" to the country that suffered from the irresponsibility of the anarchic democracy, and finally to craft a new vision for developing Russian economy.[160] Combined, these tasks entailed what he referred to "restoration

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[158] Gordon M. Hahn, "The Impact of Putin's Federative Reforms on Democratization in Russia," *Post-Soviet Affairs* 19, no. 2 (January 1, 2003): 114–53, https://doi.org/10.2747/1060-586X.19.2.114.
[159] Dale Roy Herspring, *Putin's Russia: Past Imperfect, Future Uncertain* (Rowman & Littlefield, 2007), 1.
[160] Vladimir Gel'man, *Authoritarian Russia: Analyzing Post-Soviet Regime Changes* (University of Pittsburgh Press, 2015), 73.

of the guiding and regulating role of the state" with strong authority that would reign the control over regions, fight crime and corruption, and modernize the economy.[161]

However, Putin's hands were tied by the same elite that brought him in power. Building his own political machine with the power to implement his agenda would require him to consolidate his grip on power and control economic resources to fund the regime. In fact, the legacy of political power in Russia where the potency of personal relations weighs more than the institutions would necessitate such move; Putin would never effectively command the power of the state unless he "could establish his personal authority by creating effective informal networks based on mutual trust."[162] In other words, to preserve the existing power as new leader, Putin "had no option but to jettison old ballast, including the individuals who had put him in the Kremlin and who wanted to order him around."[163]

This logic is similar to the forming of early authoritarian regimes elsewhere. Haber argues that the political survival would pit a would-be autocrat to curb the powers of existing leadership that control him.[164] In fact, as Dawisha documents, Putin's inclination to consolidate his rule was known before he became president.[165] The liberal newspaper *Kommersant* obtained and published excerpts of a covert blueprint, titled *Reform of the Administration of the President of the Russian Federation*, which detailed gradual steps to install authoritarian rule under the presidential administration. Putin translated the blueprint into practice by following three steps: reining in the independent actors, establishing a centralization over the coercive organs, and controlling the financial resources.

Reining in regional/economic actors and establishing centralized power. The move towards the consolidation started in 2001 with an attempt to structure new patterns of interaction between the state and elite that had been hijacked by corrupt regional and business leaders.[166] Although in early days Putin attempted to rule by making a consensus with the existing elite and avoiding de-privatization due to his political weakness, over time, such balancing of the

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[161] Archie Brown, "Vladimir Putin and the Reaffirmation of Central State Power," *Post-Soviet Affairs* 17, no. 1 (January 2001): 45–55, https://doi.org/10.1080/1060586X.2001.10641494.
[162] Reddaway, "Will Putin Be Able to Consolidate Power?" 29.
[163] Shevtsova, *Russia--Lost in Transition*, 39.
[164] Stephen Haber, "Authoritarian Government," *The Oxford Handbook of Political Economy*, June 19, 2008, https://doi.org/10.1093/oxfordhb/9780199548477.003.0038.
[165] Karen Dawisha, *Putin's Kleptocracy: Who Owns Russia?* (Simon and Schuster, 2015), 224.
[166] Barnes, *Owning Russia*, 175.

conflicting interests proved difficult to sustain and delayed his bid to establish his political control.[167] The task required was to strengthen his power vis-a-vis other independent economic/regional actors that would neutralize their power in decision-making.

The first step in the campaign was directed to restoring the central authority of the state, the *political statism* that would end the defiance of regional executives and subordinate them to the command of the center. As mentioned above, the regional governors almost ruled as sovereign mini-dictators over vast regions with rich economic resources and were the source of opposition to Putin during the election. Delivering a speech at federal assembly in 2004, Putin stated that:

> Federal laws had lost the power of supreme law in many regions. Things went so far that individual regions in effect found themselves outside the common legal, financial, and fiscal system of the state, stopped contributing taxes to the federal budget, and were demanding the creation of their own gold and hard currency reserves, their own energy and customs systems and regional monetary units.[168]

It was against this backdrop that Putin launched another war against the regional executives by reasserting the "vertical chain of authority" and "dictatorship of law" with the aim of executing a uniform policy and enforcing laws across the regions.[169] The initial move to reimpose central control over regions came with an administrative change that restructured the Russian federal system by establishing seven federal districts, "super-regions", under presidential administration. These federal units each were to be directed by presidential envoys, a "super-governor" who would stay above in hierarchy from elected governors and become "ears and eyes" of Kremlin to monitor the activities of governors.[170] The new federal design removed governors' power and concentrated it in the hands of the president's close circle from the security organs.

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[167] Lilia Shevtsova, "Vladimir Putin's Political Choice: Towards Bureaucratic Authoritarianism Vladimir Putin's Political Choice: Towards Bureaucratic Authoritarianism Lilia Shevtsova," in *Leading Russia: Putin in Perspective*, ed. Alex Pravda (Oxford: Oxford University Press, 2005), 230.
[168] Dawisha, *Putin's Kleptocracy*, 269.
[169] C Ross, "Putin's Federal Reforms and the Consolidation of Federalism in Russia: One Step Forward, Two Steps Back!" *Communist and Post-Communist Studies* 36, no. 1 (March 1, 2003): 29–47, https://doi.org/10.1016/S0967-067X(02)00057-0.
[170] Michael McFaul and Kathryn Stoner-Weiss, "The Myth of the Authoritarian Model - How Putin's Crackdown Holds Russia Back Essay," *Foreign Affairs* 87, no. 1 (2008): 68–84.

Another line of attack came right before and after the Beslan tragedy in September 2004 where a group of terrorists attacked local school, killing nearly 328 captive children. In August, the structure of Federation Council, Russian upper house, had been changed and the regional governors lost their automatic membership in the upper house and thus their immunity from prosecution.[171] Although the governors subsequently earned membership in new State Council, they did not have any consultative powers. Following the tragedy, Putin declared that the executive authority "should be radically restructured in order to strengthen the unity of the country and prevent further crisis."[172] This gave him a pretext to justify a power grab under his executive through which he could replace governors who violated federal laws. By diminishing the governors' power and making them beholden to presidential whims, Putin placed the foundation for a centralized authoritarian state.

The second move towards the concentration of power involved an open attack to neutralize the entrenched power of oligarchs in Russian politics. Soon after assuming power, Putin had expressed his intention to voters that the "class of oligarchs will cease to exist."[173] Against this backdrop, he began taming the oligarchs that had come to dominate Russia's economy and political scene during Yeltsin era.

As briefly mentioned above, the oligarchs became dominant through initially commodity trading, financial brokering during chaotic liberalization and acquisition of state assets as they were wildly privatized.[174] However, the financial crash in 1998 shook up their power in banking assets when the government defaulted on its bonds, leaving only a few to survive and successfully transform into real sectors. These remaining oligarchs then came to concentrate their power in two sources: the commanding heights of the economy in sectors such as energy and metallurgy and popular media. The concentrated ownership structure of the Russian economy demonstrated the extent of their power. The country's largest 23 firms, which were controlled by 37 individuals, accounted for 30% of GDP in 2001.[175] Out of 1000 firms, 35

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[171] Dawisha, *Putin's Kleptocracy*, 271.
[172] Peter Baker, "Putin Takes Steps to Consolidate His Power," *Washington Post*, 2004, https://www.washingtonpost.com/archive/politics/2004/09/19/putin-takes-steps-to-consolidate-his-power/16d2ad7f-c716-4f6f-a530-6e59c3204f67/.
[173] tTreisman, *The Return*, 95.
[174] Hoffman, *The Oligarchs*.
[175] Sergei Guriev and Andrei Rachinsky, "The Role of Oligarchs in Russian Capitalism," *Journal of Economic Perspectives* 19, no. 1 (March 2005): 132, https://doi.org/10.1257/0895330053147994.

percent were controlled by single majority shareholders. It is this highly concentrated economic power that enabled oligarchs to penetrate state structures and access the corridors of power through which they could influence the economic policies in their favor.

There were inherent problems with the oligarchy that triggered the new regime to chase them as the adversary. The oligarchs' control over resources that constitute important portion of political economy gave them leverage over political leaders and the state through, for instance, bribes, campaign financing, or threat of closure if certain policies are not adopted. These resources also could serve the oligarchs as important tools for "mobilizing or de-mobilizing workers or social groups."[176] Also, as Putin made clear, the media empires served the owners as a means to spread mass disinformation and fight against the state.[177] Once united, they could solve collective action problem and easily advance their collective interest at the expense of regime. Most importantly, the violent means they used to keep their property while capturing new ones amid state weakness were a source of instability in the country, with the aluminum war as an example.[178] Knowing that he needed resources and counter their influence, Putin launched an attack against them.

The early attack to demonstrate the new authority started with the prominent media tycoons, Gusinsky and Berezovsky who owned extensive media holdings along with other assets. After it became clear that Gusinsky was using his media empire to advance his political agenda, he was forced to relinquish his assets to Gazprom which he took a debt of $1.2 billion during the financial crisis and left Russia for exile in Spain.[179]

A similar fate happened to another mogul Boris Berezovsky, who founded his business empire in the last years of the Soviet Union. He was said to control 70% of Moscow press and 80% of national television.[180] Investing heavily in politics, Berezovsky emerged as the most influential member of the Yeltsin's "family" in Kremlin. Although Brezovsky was a member of the "launching organization" that helped Putin come to power, he became discontent with Putin's authoritarian inclinations and directly challenged him by disparaging Putin's handling

[176] Barnes, *Owning Russia*, 158.
[177] Dawisha, *Putin's Kleptocracy*, 275.
[178] S. Fortescue, *Russia's Oil Barons and Metal Magnates: Oligarchs and the State in Transition* (Springer, 2006).
[179] Sakwa, *Putin*, 151.
[180] Sakwa, "Putin and the Oligarchs," 190.

of *Kursk* disaster in media and resigning from Duma in protests (his own party with regional governors). Announcing that "information pollution" was subverting national security, Putin soon expropriated Berezovsky's assets and drove him into exile in London in 2000 where continued his political activities to overthrow Putin until his mysterious death in 2013. With the demise of two tycoons who engaged too much in politics, the regime asserted its control over media to propagate the narrative of the regime.[181]

Following the demise of two media tycoons, other oligarchs faced similar raids from the regime for their alleged tax evasion and illegal privatization deals. In a famous meeting in the Kremlin in 2000, Putin struck a tacit agreement with the oligarchs, demanding that they distance themselves from politics in exchange for maintaining the distribution of property. However, the assault was renewed before the upcoming parliamentary and presidential elections in 2003/2004. This time the victim was the oil tycoon Mikhail Khodorkovsky - the richest man in Russia with personal wealth of $8 billion - who defied the redesign of new state-business relations.

Exploiting his links and funds of Komsomol, Communist Youth League, Khodorkovsky had established the first commercial bank, Menatep, during *perestroika* era. He managed to survive the 1998 financial crisis, converting himself from a financial oligarch to an industrial oligarch; his access to the echelons of power enabled him to acquire major stakes of newly created company Yukos with largest oil reserves during notorious "loans-for-shares" privatization for a meager value. Though Khodorkovsky personified the predatory nature of Russian capitalism, as shown in his statement that "politics is the most lucrative field of business in Russia", later he came to be a believer in market capitalism and restructured his business through transparency and new corporate governance.[182]

However, his insatiable appetite to get involved in politics for advancing commercial interests made him the enemy of the regime. Putting too much trust in anarchic pluralism, coupled with his usual overconfidence, Khodorkovsky openly pursued policies in contradiction with the president and hinted towards his own wish to become the next president. He bankrolled $100 million two liberal parties, Yabloko and the Party of Right Forces to run against Putin and

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[181] William Zimmerman, *Ruling Russia: Authoritarianism from the Revolution to Putin* (Princeton University Press, 2014), 220–30.
[182] Richard Sakwa, *Putin and the Oligarch: The Khodorkovsky-Yukos Affair* (Bloomsbury Publishing, 2014), 18–21.

his United Russia party in the 2003 parliamentary election.[183] In an attempt to head off the legislation antithetical to his business interests, Khodorkovsky was buying several seats in Russian Duma. His pursuit of independent oil policy was also trespassing into the prerogatives of the new regime; the plans to sell newly merged Yukos-Sibnet to U.S. oil companies, Chevron-Texaco and ExxonMobil, would have taken the strategic sector out of Kremlin, while building new pipelines to China would cut dominance of Transneft, the state pipeline monopoly.[184] In response to his provocative behavior, the regime launched an open attack against Khodorkovsky in 2003 that culminated in his disgraceful arrest and takeover of Yukos assets.

The end of crackdown on big business that culminated in the Yukos Affair set a new course for state-business interaction in Russia. The new deal was that the Kremlin does not interfere in the businesses of oligarchs as long as they keep their "equidistance" from politics and do not attempt to challenge the state.[185] The new framework did not mean a complete annihilation of oligarchic class; instead, the oligarchs were promised to access an institutionalized channel, through the Russian Union of Industrialists and Entrepreneurs, for interaction with the state so that can help develop the economy. Yet, at the same time, the new framework represented the beginning of the economy's backsliding into statism, where centralized state emerged as an important factor in the competition for asserting real control over the property.[186] This, in reality, marked the dawn of new era where the "economic considerations and property rights can become hostage to the political struggle."[187]

After successfully purging the independent powers, Putin's final move to assert his power in the new regime was to fill the hierarchically designed state with a new elite close to him to support the new regime. According to Field and Higley, the elite are "persons occupying strategic positions in public and private bureaucratic organizations."[188] Putin's political weakness of course did not allow him to replace the key figures immediately. During first years, his political weakness and lack of support group led him to position himself to appeal to

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[183] Goldman, *Petrostate*, 110–20.
[184] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 279.
[185] Ol'ga Kryshtanovskaya and Stephen White, "The Sovietization of Russian Politics," *Post-Soviet Affairs* 25, no. 4 (n.d.): 288–90.
[186] Barnes, *Owning Russia*, 209.
[187] Shevtsova, *Russia--Lost in Transition*, 134.
[188] Lowell Field and John Higley, *Elitism*, 1st edition (London: Routledge, n.d.), 20.

different groups on political spectrum; conservatives, liberal democrats, business magnates, and the security establishment.[189] Putin's power rested in his ability to maintain a political consensus among them that was based on the need for the restoration of strong state.[190]

However, it was crucial for Putin to develop his own support group, an inner circle whom he could rely on to run the new regime he was designing. Like Gorbachev and Yeltsin, he gradually managed to form a new coalition of supporters around Kremlin, who were mostly his former colleagues and close friends with different backgrounds.[191] In general, during the early years Putin gradually expelled members of the family and drew two ideologically distinct factions to run the new regime; 1) the *siloviki* faction with security background to control the coercive organs and 2) democratic statists and liberals to manage the financial affairs.

Putin's political weakness made him keep important members of the "family" as a check on his power. Because of the promise of not changing the power ministries, Putin had to keep the members of the family; prime minister Mikhail Kasyanov, the head of the presidential administration Alexander Voloshin, and the presidential advisor and daughter of Yeltsin, Tatyana Dyachenko for some time.[192] However, as the new support base came in, they had to relinquish their positions, leaving only those who became loyal to new president and remained in the presidential administration.[193]

With the former tenants vacated their positions at Kremlin, Putin drew in "his own people", a group of close friends and associates with security backgrounds from St Petersburg who would emerge as decisive players, helping him make strategic decisions in the regime. The scholars came to describe this group as *siloviki*; a security establishment that occupied power structures of the state.[194] With Putin's power consolidated, they began to sweep in different political and economic aspect of the regime or what Rutland calls "strategic positions and critical organizations from which the elite exercise their power."[195] The power structures of the

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[189] Rutland, "Putin's Path to Power: Post-Soviet Affairs."
[190] Fiona Hill and Clifford G. Gaddy, *Mr. Putin: Operative in the Kremlin* (Brookings Institution Press, 2013), 34.
[191] Olga Kryshtanovskaya and Stephen White, "Putin's Militocracy," *Post-Soviet Affairs* 19, no. 4 (January 1, 2003): 292, https://doi.org/10.2747/1060-586X.19.4.289.
[192] Aslund, *Russia's Crony Capitalism*, 49.
[193] Kryshtanovskaya and White, "The Sovietization of Russian Politics," 297.
[194] Bremmer and Charap, "The Siloviki in Putin's Russia."
[195] Peter Rutland, "The Political Elite in Post-Soviet Russia," in *The Palgrave Handbook of Political Elites*, ed. Heinrich Best and John Higley (London: Palgrave Macmillan UK, 2018), 275

state that *siloviki* occupied included strong a presidential administration, "power ministries" and agencies such as defense, internal affairs and FSB (former KGB), the Security Council and presidential envoys, all of which came under direct control of Putin's "presidential government".[196] In short, according to a study, the number of figures in the legislature and executive rose from 6.7 percent in 1993 to 26.6 percent in 2002.[197] Figure 5 below can demonstrate the inner circle of Putin regime in his tenure.

Meanwhile, Putin managed to mix the new support group with a trusted team of liberal cohorts with whom he worked together in the city council of St Petersburg in 1990s. There was a tacit division of labor between the *siloviki* and liberal; while the former was in charge of designing a structure of political control, the latter took the role of crafting fiscal and budgetary machine.[198] Specifically, the liberals were responsible for shaping the new economic policy and introducing carefully designed waves of market reforms that aimed to increase the revenue, attract investment, and craft a stable monetary and fiscal policy, occupying such ministries as finance, economic development and presidential advisory on economic affairs.

Figure 5.

Establishing state-market nexus. In sharp contrast to Yeltsin's unfettered market capitalism, the logic of Putin's political consolidation led to the formation of new economic rules, called the Moscow Consensus, consisting of a "state-market nexus" that would help him assert control over important economic resources and find sources of revenues while allowing the power of market forces to grow economy. Reclaiming a strong role for the state in the economy, or the "*economic statism*" that lay at the heart of the new economic order was logical extension of the increasing political prerogatives of hierarchically designed and centralized authoritarian state.[199] Thane describes the new political formula as a mixture of the "ideological appeal of Russian patriotism and renewed state strength with the motive of self-interest, wrapped in the language of market liberalism."[200]

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[196] Dawisha, *Putin's Kleptocracy*.
[197] Rutland, "The Political Elite in Post-Soviet Russia," 287.
[198] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 234.
[199] Sakwa, *The Crisis of Russian Democracy*.
[200] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 237.

The linkage between a strong state and economic development was the core of Putin's political agenda, as well documented by scholars.[201] Putin's frequent use of *state* during his addresses, rather than *economy*, could attest to the beginning of economic statism. Such statist rhetoric during first years allowed Putin to construct an economic consensus among ideologically distinct factions in Kremlin, who shared a common interest to bolster the central state. Market liberals saw the strong state as an enabling actor of economic growth through its ability to "effectively collect taxes, enforce the rule of law, and defend property rights."[202] As for conservatives, both economic statists and nationalists, the strong state should have reserved a necessary role to intervene in the economy, not only to maintain order, stabilize macroeconomic management, and guide the industrial activity, but also to prevent the capture of the state by powerful economic interests.[203]

However, beyond the consensus, the facade of a strong state capable of bringing economic growth was an important pretext for Putin to establish his political control over lucrative sectors of the economy which would bestow the regime with huge financial strength. The sectors that the state put under its prerogative in the name of regime were the oil and gas industries.[204] The importance of the energy sector was in part due to the massive wealth it produced and the political challenge that independent actors in the industry could mount. While oil and gas revenues accounted for $28 billion in 1998, by 2005 the figure rose to $143 billion.[205] For the regime struggling to establish its foothold and pay the bills, higher oil prices during early 2000 was manna from heaven. Without filling the empty coppers of the state, Putin would have never established his reign over the powerful oligarchs and regional leaders and secure the loyalty of the new elite effectively. However, the energy boom only benefitted a few wealthy Russians who, having carved out the energy industry, were ready to turn their wealth into political power.

The emergence of economic statism, of course, did not intend to bring a close to the regime's commitment to liberal market reforms. On the contrary, the new economic arrangement that aimed to facilitate the regime consolidation had to combine market-oriented

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[201] Hill and Gaddy, *Mr. Putin*, 38.
[202] Miller, *Putinomics*, 23.
[203] Sakwa, *Putin*, 243.
[204] Goldman, *Petrostate*.
[205] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 187–88.

economic policy with an authoritarian recentralization. Putin summarized this in a single statement: "we must be guided by the principle, as much state as is essential and as much freedom as is necessary." Thanks to the economic recovery that came as a result of increasing oil prices and recovering production in early 2000s, the government seized the opportunity to embark on a few structural reforms targeted at easing the bureaucratic hurdles, improving the business climate, fostering confidence in investment and overhauling the judicial system.[206] With the introduction of market reforms, Putin wanted not only to reassure international community that Russia remained committed to liberal principles but to also show that he is pro-business and true believer in free market.[207]

To advance the free market ideas in economy, Putin drew to himself a group of trusted liberal economists from St Petersburg, or "systemic liberals" who worked within the regime; Andrei Illarionov, a liberal economist, as an advisor to president, Aleksey Kudrin as Finance Minister, and German Grief as head of the Ministry of Economic Development and Trade.[208] Reconciling economic orthodoxy with the new statism, the liberals recommended easing the regulatory and tax burden on business, deregulation of the economy, privatization of enterprises and balancing the budget with low inflation. The result was a design of the comprehensive action program, known as the "grief Program" which aimed to boost GDP at 8 percent through adopting a new tax code, banking regulation, WTO ascension, and cutting state expenditures.

The new tax code adopted in 2000 introduced a massive change to the existing taxes, including the replacement of progressive income tax flat rate at 13 percent and cutting the profit, sales, and value-added tax. The bureaucratic hurdles that stifled business activity also improved as a result of the changes in the requirement for acquiring the licenses and the inspection of companies. As a result, the during the period of 2000-2003 domestic business thrived; by 2003 small and medium-sized enterprises (SMEs) accounted 94 percent of all businesses.[209] One of the biggest accomplishments of the government during this period was the adoption of fiscal and monetary conservatism. Thanks to the new principle, Russia could not only manage to pay

[206] Rudiger Ahrend and William Tompson, "Fifteen Years of Economic Reform in Russia: What Has Been Achieved? What Remains to Be Done?" OECD Working Paper (Paris, 2005), https://doi.org/10.2139/ssrn.881547.
[207] Hill and Gaddy, *Mr. Putin*, 135.
[208] Aslund, *Russia's Crony Capitalism*, 70.
[209] Sakwa, *Putin*, 246.

up its external debt but also turn the budget deficit into a surplus. Foreign public debt shrank from 66.8% of GDP in 1999 to 2.7% in 2007.[210] Due to good management of rising oil prices, Russia's currency reserves also increased from $8 billion in 1999 to $44 billion in 2003 and 460$ in 2007.[211] Increasing oil prices, coupled with reforms, helped Russia become the world's 23rd largest economy in 1999 to the 9th largest economy in 2008. The economic boom lent massive popular support to the changes that Putin launched to consolidate his power.

In summary, Putin's first term is characterized by building a new foundation for his regime. Putin restored state authority and reasserted the power by eliminating the other centers of power that were competing for political influence and resources. This included curbing independent power, centralization of power, and bringing in a new team of elites that believed democratic pluralism and free markets would threaten their power. Instead, Putin's team did their best to subordinate media, impose centralized political control over regions and increase state interference in political life, while providing some rights in the name of "sovereign democracy".[212]

In the economy, Putin built a new state-market nexus that consolidated the financial capacity of the regime. Using the strong state model, he tightened his hold over key industrial and financial assets. Such arrangement aimed at least partly at shoring up his position vis-à-vis big business. The crackdown on big business that culminated in the Yukos Affair, which settled the two clashing versions of modernity in Russia, market economy with pluralist democracy versus authoritarianism and the power of the state bureaucracy in the economy, set a new course for Russia's political economy. The selective punishment directed towards a few oligarchs sent a signal that in the context of a strong state, "the economic sphere was to be controlled by the authorities and the oligarchs were to understand that their historic role as the creators of capitalism was over."[213] The rules for a new model of political economy was that the Kremlin would not interfere in oligarchs' business as long as they keep out of politics. Yet the new framework did not mean a complete annihilation of the oligarchic class; instead, they were supposed to be the engine of economic development alongside a new economic actor, the state.

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210 Wegren and Herspring, *After Putin's Russia*, 155.
211 Treisman, *The Return*, 93.
212 Zbigniew Brzezinski, "Putin's Choice," *The Washington Quarterly* 31, no. 2 (April 2008): 95–116, https://doi.org/10.1162/wash.2008.31.2.95.
213 Sakwa, "Putin and the Oligarchs," 187.

The new state-business interaction represented the beginning of backsliding into economic statism, where the centralized state emerged as an important factor in the competition for asserting real control over the property. This, in reality, marked dawn of a new era where "economic considerations and property rights can become hostage to the political struggle."[214] The "imposed consensus" of Russia's elite, as Gelman notes, was achieved through the Kremlin's use of "selective punishment of some elite sections and selective cooptation of others."[215]

But in reality, the logic behind the bureaucratic centralization, according to Alexander Lukan, was a part of regime consolidation that aimed to arrange a new economic policy through two means: "a high level of dependence on large monopolistic structures and on serving their interests—especially those engaged in oil and other raw-material sectors; and a desire to reduce the financial autonomy of the regions and to limit burgeoning regional corruption."[216]

Figure 6. The power of oligarchs vis-à-vis the state in Russia after Putin came to power

3.2.2 Emergence of personalist authoritarianism and dualistic state capitalism through 2005 to 2010

The end of Putin's first presidency in 2003-2004, was a turning point in Russian politics. By that time, Putin discarded the elements of Yeltsinism electoral autocracy - the dominance of mutual connivance of power and business and reshuffle of important figures of old regime - and

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214 Lilia Shevtsova, *Russia--Lost in Transition: The Yeltsin and Putin Legacies* (Carnegie Endowment, 2007): 135.
215 Vladimir Gel'man, "The Extinction of Political Opposition in Russia," *PONARS Policy Memo*, no. 340 (2004): 7.
216 Alexander Lukin, "Russia's New Authoritarianism and the Post-Soviet Political Ideal," *Post-Soviet Affairs* 25, no. 1 (January 1, 2009): 76, https://doi.org/10.2747/1060-586X.24.1.66.

put the foundation in place for his own authoritarian style, "Plutonism". Since the beginning of his second term in 2004, Plutonism matured as personalized system which featured the importance of subordination and loyalty in politics and the centralization of state resources in economy.[217] Putin himself further increased his personal domination in politics, emerging as a "more tsar-like figure less dependent on various elite groupings or even his long-time allies."[218]

Personalization of power. Putin's personalization of the political process in Russia was highly evident over the first decade of 2000s. Personalist regimes, a category of the authoritarianism, can be characterized by the domination of a narrow group centered around single ruler's ultimate control over policy, leadership selection, and the security apparatus.[219] Such regime features an absence or lack of autonomous institutions that could limit the power of the ruler who normally acts as the ultimate arbiter for competing elite groups and factions.[220] In general, the process of personalization involves multiple steps; the acquiring greater personal power over institutions, dominating other political actors and factions through personnel management, personally influencing the national policy-making, and permanently extending power .[221]

Scholars associate several trends in Russian politics with the rise of regime personalization. The most important one was the growing importance of Putin's personality and the influence of his entourage regarding national decision making over the formal institutions of government.[222] By the late 1990s, Russia had developed the elements of pluralist democracy; including parties of different political orientations, media free of state control, and an emerging civil society with active NGOs.[223] These democratic features earned Russia the status of partial

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[217] Lilia Shevtsova, *Putin's Russia* (Brookings Institution Press, 2010), 134, https://muse.jhu.edu/book/30592.
[218] Brian D. Taylor, *The Code of Putinism* (New York: Oxford University Press, 2018), 79.
[219] Geddes, Wright, and Frantz, "Autocratic Breakdown and Regime Transitions," 318.
[220] Henry E. Hale, "Democracy or Autocracy on the March? The Colored Revolutions as Normal Dynamics of Patronal Presidentialism," *Communist and Post-Communist Studies*, DEMOCRATIC REVOLUTIONS IN POST-COMMUNIST STATES, 39, no. 3 (September 2006): 305–29, https://doi.org/10.1016/j.postcomstud.2006.06.006.
[221] Baturo and Elkink, "Dynamics of Regime Personalization and Patron–Client Networks in Russia, 1999–2014," 79.
[222] Rutland, "The Political Elite in Post-Soviet Russia."
[223] McFaul and Stoner-Weiss, "The Myth of the Authoritarian Model - How Putin's Crackdown Holds Russia Back Essay."

democracy by Freedom House until 2004.[224] However, by 2007, the institutional changes that Putin made to weaken parliament, disqualify opposition parties from elections, subordinate the judiciary, and harass civil society initiatives, removed the checks on presidential power and reduced Russian democracy to an empty ritual.[225] By successfully offsetting the political institutions and turning them into branches of the presidential administration, Putin transformed from a balancer in pluralist regime to a dispatcher in personalist one who could take the responsibility of directing the national policy.

The emergent system of personalized rule that Putin constructed can be characterized as "Plutonism", a system in which "power is highly personalized, but constrained by the prevalence of weak institutions which limit the leader's ability to implement many of his decisions."[226] Tapping into both old and new social norms and linking formal institutions with informal one, Plutonism features the following traits: 1) the idea that "Putin does everything" (presidential monopoly on key political decisions, allowing only limited role for institutions and public discussion; 2) the acceptance of electoral authoritarianism as a facade (open competition with unfree and unfair results; and (3) reshaping the government as a technocratic apparatus to execute Putin's will.[227] Sawka describes regimes that combine formal constitutional order with authoritarian rule as a hybrid "dual state"; the *normative state* that features law and constitutionality, operating in parallel with an *prerogative state*, or administrative regime that exercises power via para-constitutional and informal means.[228]

A constitutional state allows, on the surface, space for open public politics with parties fighting for elections and relevant institutional actors influencing the decisions.[229] However, it is the parallel world, the administrative regime, that wields the actual power behind the curtain. In this world, the social relations occur in a personalized form around the leader, or what Hale

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[224] Andrei P. Tsygankov and David Parker, "The Securitization of Democracy: Freedom House Ratings of Russia," *European Security* 24, no. 1 (January 2, 2015): 77–100, https://doi.org/10.1080/09662839.2014.968775.
[225] Zimmerman, *Ruling Russia*, 220.
[226] Robert W. Orttung and Sufian Zhemukhov, "The 2014 Sochi Olympic Mega-Project and Russia's Political Economy," *East European Politics* 30, no. 2 (April 3, 2014): 176, https://doi.org/10.1080/21599165.2013.853662.
[227] Lev Gudkov, "The Nature of 'Putinism,'" *Russian Social Science Review* 52, no. 6 (November 1, 2011): 16, https://doi.org/10.1080/10611428.2011.11065455.
[228] Sakwa, "The Dual State in Russia."
[229] Richard Sakwa, "Putin's Leadership: Character and Consequences," *Europe-Asia Studies* 60, no. 6 (August 1, 2008): 879–97, https://doi.org/10.1080/09668130802161132.

calls the "patronal president"; the key factions do not submit themselves to the limits of constitutional state; and they bend the rules and exercise para-political schemes to advance their goals.[230] In such a personalized regime, Putin acts as the boss over the centralized political machine and the 'pyramid of power', which, consisting of varying political interests or informal patronage groups based on personal loyalties and exchange of goods, formulate and execute the national decisions.[231] Although personalized systems grant certain spheres of influence and autonomy for faction leaders, the usually requires constant "hands-on management" (*rucinol upravlenie*) from the boss.

The figure 8 below describes the arrangement of the ruling elites with different interests under the vertically organized executive power of Putin, or what Marchenko calls the informal "Politburo 2.0". Several traits characterize the "Politburo 2.0". It is not the formal status of the members, but rather the informal relations that determine the influence on decision-making. As for the composition, it consists of different elite circles that can be referred to as "security" in power ministries, "politicians" in presidential administration and state organs, "state oligarchs" in energy and defense, and "business oligarchs" in mining and metallurgy.[232] According to Taylor, these informal groups, each represented by powerful figures, feature six key characteristics: informality in relations, shared background in formation, porous boundaries between state and business, competition for resources and influence, fluidity in political identity and multilevel structure of relations.[233]

Figure 7.

Establishing "Putin omics" - Putin as wealth manager in dualistic state capitalism. The formation of the new regime had an accompanying influence in the economic arrangements of the state-market nexus that emerged under elite consensus. Comparative regime research shows that the personalization of power under a single autocrat gives rise to the personal discretion in

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[230] Henry E. Hale, *Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective* (Cambridge: Cambridge University Press, 2015), https://doi.org/10.1017/CBO9781139683524.
[231] Shevtsova, *Russia--Lost in Transition*, 40.
[232] Yevgeny Minchenko, "Vladimir Putin's Big Government and the 'Politburo 2.0'" (Moscow: Minchenko Consulting Communication Group, 2013).
[233] Taylor, *The Code of Putinism*, 83–86.

economic policymaking, which normally takes the form of personal control over the resources with the aim of maximizing wealth for the rulers and the elite.[234] Control over key resources also helps the personalist ruler to address the increased demand of crafting new mechanisms for regime survival. Bueno de Mesquita et al. maintain that the redistribution of patronage rents, usually coming from energy exports, is the key tool at the leader's disposal.[235] Control over the resource rents "induces a strong norm of loyalty to the incumbent leader because such rents can be used as private rewards for coalition members."[236]

In response to the growing imperatives of the personalist regime, "Putin the Decider" made changes to the previous economic arrangement that was based on an equal partnership between state-market actors. The new political economy emerged under the personalist regime featured *dualistic* state capitalism with "state" and "market" sector; the state controlled the commanding heights of the economy, supposedly for the purpose of "modernization", while the economic sectors deemed not strategic were open to market forces. The only exception was for oligarchs that stayed in between, having a foot in both sectors. The new economic arrangement that reflected the personalized nature of the regime led some scholars to describe Putin as the CEO of Russia Inc.[237]

In this managed capitalism, every actor has a predefined role to carry out.[238] State intervention expanded from limiting its role to only rules and regulations, to having a missionary role in the "strategic" sectors of the economy such as oil, gas, finance, and heavy industries through aggressive intervention and direct ownership. Oligarchic businesses transformed from being an equal partner to becoming subordinate to the needs of the state. Being stripped of the political influence, oligarchic businesses in "strategic sectors" could keep functioning provided they stay loyal to the regime, aligning their business in line with Kremlin's overall direction. At the same time, they are required to "play an active role in helping the Kremlin to realize its political, economic, and social agenda, dipping into their coffers to subsidize Kremlin-approved

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[234] Geddes, Wright, and Frantz, *How Dictatorships Work*.
[235] Bruce Bueno de Mesquita et al., *The Logic of Political Survival* (Cambridge, MA, USA: MIT Press, 2003), 65–68.
[236] De Mesquita et al., "Policy Failure and Political Survival," 154.
[237] Treisman, *The Return*, 115; Hill and Gaddy, *Mr. Putin*.
[238] Philip Hanson, "The Turn to Statism in Russian Economic Policy," *The International Spectator* 42, no. 1 (March 1, 2007): 29–42, https://doi.org/10.1080/03932720601160336.

social programs."[239] At the "liberal" end of the state capitalism, the regime accepted that courts were necessary to a certain extent to assure entrepreneurial liberty, sanctity of contracts, private property rights, and competition. It is in the market sector that small businesses in manufacturing, trade, and retail could operate freely without being implicated by political battles in strategic sectors. Considering the small business to be not only the engine of economic growth and fiscal stability, but also a tool to prevent popular discontent, the state introduced various reforms to promote small business activities.

The aggressive expansion of the state through takeovers, both coercive and voluntary, became evident under Putin during his second term, demonstrated in table 6 below. It was manifested in several instruments through which state extended its hand over influential sectors of economy.[240] Namely, state expansion through 2005-2008 included major acquisition of companies by the state and consolidation of state ownership in strategic industries, banks and media, creation of vertically integrated state corporations and various investment funds, as well as the slowing down of privatization. The "strategic" industries included three sectors; 1) lucrative natural resources; 2) heavy industries; and 3) finance.[241]

Most prominent among them is the staggering number of oil-industry acquisitions by gas monopoly Gazprom and its affiliates during 2005–2007 as described in the figure below. In addition to the takeover of Yukos assets in 2004, the regime adopted a law to make the oil sector, as well as others, as being of "strategic" importance to Russia's interests. This gave the regime a pretext to revisit its position with both multinational oil companies and domestic oil tycoons.[242]

Intimidating state control was also observed in metal production, controlled by the oligarchs as well as the financial sector. Without controlling the metal sector, the Kremlin preferred to use its indirect control via persons loyal to the state's strategic goals. At the same

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[239] Peter Rutland, "The Oligarchs and Economic Development," in *Putin's Russia: Past Imperfect, Future Uncertain*, 4th edition (Lanham, Md. : Rowman & Littlefield Publishers, 2010), 169.
[240] Tompson, "Back to the Future?"
[241] Kari Liuhto, "Genesis of Economic Nationalism in Russia" (PEI Electronic Publications, Pan-European Institute, 2008).
[242] Cédric Durand, "Between Developmentalism and Instrumentalization: The Comeback of the Producing State in Russia," *Journal of Innovation Economics Management* n° 2, no. 2 (December 18, 2008): 171–91.

time, state banks gradually replaced the private banks and increased their share in the banking assets from 40% in 2000 to 60% in 2010.[243]

Figure 8.

Figure 9.

Another essential element of state expansion was the genesis of "state corporations" in Russia, a unique type of state company formed in order consolidate state-owned assets of over 400 companies in heavy industries that Putin invented to help strengthen state power and control over industry.[244] Among them was the establishment of important holding corporations, Rosoboronexport and Rosatom which, concentrating the heavy, arms, and nuclear industries under state arms, with the aim of increasing the competitiveness of Russian heavy industry.[245] Almost 13 percent of federal transfers, accounting for 2.3 percent of GDP, were direct transfers to state corporations. Following the takeovers and expansions, the share of SOE's in total Russian market capitalization increased from 24% to 40% from 2004 to 2007.[246] As of 2014, their share in total market capitalization accounts for 39%, the highest in OECD countries whose public sector various between 3% to 10%. The trend stopped after 2007 following the onset of the financial crisis which led the regime to order several state-owned banks to gain control over troubled financial institutions.

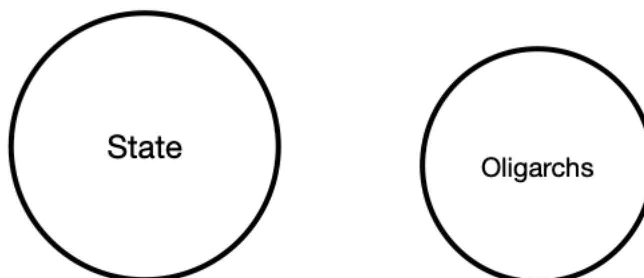
Unlike its counterparts, in Russian-style state capitalism the state sectors are not directly managed by ministries or agencies. Instead, the direction of the state sector falls into the personal fiefdom of "state oligarchs"; loyal friends Putin's, who controls the assets in the name of the regime; they sometimes make profits, navigating the harsh conditions of global capitalism, other times execute the state-mandated necessary social obligations, but never fail to enrich themselves. According to Treisman, nine members of Putin's inner circle have been in charge

[243] Andrei Vernikov, "The Impact of State-Controlled Banks on the Russian Banking Sector," *Eurasian Geography and Economics* 53, no. 2 (n.d.).
[244] Durand, "Between Developmentalism and Instrumentalization."
[245] Vadim Volkov, "Russia's New 'State Corporations' Locomotives of Modernization or Covert Privatization Schemes?" (PONARS Eurasia Policy Memo No. 25, IERES, George Washington University, 2008).
[246] David M. Woodruff, "The Expansion of State Ownership in Russia: Cause for Concern?" *Development and Transition*, no. 7 (2007): 11–13.

of state companies whose combined revenues accounted for 18% of GDP.[247] In summary, the regime that emerged under Putin's personalized rule strengthened his statist vision, joining political power with financial wealth and subordinating oligarchs to his power.

Table 6.

Figure 10. The power of oligarchs vis-à-vis the state in Russia after personalization of power



3.2.3 The embedded Putinism from 2012 to 2018

As Putin's two four-year terms were beginning to come to an end by 2008, the question of political succession was in the air. Faced with political intrigue around Kremlin, Putin took the bold step of naming new candidate for presidency, Dmitry Medvedev, the first deputy prime minister and a close friend of Putin from St Petersburg. After Medvedev easily won the presidency with 70 percent of the vote, Putin became prime minister, according to an agreement between them. This temporary sharing of executive roles between Putin and Medvedev came to be known as the "tandem ruling".[248] After this short interregnum, Putin decided to return to power in 2012 but this time he would face a new round of challenges, both domestically and internationally, that would require him to make several changes to his regime's governance. Two important events had a profound impact on the political economy during Putin's third presidency from 2012 to 2018: the outbreak of massive protests following the parliamentary election in 2011 and the increased confrontation with the West following the annexation of Crimea in 2014.[249]

[247] Daniel Treisman, "Putin's Silovarchs," *Orbis* 51, no. 1 (December 1, 2007): 141–53, https://doi.org/10.1016/j.orbis.2006.10.013.
[248] Andrew Monaghan, "The Russian Vertikal: The Tandem, Power and the Elections" (Russia and Eurasia Programme Paper, Chatham House, 2011).
[249] Gel'man, *Authoritarian Russia*.

Embedded Putinism: the politics of eternity and two modes of governance. Although a puppet in power given the constraints of the Putinist framework, Medvedev attempted to chart his own path by strengthening the institutions of the constitutional state against the "administrative regime" and conducting economic modernization throughout his presidency from 2008 and 2012.[250] However, Putin's informal but strong leverage on decision making was so strong that the reformist vision of statist liberal camp centered around the new president was rendered ineffective. On the contrary, the regime of two camps in tandem, siloviki and liberals, "disoriented the state apparatus, which escaped political leaders' control and… remained passive and demobilized."[251] In the face of state slackness, the risk of complete overhaul of centralized control, internal infighting of factions and ongoing protests, Putin decided to return to power and won the presidency with 63.2 percent vote in 2012. However, Putin's return to power further intensified the ongoing protests that erupted in response to the electoral fraud in the parliamentary elections in late 2011 by the citizens discontented by the deteriorating quality of life after the financial crisis.[252] The massive protests that spilled over the presidential elections in March 2012, were the largest since Gorbachev era and clearly demonstrated the frustration of the "enraged urbanites" of Moscow, including lawyers, doctors, and entrepreneurs over the political succession. The protests showed the regime that the rhetoric of 2000s, economic prosperity through the strong state, was no longer enough to win the support of the politically active middle class in major cities of Russia.[253]

In response to the fear of losing the legitimacy, the regime came up with new tactics. On one hand, the Kremlin started to use the classic method of co-opting the citizens, offering them increased salaries and benefits. On the other hand, it adopted several institutional changes that sanctioned the protests, labelled the NGO's as foreign agents, contained dissent and harassed the opposition through more repressive regulations of free speech and control over information and the internet.[254] Putin himself claimed that the protests were a part of deliberate

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[250] Richard Sakwa, *Putin Redux: Power and Contradiction in Contemporary Russia* (Routledge, 2014).
[251] Gel'man, *Authoritarian Russia*, 107.
[252] Graeme Robertson, "Protesting Putinism," *Problems of Post-Communism* 60, no. 2 (March 1, 2013): 11–23, https://doi.org/10.2753/PPC1075-8216600202.
[253] Karrie J. Koesel and Valerie J. Bunce, "Putin, Popular Protests, and Political Trajectories in Russia: A Comparative Perspective," *Post-Soviet Affairs* 28, no. 4 (October 1, 2012): 403–23, https://doi.org/10.2747/1060-586X.28.4.403.
[254] Gel'man, *Authoritarian Russia*.

scheme orchestrated by the West to destabilize Russian politics. However, such maneuvering further dissatisfied the urban middle class and put the regime into the corner, as reflected in drastic fall in Putin's popularity rating in 2013, the lowest since his ascend to power.

To regenerate active support to the regime while also neutralizing the emerging social forces, Kremlin unleashed another weapon in its arsenal; it replaced the old appeal of economic prosperity with the new one based on national pride, traditional values, and a sense of external threat.[255] Faced with a dire need of support for the regime amid economic downturn, Putin had to find a "serious mobilization project", similar to the war in Chechnya in early 2000 and Georgia in 2008 that gave a huge boost to his popularity.[256] Thus, he changed the basis of the regime's legitimacy from economic rhetoric to nationalist ideology, culminating in the annexation of Crimea, a part of sovereign Ukraine, in 2014.[257] As Guriev argued that in order to stay in power regime adopted new nationalist ideology at the expense of economy.[258]

The seizure of Crimea, which gave Putin an astronomically high approval ratings, almost 89 percent in 2015, invited a new era of confrontation with the West and a series of economic sanctions. This gave Putin a pretext to discard his role as a stabilizer and adopt new one as "savior and protector of a nation" against the external threat. Following the Crimean seizure, Putinism added two additional faces to its personalist dimension that hollowed out the formal institutions; *conservative* and *populist*.[259] Its *conservative* face does not only promote traditionalist social agenda, but also vilifies external hostile forces in order to maintain the status quo. As Oxenstierna argues, from his third presidency Putin 3.0 moved towards the renewed version of authoritarianism with doctrines that clearly signaled "Russia's intention to reclaim

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[255] Daniel Treisman, *The New Autocracy: Information, Politics, and Policy in Putin's Russia* (Brookings Institution Press, 2018), 5–15.
[256] Timothy Frye, Ora John Reuter, and David Szakonyi, "Hitting Them with Carrots: Voter Intimidation and Vote Buying in Russia," *British Journal of Political Science* 49, no. 3 (July 2019): 857–81, https://doi.org/10.1017/S0007123416000752.
[257] Leon Aron, "Putin versus Civil Society: The Long StruggLe for Freedom," *Journal of Democracy* 24, no. 3 (2013): 77.
[258] Leon Aron, "Putin's Russia: How It Rose, How It Is Maintained, and How It Might End," in *What's next for Russian Foreign Policy, Society, and Economy?* (Washington, D.C: American Enterprise Institute, 2015).
[259] M. Steven Fish, "The Kremlin Emboldened: What Is Putinism?" *Journal of Democracy* 28, no. 4 (October 7, 2017): 61–75, https://doi.org/10.1353/jod.2017.0066.

its position as a great power in the world."[260] In contrast, the *populist* emphasizes the crowd-pleasing efforts to curb excesses of liberal democracy such as equality of rights and feminism.

The regime based on embedded Putinism during this period started to present quite a different patter of politics and decision-making. The politics of embedded Putinism looked more like what Snyder calls as the "politics of eternity", which calls a constant reference to past greatness and manufacturing conflicts with external enemies to distract the people from domestic problems.[261] The politics of eternity then brought forth a hybrid nature of elite decision making in Russia; "normal politics" or "autopilot" and "manual control".[262] The normal politics involves many monotonous tasks of the state and subject to the formal deliberations and informal battles of different interests groups including, bureaucracy, business, parliament, and powerful individuals. Putin rarely takes stand in normal politics, leaving the matter for subordinates of different factions to sort out, provided that the infighting does not destabilize the regime. In contrast, manual control comes in when normal politics breaks down. It requires the "top-down dictation of actions" and falls to Putin himself. The important spheres of manual control exclusively preserved for Putin include foreign and energy policy. Normally manual control bypasses the formal state institutions and involves what Sakwa calls para-constitutional practices and surrogates.[263] In short, since his third presidency, the regime in Russia featured embedded Putinism based on the ideological mixture of three cores; centralization, personification, and idealization.

"Putinomics" in trouble: state capitalism as a tool to preserve embedded Putinism. In the economic realm, the high oil prices and days of economic glory that gave Putin the wind at his back in early 2000s were almost over. The global financial crisis in 2008 was a major blow to state-managed Russian economy and since then it could not return to high level of economic growth. Another round of turbulence that further weakened the exhausted economy came with the sanctions that the West imposed in response to Russian aggression in Ukraine in 2014 and

[260] Susanne Oxenstierna and Per Olsson, "The Economic Sanctions against Russia: Impact and Prospects of Success," *Nordisk Oestforum* 30, no. 1 (2015).
[261] Timothy Snyder, *The Road to Unfreedom: Russia, Europe, America* (New York: Tim Duggan Books, 2018), 1–15.
[262] Treisman, *The New Autocracy*, 36.
[263] Sakwa, "The Dual State in Russia."

the accompanying fall in oil prices in 2015.[264] President Putin himself stated that Western sanctions costed Russia $160 billion, while sudden drop in price of oil from around $110 in 2014 to $47 in 2015 severely exhausted the oil-dependent budget.[265] The impact of the economic slowdown also led to the loss of business confidence, which in turn caused a drop in investment and an increase in capital outflow.

The economic slowdown clearly demonstrated that Russian state capitalism which had promised economic modernization had in fact become "crony capitalism" in which powerful state oligarchs dominated the rent-producing industries such as oil & gas, metal, and banks at the *expense* of private market forces.[266] The economic slowdown further locked the economy into "rent addiction" where energy rents not only became the only source of economic growth, but it also had to prop up and invest in other inefficient rent-dependent sectors.[267] As a part of the anti-crisis program, for instance, 199 strategic yet inefficient companies, irrespective of the ownership structure, were selected for economic assistance, crowding out the efficient ones.[268] According to Russian economist Mau the economic recovery in 2014 recovered to its pre-crisis level "at the cost of a regression in the branch structure of economy: the extraction of raw materials exceeded pre-crisis levels by 5% and processed output exceeded pre-crisis levels by approximately 1%."[269]

In the face of these new challenges, the regime redesigned the economic priorities of state capitalism for the sake of impending threats to the stability. The new policies that further pushed the economy towards *dirigiste* were designed to address three main concerns necessary to maintaining the status quo; 1) maintaining elite cohesion amid decreased rents, 2) maintaining

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[264] Nigel Gould-Davies, "Russia, the West and Sanctions," *Survival* 62, no. 1 (January 2, 2020): 7–28, https://doi.org/10.1080/00396338.2020.1715060.
[265] Richard Connolly, "The Empire Strikes Back: Economic Statecraft and the Securitisation of Political Economy in Russia," *Europe-Asia Studies* 68, no. 4 (April 20, 2016): 753, https://doi.org/10.1080/09668136.2016.1156056.
[266] Simeon Djankov, "Russia's Economy under Putin: From Crony Capitalism to State Capitalism" (Policy Brief, Peterson Institute for International Economics, 2015).
[267] Clifford G. Gaddy and Barry W. Ickes, "Russia's Declining Oil Production: Managing Price Risk and Rent Addiction," *Eurasian Geography and Economics* 50, no. 1 (January 1, 2009): 1–13, https://doi.org/10.2747/1539-7216.50.1.1.
[268] Aslund, *Russia's Crony Capitalism*, 90–95.
[269] Vladimir Mau, "Between Modernization and Stagnation: Russian Economic Policy and Global Crisis," *Ekonomicheskaya Politika* 2 (2013): 10.

social stability through an increased spending spree and 3) securitization of the economy in order to insulate the main sectors while also searching for new income sources.[270]

One of the main concerns for the regime during the economic downturn was to maintain the support of the elite and important constituencies. Maintaining elite cohesion became gravely serious for Putin, especially after 2014 when the US Treasury targeted individuals for sanctions, namely Yury Kovalchuk, Gennady Timchenko and the Rotenburg brothers, all of whom close cronies of Putin.[271] Yet during the sanctions throughout 2015, Russia's leadership managed to channel resources to the politically connected regime supporters through mega-projects. The sanctioned cronies, for example, received lucrative construction contracts to build the pipelines for Gazprom, gas monopoly, in addition to the construction for the preparation of Sochi Olympics and 2018 World Cup, while state-owned companies successfully lobbied and tapped into the currency reserves stashed in the sovereign wealth fund.[272] In the same manner, the supporting constituencies of the regime benefited from increased government spending that aimed to raise pensions and public wages. Lastly, economic policies started to be defined by the security concerns in that the government emphasized the insulation of Russian economy from external threats. These security concerns required that the government might allocate the resources to sectors vital to national security at the expense of other sectors.[273]

Table 7. Characteristics of Putinist regime by 2010

	Democracy	Authoritarianism	Putinism
Leader	President or prime minister elected for a limited term	The party leader, presidential dictator for life, "the strong man"	Patronal president located at the executive, imbued with charisma, ruling with an inner circle based on loyalty

[270] Richard Connolly and Philip Hanson, "Import Substitution and Economic Sovereignty in Russia" (Research Paper, Chatham House, 2016).
[271] Oxenstierna and Olsson, "The Economic Sanctions against Russia: Impact and Prospects of Success."
[272] Orttung and Zhemukhov, "The 2014 Sochi Olympic Mega-Project and Russia's Political Economy."
[273] Connolly and Hanson, "Import Substitution and Economic Sovereignty in Russia."

Government	Party or coalition of parties, presidential administration	Appointment by the dictator, members of the family, or single party	Ministries divided up by siloviki, in charge of power ministries, technocrats, and experts in administrative structures and liberals in economic affairs
Separation of powers	Well-defined institutional division of power among branches with functions defined in the laws; the system of checks and balances	The absence of separation of powers; unrestrained executive or the party dominates the other branches	Real power belongs to the president along with factions in Kremlin with different orientation and interests
Economic system	Free market economy with limited state intervention; predominance of private business	Mixture of free market and state-led economy; key sectors of economy belong to ruling elite	Dualistic state capitalism

3.3 The economic and political transition in an independent Kazakhstan

The collapse of Soviet Union and the crumbling economy it commanded for decades forced the post-Soviet countries to find a new type of economic system that balanced between the state and the market. Exhausted by the deformities of the Soviet economy for years, the satellite countries in Central Asia, including Kazakhstan, embraced market economics as the antidote to development. This section describes the process of market liberalization in Kazakhstan following its independence and subsequent rollback under the personalized power of President Nazarbayev in early 2000.

The politico-economic foundation of Kazakhstan until independence. With its vast territory sharing borders with two superpowers, Russia and China, Kazakhstan is the largest country in Central Asia in terms of territory and with the population of 17 million ethnically diverse people. Historically speaking, Kazakh people, composed of different tribal groups, lived in the vast steppes of Central Asia without any predefined boundaries where they engaged in pastoral nomadism as their main economic activity. The gradual intrusion of Russian settlers to the territory in the eighteenth century led to the expansion of farming and commercial activities. It was after the Bolsheviks took power in Moscow that Kazakhstan, like other four countries in the region, was converted into a satellite republic under the Soviet Union in 1924.[274]

The traditional organization of economic and political life of people in Kazakhstan dramatically changed after the country became subject to Soviet rule.[275] As in other countries in the USSR, the management of the economy was conducted under the framework of the command economy where the state-enterprises in key industries such as mining, energy and foreign trade were controlled by the bureaucracy at both Union level and republic level.[276] At the micro-level, each enterprise had two-level supervisory systems whose interests usually clashed with each other; branch ministries of the republic and local committees of Communist Party. Although there was a certain leeway in administering lower tier enterprises, the republic developed a strong dependency on Moscow's central authority for enterprise management until the introduction Gorbachev's *perestroika* in 1980s that granted certain autonomy to enterprise managers.

The molding of the Kazakhstani economy to fit into the Soviet division of labor gave rise to certain consequences. The high degree of inter-republic economic integration meant that Kazakhstan only exported mineral resources along with a few agricultural products, while remaining dependent on the imports of consumer goods from other republics. Kazakhstan's main trading partner within the Union was the neighboring Russia; the exports of manufacturing

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[274] Olivier Roy, *The New Central Asia: The Creation of Nations* (NYU Press, 2007), 50–80.
[275] Richard Pomfret, *The Central Asian Economies Since Independence* (Princeton, New Jersey: Princeton University Press, 2006), 26, https://press.princeton.edu/books/hardcover/9780691124650/the-central-asian-economies-since-independence.
[276] Janos Kornai, *The Socialist System: The Political Economy of Communism* (Oxford University Press, 1992), 67–87, http://www.oxfordscholarship.com/view/10.1093/0198287763.001.0001/acprof-9780198287766.

production accounted for 60%, including oil and gas (53.4%), ferrous metal (over 80%) and chemical industry (55.4%), while imports of varying products stood at 50%.[277] As a significant amount of oil and gas produced in Kazakhstan was exported to Russia, the republic had a few refineries but which processed oil from Siberia rather than from the republic itself. The country was about to face dire consequences of this huge dependency after the Union disintegrated.

In the political realm, the current territory of Kazakhstan prior to the tsarist Russian conquest was a political confederation of three independent *hordes* that had a premodern system of governance with pastoral nomadic populations.[278] Unlike Tsarist Russia, Soviet Russia engaged in deliberate modernization, or Sovietization and social engineering of Kazakh society.[279] The first institutional change the Soviets carried out was the elimination of kinship-based local identities by dividing the country into the "state". Acquiring a titular nationality under the logic of "one ethnic group, one territory", Kazakhstan became the Kazakh Soviet Socialist Republic (SSR) in 1936.[280] The centralization of the Soviet system in Russia produced a parallel governing party and state apparatus in the republic; Kazakhstan had its own party structure, ranging from the Central Committee of the Communist Party of Kazaks SSR, headed by a first secretary, to the regional committee of Communist Party, to the lowest-level party cells.[281] Later on, Bolsheviks also promoted the local cadres under the policy of *korenizatsiya* (localization) to ensure the effectiveness of policy implementation. However, over the years of loosening oversight and slow rotation, local cadre politics became a breeding ground for patronage groups to amass significant power base. The patronage practice based on personal loyalty grew rampant in the party system during the Brezhnev era as the example of his protege, Dinmuhammad Kunaev, who was party chief in Kazakhstan from 1964 to 1986, can demonstrate.[282] However, when Gorbachev came to power with his sweeping reforms, the

[277] Yelena Kalyuzhnova, *The Kazakstan Economy: Independence and Transition* (UK: Macmillan Press, 1998), 30–40.
[278] Martha Brill Olcott, *The Kazakhs* (Hoover Press, 1995), 15–20.
[279] Gregory Massell, *The Surrogate Proletariat: Moslem Women and Revolutionary Strategies in Soviet Central Asia, 1919-1929* (New Jersey: Princeton: Princeton University Press, 1974).
[280] Pauline Jones Luong, *Institutional Change and Political Continuity in Post-Soviet Central Asia: Power, Perceptions, and Pacts* (Cambridge: Cambridge University Press, 2002), 65, http://ebooks.cambridge.org/ref/id/CBO9780511510199.
[281] Kathleen Collins, *Clan Politics and Regime Transition in Central Asia* (Cambridge University Press, 2006), 84.
[282] Dilip Hiro, *Inside Central Asia: A Political and Cultural History of Uzbekistan, Turkmenistan, Kazakhstan, Kyrgyz Stan, Tajikistan, Turkey, and Iran* (New York: Overlook Duckworth, 2009), 235.

corrupt party secretary Kunaev was first replaced by ethnic Russian Gennady Kolbin and then by native Kazakh, Nursultan Nazarbayev in 1989.

Independence and transition in post-Soviet Kazakhstan. The Soviet system started to crumble by 1992 as shock therapy reforms freed most of prices, leading to rampant inflation. Yeltsin's decision to take Russia out of defunct structure of the USSR in 1991 was the final nail in the coffin. With the collapse of the Soviet Union, the republics of Central Asia, including Kazakhstan become "accidentally" independent countries in 1991 despite their reluctance.[283] In the early years right after the independence, Nazarbayev, the new president of Kazakhstan who had to suddenly change his communist hat into a democratic on, was confronted with a triple crisis: reclaiming nationhood, restructuring the economy, and consolidating power within the new political structure.

The country was also on the verge of a possible internal conflict between ethnic Russians and Kazakhs while the economy was vulnerable as a result of its rupture from the rest of the Soviet empire upon which it largely depended.[284] By 1991 and following the *perestroika* reforms, Kazakhstan had inherited a moribund economy that suffered from falling economic output, a sharp rise in consumer prices, and ever-increasing shortages.[285] Despite the largesse of resources, the fate of the economy at large and particularly the oil industry was in a shambles with the fall of the Soviet Union.

At the beginning of its independence in 1991, Central Asian states faced three external economic shocks that compelled them to adapt market reforms; the dismantling of central planning, the dissolution of the Soviet Union and hyperinflation.[286] The end of the central planning created serious problems related to disorganization, which resulted in transitional depression.[287] In other words, disruptions in established trade links and difficulties in obtaining necessary inputs led to a breakdown in inter-republican economic relations. The dissolution of

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[283] Sally N Cummings, *Kazakhstan: Centre-Periphery Relations* (London; Washington, DC: Royal Institute of International Affairs; Distributed worldwide by the Brookings Institution, 2000).
[284] Olcott, *Kazakhstan*, 20.
[285] Myant and Drahokoupil, *Transition Economies*.
[286] Pomfret, *The Central Asian Economies in the Twenty-First Century*, 12.
[287] Olivier J. Blanchard and Class of 1941 Professor of Economics Olivier Blanchard, *The Economics of Post-Communist Transition* (Clarendon Press, 1997), 45.

the USSR and emergence of new national borders further exacerbated supply links and ultimately led to a decline in output.[288]

Another major breakdown was related to the currency system within the Union. All Central Asian countries suffered from a hyperinflation because they kept the ruble as a common currency in an attempt to maintain their existing trade links. Added to this was a high budget deficit that was partly the result of government's inability to raise taxes. According to Pomfret, inflation in Kazakhstan was running four digits until the government was able to control inflation below 50 percent with stabilization efforts in 1996.[289] A sharp drop in real output and increase in inflation led to a deterioration in living standards.

These external shocks were especially dire in Kazakhstan for three reasons.[290] First, the dissolution of the USSR ended direct transfers to Kazakhstan from Moscow. As a result, during 1991-1994, GDP decreased by around 60 percent. Second, the economy of Kazakhstan was closely connected with the neighboring republics of the USSR – as briefly mentioned above, in the wake of independence Kazakhstan's electrical grids, industrial plants, and oil refineries were entirely interlinked with Russia. Besides, until independence, about half of all oil produced was exported to Russia. Although the dissolution of the USSs provided Kazakhstan a chance to export its energy products, oil, and gas, to the world markets in real prices, the actual opportunity was constrained by country's dependence on the Russian pipeline network.[291] Finally, the central ministries had installed de facto control of 90 percent of industries in Kazakhstan, circumventing Nazarbayev's leadership as first secretary of the Communist Party of the Kazakh SSR.[292]

These external shocks intensified the internal debate about the future direction of the economy. In the face of possible collapse, Kazakhstan's leadership adopted a rapid reform strategy to construct a market-oriented economy. The government, being literally broke, had no option but to engage with the international community so that it could attract international

[288] Myant and Drahokoupil, *Transition Economies*, 60.
[289] Richard Pomfret, *The Central Asian Economies Since Independence* (Princeton, New Jersey: Princeton University Press, 2006), 52
[290] Sally Cummings, *Oil, Transition and Security in Central Asia* (Routledge, 2004), 33.
[291] Richard Pomfret, *The Economies of Central Asia* (New Jersey: Princeton: Princeton University Press, 1995), 55.
[292] Anne E. Peck, *Economic Development in Kazakhstan: The Role of Large Enterprises and Foreign Investment*, Central Asia Research Forum Series (London: Routledge Curzon, 2003), 60.

companies and their investment. Emphasizing an "economy first, politics second" approach, President Nazarbayev said "the market is democracy based on rigorous financial accountability."[293] In order to construct marketization, the leadership opted for neoliberal policies under the framework of price and trade liberalization, private ownership, and privatization, and reducing the role of the state in the economy. These market reforms meant that Kazakhstan could secure substantial investment for upgrading its pipelines and constructing alternative routes in order to increase oil production, a critical source to sustain independence. As Blackmon emphasized, the political considerations that emerged from the path dependency of the country's economic design influenced the pattern of economic development in Kazakhstan in the subsequent years of its transition.[294]

With the launch of these overwhelming sets of reforms, which is summarized above in table 8, Kazakhstan became the fastest reformer in Central Asia. Within a few years, the government freed consumer prices, liberalized the trade, and stabilized the budget. As the EBRD transition indicators showed, Kazakhstan came closest to establishing a market economy in the Commonwealth of Independent States (CIS) by early 2000. These market reforms are summarized in graph above. As Cummings noted, comprehensive market reform created "pockets of reliable business infrastructure, notably the banking sector, pension reform and foreign investment law."[295]

Among these policies, privatization and enterprise reform were the main components of the package which would institute private sector as the new engine of would-be market capitalism. This point was well recognized by Nazarbayev himself: "what the country needed to get the radical reforms up and running was a backbone of proprietors who would become engines of economic regeneration by saving the enterprises they had privatized and turning them into paying concerns. By transferring former state enterprises into private hands, we sought to free them from state management and intervention."[296]

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[293] Cohen, *Kazakhstan: The Road to Independence. Energy Policy and the Birth of a Nation*, 21.
[294] Pamela Blackmon, "Back to the USSR: Why the Past Does Matter in Explaining Differences in the Economic Reform Processes of Kazakhstan and Uzbekistan," *Central Asian Survey* 24, no. 4 (2005): 391–404.
[295] Cummings, *Oil, Transition and Security in Central Asia*, 28.
[296] Yilamu, Wumaier. "The Influence of Neoliberalism on Economic Liberalization in Post-Soviet Uzbekistan and Kazakhstan." In *Neoliberalism and Post-Soviet Transition*, ed. Wumaier Yilamu (London, Palgrave Macmillan, 2018), 99.

Table 8.

To accelerate enterprise restructuring, in 1992 the government adopted a three-pronged approach to privatize 37,000 state enterprises. Dividing these enterprises into categories based on size, the privatization program proceeded in three stages.[297] In first stage (1991-1992), housing and small-scale enterprises (up to two hundred workers) were sold at auctions for cash via coupons. The second stage (1993-1995) aimed to privatize medium-scale enterprises (up to five thousand workers) through public vouchers based on the Russian example; 10 percent of shares were given to worker collectives while citizens with vouchers could buy shares from 51% that the Investment Privatization Fund (IPFs) owned.[298] In the final stage, which lasted util early 2000, the government began to sell 250 large and 1,000 special politically-connected enterprises (over five thousand workers and in strategic sectors) that accounted for the core of the economy on a case-by-case basis.

The second and third stages of privatization become an epic story for Kazakhstan. The lack of transparency, corruption, and rapid haste with which the companies were sold made privatization "a sale of the century"; enterprises could be bid for and won in a few days.[299] Comparatively speaking, privatization was however quite different from its Russian counterpart. Unlike Russia, the government announced that it would experiment with putting shares of large enterprises to foreign investors through either management contracts, joint ventures, or outright sales. Nazarbayev himself emphasized the importance of foreign investment in effectively developing natural resources in Kazakhstan.

Foreign investors contracted or/and purchased 57 out of 94 big enterprises offered for sale during the second and third stages of privatization. The table below provides some detail of the large enterprises that generated some $7 billion for the government throughout 1995 and 1996.[300] Another important development was that in the desperate for cash, the government started to aggressively privatize enterprises in oil, gas, refining, mining, and non-ferrous

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[297] Kalyuzhnova, *The Kazakstan Economy: Independence and Transition*, 75.
[298] J Robert Brown, "Culture, Chaos, and Capitalism: Privatizatin in Kazakhstan," *Journal of International Law* 19, no. 4 (1998): 935–37.
[299] Anne E. Peck, "Industrial Privatization in Kazakhstan: The Results of Government Sales of the Principal Enterprises to Foreign Investors," *Russian & East European Finance and Trade* 38, no. 1 (2002): 31–58.
[300] Pomfret, *The Central Asian Economies Since Independence*, 54.

industries as the financial crisis deepened.[301] Newly appointed Prime Minister Kazhegeldin allowed investors to hold up to 100 percent equity in these enterprises. Vying for the pieces in lucrative industries, various international investors from United States, Canada, China, Japan, and Korea started taking over important assets in the country. However, compared to other sectors, the development of oil production and transportation became a major source of economic development and foreign investment.[302] Kazakhstan attracted the largest FDI per capita in the CIS, growing to an average of $1.8 billion 1995-2004, in which oil sector accounted for 80 percent. As a result, by 2000 almost 86% of oil production in the economy came from international oil companies, such as Exxon Mobil, Chevron, and Eni. Contracts for giant oil fields such as Tengiz, Kashagan, and Karachaganak were concluded as Production Sharing Agreements (PSAs).

This extensive privatization substantially altered the ownership structure of the economy with the share of the private sector rapidly increasing. By 1999, 75.6 percent of the "economy was already privatized, including 80.2 percent of small enterprises, 40.8 percent of medium enterprises, and 52 percent of large enterprises."[303] As a result, private sector share increased from 25 per cent of GDP in 1995 to 65 per cent in 2002. However, by early 2000, the government slowed the pace of privatization and held a major share in natural monopolies, including national oil & gas companies, railways, and pipelines.

As in Russia, the final phases of the privatization program in Kazakhstan were usually associated with the wealth accumulation of the elite, who would become the oligarchs of Kazakhstan. As observers claimed, the majority of fund managers who benefited from the cheap sale of state assets during privatization include Mukhtar Ablyazov of Astana Holding, who later became the minister of energy, industry, and trade, and Bulat Abilov of Butya Kapital. Unlike Russia where the state resources were captured by nascent "capitalists", in Kazakhstan the elite of political regime - loyal friends, young businessman, family members, and old allies - dominated the economic resources.[304] Nazarbayev himself stayed on top by being the chief, as

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[301] Olcott, *Kazakhstan*, 139.
[302] Anders Aslund, *How Capitalism Was Built: The Transformation of Central and Eastern Europe, Russia, the Caucasus, and Central Asia*, 2nd ed. (Cambridge: Cambridge University Press, 2012), 79, https://doi.org/10.1017/CBO9781139207850.
[303] Olcott, *Kazakhstan*, 137.
[304] Jonathan Murphy, "Illusory Transition? Elite Reconstitution in Kazakhstan, 1989 – 2002," *Europe-Asia Studies* 58, no. 4 (June 1, 2006): 523–54, https://doi.org/10.1080/09668130600652092.

the case of Kazakhgate scandal showed. Bohnenberger shows that providing access to resources through privatization was important to establish and control the elite network, who, being loyal to Nazarbayev, would dominate the decision-making in the country.[305] Describing the process as "the robbery in the daylight", Olcott documents several cases of dubious privatization that seemed to have benefited both regime insiders, Nazarbayev himself, and his family members.[306]

3.4 The rise of the president Nazarbayev and consolidation of power in independent Kazakhstan

Narratives of the Kazakhstani regime and its trajectory after independence without a reference to the personality of president Nazarbayev would be incomplete. Following independence in 1991, the Kazakh regime did not differ in its trajectory from other neighboring Central Asian countries: "dominated by nominally elected, yet effectively authoritarian president."[307] Although it flirted with the idea of democracy and political participation in the early years of the transition, over the years the country ended up being like a family run business under Nazarbayev.

Born in a village near the former capital Alma Ata in 1940, Nursultan Nazarbayev worked at metallurgical complex before transforming into a full-blown communist apparatchik. Using his bureaucratic skills and the patronage necessary to grow in the party ranks, Nazarbayev become prime minister at the age of forty-four.[308] In 1989 he succeeded ethnic Russia Gennady Kolbin as the first secretary of CP. With independence, the elected deputies of the Supreme Soviet named him to the post of the newly created presidency in 1991 in which he received 98 percent of vote.[309] Upon becoming the new leader, he faced the task of building new political institutions conducive to maintain his precarious power.

Though the republic gained independence in 1991, the first constitution was only adopted in January 1993. According to the new constitution, the government was divided into

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[305] Simone Bohnenberger-Rich, "China and Kazakhstan: Economic Hierarchy, Dependency and Political Power?" (PhD dissertation, London School of Economics and Political Science (LSE), 2015), http://etheses.lse.ac.uk/3126/.
[306] Olcott, *Kazakhstan*.
[307] David Isao Hoffman, "Oil and State-Building in Post-Soviet Azerbaijan and Kazakhstan" (PhD dissertation, Berkeley, University of California, 2000), 239, http://adsabs.harvard.edu/abs/2000PhDT.......227H.
[308] Sally Cummings, *Kazakhstan: Power and the Elite*, 1st edition (London: New York, I.B. Tauris, 2005), 14–20.
[309] Olcott, *Kazakhstan*, 28.

three branches, executive, unicameral legislative and judiciary. The office of presidency gained a political supremacy over the other branches with the aim of establishing concentrated power and furthering the economic reform. Nazarbayev aimed at centralizing the control over the territories by appointing the regional governors. However, there was an element of plurality with the political opposition that resulted from the formation of multiple parties. Luong claims that over the years, political contestation among three important actors, executive, regional leaders, and deputies in the Soviet, a created a managed democracy where the elite somehow attempted to put barriers on the political activity that proliferated after the independence.[310]

Table 9.

The balance started to tilt towards the presidency when a power struggle began between the executive and legislative over the course of economic reform in 1993, just like Yeltsin's Russia. Although Nazarbayev and his advisors in the presidency advocated the shock-therapy style reform similar to the one Russia adopted, the deputies, who had garnered enough political ambition and stakes in state enterprises, deliberately resisted the reform as a result of growing popular disenchantment with the flailing economy. As Olcott argues, they did not oppose the reform because “they distrusted the institution of private property, but because they objected to the abuses of the allocation process.”[311]

Claiming that the legislature obstructed the reform, Nazarbayev ordered the democratically elected Supreme Soviet to “voluntarily” dissolve itself in 1993. In the meantime, the interim parliament delegated its power to the executive where Nazarbayev ruled by presidential decrees until the new parliament was formed in 1994.[312] He wanted to make the parliament rubber stamp for economic reform: the new parliament consisted of officials in state or partially privatized organizations along with freshman with no political experience. However, an accord between Nazarbayev and parliament ended when the constitutional court decided to invalidate the 1994 parliamentary elections in 1995, allegedly pressured by Nazarbayev himself.

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[310] Pauline Jones Luong, *Institutional Change and Political Continuity in Post-Soviet Central Asia: Power, Perceptions, and Pacts* (Cambridge: Cambridge University Press, 2002)
[311] Olcott, *Kazakhstan*, 22.
[312] Sally Cummings, *Power and Change in Central Asia* (Routledge, 2001), 64.

The court ruling gave Nazarbayev an opening to redefine the constitution of the country and avoid upcoming presidential elections in 1995. His argument was that "without such a consolidation, Kazakhstan would fail to develop the legal infrastructure necessary to secure private property and attract foreign investment."[313] For Nazarbayev, Kazakhstan needed to be a strong presidential republic because it lacked a parliamentary culture and traditions and a well-developed multiparty system. As a result, two consecutive referenda were held; first, with 95.8 percent approval, allowed the president to extend his rule by 2000, while the second produced a new constitution that gave him more power.[314]

By 1995, the pro-Western democratic romanticism was over. [315] The second constitution in 1995 expanded the president extensive powers at the expense of other independent bodies, including the media. Maintaining a nominal separation between the branches, it effectively turned the now-bicameral legislature a passive consultative body in which the president mainly initiated legislation. With this expanded power, the president could dissolve the parliament at a whim and appoint a deputies and senators.

Although the institutional design granted an upper hand to the president, it was not until early 2000 that Nazarbayev could firmly consolidate his power. During the transition years, Nazarbayev had to share the power with the supporters of regime through co-optation, many of whom retained their position of power after independence.[316] According to Isaac, the use of informal political practices, or the patronage, early in the transition years helped Nazarbayev consolidate his formal power.[317] The early regime coalition that came to occupy the power structures along with economic positions basically consisted of three intertwining players: ex-communist apparatchiks (Nazarbayev's Soviet era allies), family members of Nazarbayev, and young businessmen.[318] In this new regime, which Masanov call as a 'protectorship–client'

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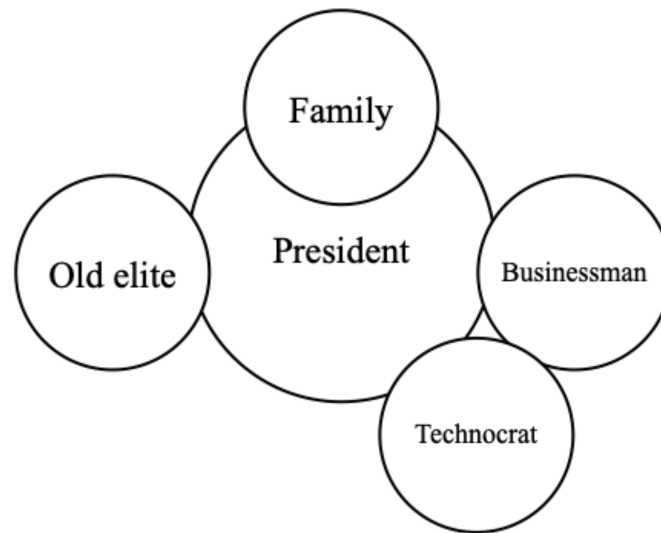
[313] Olcott, *Kazakhstan*, 21.
[314] Annette Bohr et al., "Kazakhstan: Tested by Transition" (London: Chatham House Royal Institute of International Affairs, 2019), 10–15.
[315] Jürgen Wandel and Botagoz Kozbagarova, "Kazakhstan: Economic Transformation and Autocratic Power," SSRN Scholarly Paper (Rochester, NY: Social Science Research Network, July 15, 2009), 6–7, https://papers.ssrn.com/abstract=1434522.
[316] Dosym Satpaev, "An Analysis of the Internal Structure of Kazakhstan's Political Elite and an Assessment of Political Risk Levels," in Uyama Tomohiko (ed.) *Empire, Islam, and Politics in Central Eurasia* (Slavik Research Center, Hokkaido University, 2007).
[317] Rico Isaacs, "Informal Politics and the Uncertain Context of Transition: Revisiting Early-Stage Non-Democratic Development in Kazakhstan," *Democratization* 17, no. 1 (2010): 1–25.
[318] Murphy, "Illusory Transition?"

system, Nazarbayev maintained political power through a "series of dyadic and interconnected patron–client relationships."[319] In this patronal politics, it is informal networks that wields actual power and engage in competition for access to resources. The role of Nazarbayev was to serve as main arbitrator in the competition over assets by the patronage networks, as described below in figure 11.

Figure 11. The elite groupings in Kazakh regime under Nazarbayev by 2004



The former communists who were close to Nazarbayev became the presidential inner circle, securing for themselves successful positions around lucrative economic sectors. The family included his daughters and sons-in-law, Rakhat Aliev, a surgeon, and Timur Kulibaev, the son of Nazarbayev ally. The family came to dominate the media, finance, and energy industry in the name of Nazarbayev, as next chapters describe in detail. The businessmen were relatively young newcomers with engineering backgrounds who became wealthy after privatization and oscillated between government and business over the years. These include academic-turned businessman Mukhtar Ablyazov, who, having made his fortunes in finance,

[319] Rico Isaacs, "Nur Otan, Informal Networks and the Countering of Elite Instability in Kazakhstan: Bringing the 'Formal' Back In," *Europe-Asia Studies* 65, no. 6 (2013): 1055–79.

went to become Minister of Energy, Industry and Trade, and Karim Masimov who headed the Halyk Bank for some time and became Deputy Prime Minister.[320]

3.5 A challenge to personalization of power and rising economic nationalism under Nazarbayev: 1998–2005

The firm foundation of a market economy and political institutions led Nazarbayev to believe in the stability of the new political system. However, such optimism was to be short-lived; in 2001, Nazarbayev faced a serious political challenge to his power from insiders who defected from the regime.[321] The source of renewed political contention came from the disgruntled bourgeoisie and political class that emerged an unintended side effect of the economic policies launched during early transition.[322] As mentioned above, the economic transformation and subsequent prosperity bred new members of the wealthy elite who had benefited enormously from privatization. Although these elites were fortunate to gain access to resources for cheap, over time they started to increasingly feel that political power and economic resources were being monopolized in the hands of the presidential family at the expense of other business groups.[323]

The cross-cutting political feud came to the fore during early 2000s when the president's son-in-law, Aliev used his position at the Committee for National Security (KNB) to subdue other businesses. Aliev wanted to take over the businesses of influential oligarch and former energy minister Mukhtar Ablyazov in finance and media, including Bank Turan Alem (BTA), which was a major competitor to the family's bank.[324] Another incident that fueled the confrontation was the auction in which Halyk Bank was sold not to public contender Ablyazov's investment group, but to latecomer Aliev's financial group. Failing to act as an intermediary, Nazarbayev publicly lent his support to his son-in-law, sending a warning the businessman. This further exacerbated the grievances, expressed by entrepreneur Bulat Abilov, who once

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[320] Murphy, "Illusory Transition?"
[321] Gregory Gleason, *Markets and Politics in Central Asia* (London: Routledge, 2003), 62.
[322] Junisbai and Junisbai, "The Democratic Choice of Kazakhstan."
[323] Alima Bissenova, "Growing Prosperity in Kazakhstan Creates Pressure for More Open Political System | Eurasianet," *EurasiaNet*, 2002, https://eurasianet.org/growing-prosperity-in-kazakhstan-creates-pressure-for-more-open-political-system.
[324] Barbara Junisbai, "Improbable but Potentially Pivotal Oppositions: Privatization, Capitalists, and Political Contestation in the Post-Soviet Autocracies," *Perspectives on Politics* 10, no. 4 (2012): 891–916.

failed to participate in the privatization of lucrative metallurgy complex: "The family-clan driven economy, built with your participation and supervision hinders not only the development of business but the entire Kazakhstani society… It is because of your policies that our nation's wealth, its best industrial enterprises, were unfairly transferred to so called "investors" with shadowy biographies!"[325]

Within the existing system, the dissatisfied elite came to understand that the main threat to their economic interests was the power of the family which arbitrarily decided the fate of entrepreneurs. These elites were prevented from participating in the most lucrative sectors of the economy, such as oil, metallurgy, banking, and communication because they those had been appropriated by the president's family and inner cycle. In response, 19 important business and political figures came together to establish a pro-reform opposition party, the Democratic Choice of Kazakhstan (DCK) in 2001. The masterminds included Mukhtar Ablyazov, Bular Abilov (director of Butya-Kapital investment company), Galymzhan Zhakiyanov (co-founder of the Semey financial-industrial group and former governor of Pavlodar region), and Nurzhan Subkhanberdin, (chairman of the Kazkommertsbank investment conglomerate with largest bank in Central Asia).[326] The driving force behind the DCK's was a demand to create meaningful political reform that would ensure a commitment to the rule of law and decentralization of political authority in the face of growing monopolization of power under single autocrat and his family.[327] Having previously benefitted from economic spoils, they now wanted to have access to political power and decision making so that they could protect their business interest and maintain their economic status. Interestingly, the DCK animated the tense political environment in the country, reinvigorating scattered activities of previous oppositions parties like the National Congress, Azamat, and former Prime Minister Akezhan Kazhegeldin's Republican Party.[328] All together, they formed a new alliance the United Democratic Party (UDP).

[325] Junisbai and Junisbai, "The Democratic Choice of Kazakhstan."
[326] Simone Bohnenberger-Rich, "China and Kazakhstan: Economic Hierarchy, Dependency and Political Power?" (PhD, London School of Economics and Political Science (LSE), 2015), 45, http://etheses.lse.ac.uk/3126/.
[327] "Political Freedoms in Kazakhstan," Human Rights Watch (Washington, D.C: Human Rights Watch, 2004), https://www.hrw.org/node/255591/printable/print.
[328] Alima Bissenova, "Kazakh Opposition Eoverplays Its Hand, Faces Repression" (Analytical Articles, The Central Asia-Caucasus Analyst, 2002).

Developing a new program, "Kazakhstan without Nazarbayev", the DCK attracted prominent figures that include governors, ministers, and oligarchs.

Facing this domestic challenge, Nazarbayev immediately took "strict measures" to neutralize the dissidents who might destabilize the country.[329] He then reasserted control by dissolving the movement and jailing the perpetrators. The main instigators, Mukhtar Ablyazov and Galymzhan Zhakiyanov, along with several other businessman and ministers, were arrested with the charge of embezzlement, abuse of power and corruption in 2002. Another victim was Nurzhan Subkhanberdin, whom the presidential advisor described as 'Kazakh Khodorkovsky', in reference to the Russian oligarch jailed by Putin in 2003.[330] Although the regime did not launch an outright expropriation of assets of the oligarchs, officials raided Kazkommertsbank and BTA with a tax audit and forced to pay millions, similar to Russian case. Also, similar to Putin, Nazarbayev made clear that business leaders would no longer meddle or 'interfere' in politics. Ablyazov was later released on the condition that he would stay out of politics and eventually became head of BTA again until his second falling in 2008.[331] Following the no-politics warning, several businessmen who supported the cause also immediately renewed their allegiance to the regime. Successfully responding to the challenge of outsiders, the old elite once more strengthened their muscle in the political and economic assets of resource-rich Kazakhstan.

The domestic challenge was soon followed by the color revolution in neighboring Kyrgyzstan in 2005 that toppled the incumbent president.[332] Increasingly alarmed by compounding challenges, Nazarbayev conducted an important restructuring of the regime that allowed him to take full control over the political sphere while personalizing his power. In the new arrangement, Nazarbayev started to rule the country through a combination of formal and informal mechanisms, which included institutional manipulation and personalization based on patronage.[333]

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329 Bissenova.
330 Murphy, "Illusory Transition?," 547.
331 Liz Fuller, "What Caused The Second Downfall Of Mukhtar Abliyazov?," *RadioFreeEurope/RadioLiberty*, 2009, https://www.rferl.org/a/What_Caused_The_Second_Downfall_Of_Mukhtar_Abliyazov/1499164.html.
332 Valerie Bunce and Sharon L. Wolchik, "Debating the Color Revolutions: Getting Real About 'Real Causes,'" *Journal of Democracy* 20, no. 1 (2009): 69–73.
333 Cummings, *Power and Change in Central Asia*, 168.

To be more precise, the changes took two forms. First, the regime pushed back by restricting independent media, NGOs, and political parties. With the presidential election approaching in 2005, the regime also cracked down several opposition members, several of whom were found dead.[334] Furthermore, an important institutional change was the reestablishment the party of power, "Nur Otan", to mitigate elite fragmentation amid the increasing influence of the presidential family.[335] The main purpose of the party was to minimize the ability of independent actors to challenge the regime by providing wider homogeneity in state apparatus and concentrating political supporters in a single institution.[336] In other words, the regime reconsolidated power by complementing informal patronage relations with the formal institution of a party that absorbed the existing movements. As result, Nur Otan dominated parliamentary elections in 2004, leading a way towards strong presidential election scheduled in 2005.

Second, the domestic challenge by the business elite was followed by a reconfiguration of the elite groups through informal mechanisms of patronage. The important financial-industrial group that wielded important power around the personality of the president involved the inner circle, outer circle, and distant circle. The latter two groups, the inner and outer circles, are formed from a "wide strata of oligarchic or regional rent-seeking actors, acting together with or in place of governmental institutions primarily via client-based networks of patronage and pork barrel rewards."[337] More specifically, the inner circle is made up of: 1) the presidential family members, including daughters, sons-in-law and brothers; 2) president's companions, the group that is located within the proximity of presidential administration, and 3) personal proteges, technocrats, professionals and high-level officials appointed by the president.[338]

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[334] Cohen, *Kazakhstan: The Road to Independence. Energy Policy and the Birth of a Nation*, 40–50.
[335] Davor Boban, "The Presidential-Hegemonic Party and Autocratic Stability: The Legal Foundation and Political Practice in Kazakhstan," *Zbornik Pravnog Fakulteta u Zagrebu* 67, no. 1 (March 6, 2017): 66–70.
[336] Isaacs and Whitmore, "The Limited Agency and Life-Cycles of Personalized Dominant Parties in the Post-Soviet Space."
[337] Anja Franke, Andrea Gawrich, and Gurban Alakbarov, "Kazakhstan and Azerbaijan as Post-Soviet Rentier States: Resource Incomes and Autocracy as a Double 'Curse'in Post-Soviet Regimes," *Europe-Asia Studies* 61, no. 1 (January 1, 2009): 113, https://doi.org/10.1080/09668130802532977.
[338] Satpaev, "An Analysis of the Internal Structure of Kazakhstan's Political Elite and an Assessment of Political Risk Levels," 268.

The members of inner circle close to the president came to control the lucrative sectors of economy including oil and gas industries. They came to penetrate other sectors of the economy, including banking, metallurgy, and communications. Although they are permitted to do gain wealth through business, the business elite in outer circle was denied an entry into the lucrative sectors controlled by the inner circle; they pulled out of politics that might damage their business interest.[339] This means that there is an informal and tacit pact among these three groups to which the outer and distant circles are expected to abide by as the rules of the game. The figure 12 below illustrates the important members of family, inner circle, and outer circle.

In short, as a consequence of elite fragmentation that threatened regime stability, Nazarbayev came to preside over a personalist political system where he plays the role of guarantor of elites' privileged access to resources and final arbiter to whom elites appeal when serious conflict arises between the circles.[340] In this personalist regime, only the ruler that is able to align the competing interests of the elite, can maintain the stability of the his regime because the elite might at any time cooperate to oust the ruler. To suit the political system to the whims of president, Nazarbayev came to rely on extensive patronage networks in which personal loyalty is given to the sole patron "who distributes administrative status and financial resources to his subordinates in accordance with his or her own strategies of promotion."[341]

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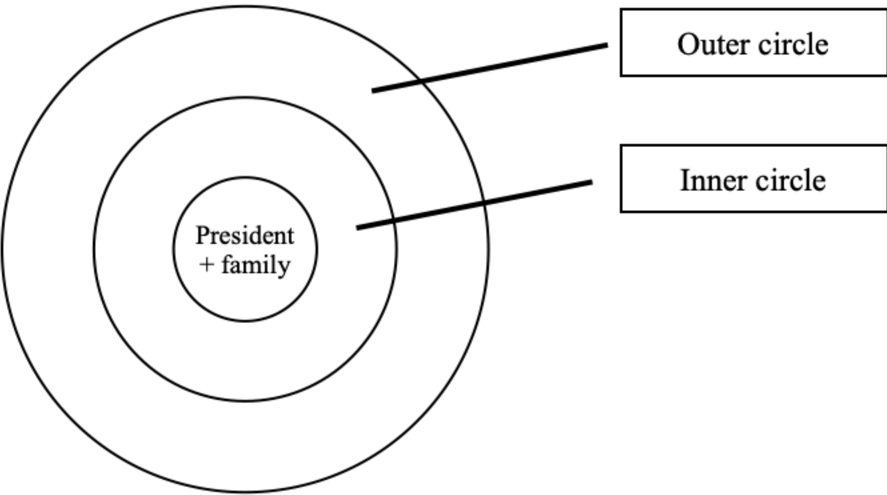
[339] Barbara Junisbai, "A Tale of Two Kazakhstans: Sources of Political Cleavage and Conflict in the Post-Soviet Period," *Europe-Asia Studies* 62, no. 2 (March 1, 2010): 235–69, https://doi.org/10.1080/09668130903506813.
[340] Marlene Laruelle et al., *Kazakhstan in the Making: Legitimacy, Symbols, and Social Changes*, Reprint edition (Lexington Books, 2016), 10–20.
[341] Peyrouse, "The Kazakh Neopatrimonial Regime," 345.

Figure 12. Formation of elite groupings around Nazarbayev



The rise of economic nationalism. Feeling threatened by domestic challenges, Nazarbayev began to seriously redefine the relationship between political authority and other economic actors; he came to realize that "the oligarchs possess enough revenues to guarantee them political autonomy, which…could be used against the president as the strong man of the country and against his family as an economic actor."[342] In a speech at the newly elected parliament's opening session on November in 2004, Nazarbayev vilified the oligarchs as having monopolized the economy. He said that "about 10 mega-holdings…control more than 80 percent of the Kazakhstani economy…they…are against the appearance of competitors…obstacles for the development of small and mid-size business."[343] He went on to say that after collecting money and strength, the oligarchs will "start to strive for power". Thus, the logical response of Nazarbayev was to strengthen the state control over the important assets of the economy for the sake of regime stability. The rise of state assertiveness came to manifest itself in two changes; 1) espousing economic nationalism in energy sector in early 2000s and 2) installing state (read: family) control over strategically important and large state companies.

Table 10.

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[342] Peyrouse, 345.

[343] Ibragim Alibekov, "Nazarbayev Seeks to Close Kazakhstani Political Sphere by Opening Economy," *Eurasianet*, 2004, https://eurasianet.org/nazarbayev-seeks-to-close-kazakhstani-political-sphere-by-opening-economy.

The onset of economic nationalism in the energy sector stemmed from both domestic political evolutions and presence of foreign companies. On one hand, Nazarbayev understood that maintaining the stability of his regime, building up his patronage system, and ultimately asserting political legitimacy would be impossible if not for the ample wealth beneath Kazakhstan's soil. The natural resources rent, particularly the hydrocarbon windfall, was manna from the heaven for the ailing economy of Kazakhstan after the collapse of Soviet Union. The president knew that oil wealth would be the primary source of government revenue and would be the spoils for the patronage network he was about to build for his consolidation of power.

However, to reap the full oil bonanza, Nazarbayev first had to ensure a firm grip on the industry which was dominated by international companies after independence. So, the regime's attempted to increase its control over the commanding heights through state ownership or the switch to "managed capitalism", starting with so-called resource nationalism. With oil prices rising and the state gaining some capacity, the regime now started to view the presence of international oil companies as a possible challenge to power.[344] The overall mood among the political elite was that "shock therapy weakened the authority of the state and its ability to command its own resources" and "handing foreign investors overly favorable conditions, enabled "foreign interests" to influence local political life".[345] According to Domjan and Stone, resource nationalism in Kazakhstan after 2004 took three forms; increasing the state control of the industry through single entity, KazMunaiGaz (KMG) national oil company that was under president's personal control, putting more pressure on international oil companies through legislative and regulatory measures, and increasing state ownership in major oil projects.[346]

The legislative campaign against targeting international companies first came in the form of new tax reform, increased loyalty, and new obligations to support domestic businesses through local content strategy.[347] As well noted, foreign companies were rebuked for failing to

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[344] Adil Nurmakov, "Resource Nationalism in Kazakhstan's Petroleum Sector: Curse or Blessing?" in Indra Overland (ed.) *Caspian Energy Politics: Azerbaijan, Kazakhstan and Turkmenistan,* Caspian Energy Politics: Azerbaijan, Kazakhstan and Turkmenistan. - London [u.a.]: Routledge, ISBN 0-415-69320-9. - 2010, p. 20-37 (London: Routledge, 2010).
[345] Peyrouse, "The Kazakh Neopatrimonial Regime," 352.
[346] Domjan and Stone, "A Comparative Study of Resource Nationalism in Russia and Kazakhstan 2004–2008."
[347] Serik Orazgaliyev, "Nationalization and the Role of National Oil Companies: The Case of Kazakhstan," in *Reforming State-Owned Enterprises in Asia: Challenges and Solutions*, ed. Farhad

subcontract to local companies. In addition, the government passed a law on PSA which strengthened the position of KMG by guaranteeing its right to a 50% stake in upcoming projects.[348] Thanks to its preemptive rights, Kazakhstan has increased its share in the energy sector since 2005 and consolidated certain assets under national oil company KMG.

In 2003, there were increasing discussions regarding the new trend where nascent Kazakh oil companies started to purchase assets previously owned by foreign investors.[349] The most notable example was related to PetroKazakhstan (formerly named as 'Hurricane Hydrocarbons' from Canada), the sixth largest oil company in the country with major assets. In short, the rebellion began when PetroKazakhstan not only refused to provide subsidized oil to be used in agriculture, but also heavily criticized the government for a lack of transparency. The company soon found itself surrounded by an array of charges and lawsuits on environmental grounds. As a result, the company was forced out of market in 2005 and the government, after negotiating with a prospective buyer, the CNPC, bought 33 percent of the shares in PetroKazakhstan and 50 percent of the shares in the Shymkent oil refinery, the largest in the country.[350]

The regime employed a plot scheme to acquire Karazhanbas, another company with an output of 50,000 barrels per day and 400 million barrels of reserves. During privatization, 94.62% of Karazhanbas was bought from the government by a Canadian company, Triton-Vuko Energy Group (or Nations Energy Company). When Nations Energy Company decided to sell its assets in Kazakhstan to Chinese company CITIC Group, the government intervened and bought Energy Company in partnership with CITIC. As a result, KMG emerged as second leading oil producer by 2008, owning about 30% of production and about 40% of proved reserves in Kazakhstan.[351] Resource nationalism and takeovers also continued until the 2010s, as will be discussed in the next section.

Taghizadeh-Hesary et al., ADB Institute Series on Development Economics (Singapore: Springer, 2021), 323–41, https://doi.org/10.1007/978-981-15-8574-6_16.
[348] Ostrowski, *Politics and Oil in Kazakhstan*, 120.
[349] Ryan Kennedy and Adilzhan Nurmakov, "Working Paper: Resource Nationalism Trends in Kazakhstan, 2004–2009" (Fridtjof Nansen Institute, 2010).
[350] Orazgaliyev, "State Intervention in Kazakhstan's Energy Sector."
[351] Kennedy and Nurmakov, "Working Paper: Resource Nationalism Trends in Kazakhstan, 2004–2009."

Scholars emphasize that what seemed to be increasing state control in economy was a deliberate strategy of Nazarbayev to balance state and market forces and enhance the industrial development of Kazakhstan.[352] According to this peculiar way of development that imitates "Asian tigers", industrial development can only happen when active state involvement guides market forces. In fact, Nazarbayev laid out such developmental ambition first in 1997 the document labeled as "Kazakhstan 2030: Prosperity, Security and Ever-Growing Welfare of All the Kazakhstanis" and later in "Strategic Plan of Development".[353] In 2006, the program was renewed as "The Strategy for Kazakhstan to Become One of the Top 50 Most Competitive Countries in the World". Both documents outline the perfect formula of how the market can complement state interference.

According to the blueprints, establishing a free-market economy that can create conditions for business and attract foreign investment must be the priority. Yet, the importance of state role in economic affairs should not be forgotten; in fact, it maintains that the state is "the only actor able to be an "engine" of rapid industrial modernization and innovation, while the private sector is not yet strong enough to invest long-term in hi-tech industries."[354] The creation of around 30 national champions, including KMG, was an important step to realize the goals of increasing country's competitiveness and providing an industrial foundation to important sectors. For this, the government established several institutions that would drive an economic development: the Development Bank of Kazakhstan in 2001, the Investment Fund of Kazakhstan in 2003, and the National Innovation Fund in 2004.[355] In 2006, the president radically expanded the scope of its developmental strategy with the aim of "transforming Kazakhstan into one of the "50 most competitive, dynamically developing countries in the world" within a decade. The program included the creation of additional institutions, the "Samruk" state-holding company and the "Kazyna" sustainable development fund, which next chapter

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[352] Cohen, *Kazakhstan: The Road to Independence. Energy Policy and the Birth of a Nation*.
[353] Richard Pomfret, "Kazakhstan's 2030 Strategy: Goals, Instruments and Performance" (American Economic Association Annual Conference, Philadelphia, 2013),
[354] Ailuna R. Utegenova, "Kazakhstan's 2030 Development Strategy: Significance and Results," in *OSCE Yearbook 2010*, ed. Institute for Peace Research and Security Policy at the University of Hamburg / IFSH (Nomos Verlagsgesellschaft mbH & Co KG, 2011), 137, https://doi.org/10.5771/9783845229584-133.
[355] Richard Pomfret, "Kazakhstan's 2030 Strategy: Goals, Instruments and Performance" (American Economic Association Annual Conference, Philadelphia, 2013),

will discuss in more detail. In short, the regime's attempt to blend the state control with a market economy following the domestic challenge created the foundation for the state capitalism.

3.6 The embedded personalism and dualistic state capitalism under Nazarbayev: 2007-2016

It was not until the early 2010s that the Kazakh regime successfully completed the creation of a new politico-economic order, dualistic state capitalism. The end of first decade of the 2000s marks two important events that prompted the regime to take drastic actions to increase state control over the economy. The first is concerned with increasing tension among factions that the Kazakh regime confronted over the internal balance of power and succession, while the second is related to the devastating impact that the 2008 financial crisis brought upon the Kazakh economy.[356]

The major triggering event that led Nazarbayev to put his hand fully over the economy came from within the presidential family, sparked a power struggle at the higher echelon of power was Rakhat Aliev who was married to Dariga, a daughter of Nazarbayev.[357] Aliev had served as head of tax policy and he had collected compromising material on the elite in Kazakhstan.[358] After disseminating some sensitive materials, the president reassigned him to be deputy chief of the Committee for National Security and Deputy Foreign Minister. As mentioned above, during the early 2000s, Aliev abused his position and exerted pressure on various businesses, causing intra-elite strife in the country. By the early 2000s, Aliev, along with his wife Dariga Nazarbayeva, were de facto owners of several private banks, held shares of a private oil company, and directed an extended media empire and TV channels.[359]

Aliev soon started to show political ambitions and sought increasing control over administrative and financial resources.[360] As a way to offer concessions to the young business elite and sideline a potential challenger, Nazarbayev first sent Aliev to Austria as an ambassador and then to the OSCE in 2006. A year after coming back to Kazakhstan, Aliev fell further from grace when he attacked the president, threatening to release materials revealing corruption at

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[356] Cohen, *Kazakhstan: The Road to Independence. Energy Policy and the Birth of a Nation*, 56.
[357] John Heathershaw and Alexander Cooley, "Offshore Central Asia: An Introduction," *Central Asian Survey* 34, no. 1 (January 2, 2015): 1–10, https://doi.org/10.1080/02634937.2015.1008816.
[358] Junisbai and Junisbai, "The Democratic Choice of Kazakhstan."
[359] Junisbai, "A Tale of Two Kazakhstans."
[360] Rico Isaacs, *Party System Formation in Kazakhstan: Between Formal and Informal Politics* (Routledge, 2011), 75–80.

the top echelons of power.[361] After demonstrating his open intent to run against the president, he had to flee to Vienna, where he continued his opposition by revealing compromising materials in his book "Godfather-in-law" until his mysterious death in 2015. Back in Kazakhstan, Aliev was charged with kidnapping the managers of NurBank, killing the political opponent Altynbek Sarsenbayev, and attempting to organize a plot to oust the president Nazarbayev. As the scandal, *Rakhatgate*, gained international publicity in 2007, Dariga divorced Aliev while Nazarbayev withdrew all his protection from him. In early 2008, the regime started to nationalize his assets in media, oil, and banking while the court sentenced him in absentia to 20 years in prison.[362]

With Aliev cast out from the political circle, Nazarbayev came to realize that he had to ensure "his rule at the expense of the political ambition and clout of his own family."[363] Following the downfall of the troublemaker, Nazarbayev moved to restore the internal balance of power by first distancing himself from the family, conducting personnel reshuffling and making necessary changes to the constitution. The first move involved the dismissal of important family members, Dariga Nazarbayeva and Timur Kulibaev, another son-in-law, from power positions.[364] Two important assets controlled by Aliev-Dariga family, Nurbank and Khabar News Agency were re-nationalized and put under the president's control in 2007.[365] In the same year, Kulibaev, who had also entertained political ambitions with his billions in personal wealth, was dismissed from his position as the deputy chair of the board of directors of Samruk, the largest government holding.

The second move came in 2007 when the president signed amendments to the constitution under the guise of enhancing the role of parliament and democratizing the country. In reality, such amendments lifted the term limit on the country's first chief executive – Nazarbayev – with the possibility of making him president-for-life. According to Schatz and

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[361] Alexander A. Cooley and John Heathershaw, *Dictators Without Borders: Power and Money in Central Asia*, *Dictators Without Borders* (Yale University Press, 2017), 135, https://doi.org/10.12987/9780300222098.
[362] Simone Bohnenberger-Rich, "China and Kazakhstan: Economic Hierarchy, Dependency and Political Power?" (Ph. D, London School of Economics and Political Science (LSE), 2015), http://etheses.lse.ac.uk/3126/.
[363] Isaacs, "Nur Otan, Informal Networks and the Countering of Elite Instability in Kazakhstan: Bringing the 'Formal' Back In," 1070.
[364] Junisbai, "A Tale of Two Kazakhstans."
[365] Laruelle et al., *Kazakhstan in the Making*, 134.

Maltseva, these moves sent an important signal to the possible challengers that he, not the collective family, was still in charge in the regime and that he would in no way tolerates disloyalty.[366] After the trial, Nazarbayev himself said that "this is a harsh lesson, not only to those close to me, but to all the people vested with power in our state".[367]

The domestic power struggle was soon followed with another headache for the regime, the financial crisis that started in late 2007, hitting two important service sectors drove the economy, the construction, and financial services. According to the Ministry of Economy, these two sectors accounted for 45% of the GDP growth in 2007.[368] The real estate boom had started because of inexpensive mortgage loans that the banks pumped money into, capitalizing on the euphoria that the "construction boom could become a locomotive for the country's development, improving people's living and housing standards, creating jobs, and even stimulating industrial output".[369] According to Ademi, almost 25% of bank loans went to real estate sector, which grew 30% in 2007.[370] Yet due to the credit crunch and collapse in demand, the construction companies found themselves squeezed or on the verge of possible collapse. As many people had invested in the housing projects, called "share-holding participation", the government had to bail out the construction companies.

Another hard-hit sector was banking & financial services. Due to low domestic savings and availability of cheap credit, many banks heavily relied on external borrowing to provide loans to a growing middle class. The banking sector accumulated an external debt of around $40 billion by the end of 2008, which accounted for 50% of total borrowing. In total, real estate mortgages accounted for one-third of the banking loans.[371] Once the subprime mortgage crisis hit world financial markets, heavy reliance on externally debts left not only the banks, but also the whole economy vulnerable to the crisis. The liquidity problem was soon followed by an

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[366] Edward Schatz and Elena Maltseva, "Kazakhstan's Authoritarian 'Persuasion,'" *Post-Soviet Affairs* 28, no. 1 (January 1, 2012): 59–60, https://doi.org/10.2747/1060-586X.28.1.45.
[367] Lillis Joanna, "Bill to Boost Nazarbayev's Powers in Kazakhstan Remains Theoretically Alive," *Eurasianet*, 2010, https://eurasianet.org/bill-to-boost-nazarbayevs-powers-in-kazakhstan-remains-theoretically-alive.
[368] Cohen, *Kazakhstan: The Road to Independence. Energy Policy and the Birth of a Nation*, 77.
[369] Alima Bissenova, "Construction Boom and Banking Crisis in Kazakhstan," *The Central Asia - Caucasus Analyst*, 2009, http://www.cacianalyst.org/publications/analytical-articles/item/11850-analytical-.
[370] Isadora Ademi, "Growth and Development Strategy," *Express K* 206 (2007): 8.
[371] Cohen, *Kazakhstan: The Road to Independence. Energy Policy and the Birth of a Nation*, 78–80.

outflow of foreign currency and rise in inflation. Amid the possible collapse of economy, the government decided to step in and set up an aid fund, including a transfer of $4 billion from oil stabilization fund, to ensure liquidity for banks with foreign debts and to prop up real estate.[372]

The domestic crisis dealt multiple blows to regime stability, the performance legitimacy of the regime being most damaged. In fact, the country's economic performance lay at the heart of the regime's legitimacy and president's popularity. As Schatz argued there was an implicit social contract where the people accepted human rights abuses as the tolerable "costs" of economic success.[373] A few years ago Nazarbayev even promised to enter the exclusive club of the world's ten largest exporters of oil and to catch up with the living standards in developed countries. Buoyant expectations turned into political discontent.

However, Nazarbayev soon managed to escape the debacle by easing social tension and spreading responsibility for the crisis onto lower-level elites. Most importantly, the decisive actions taken to mitigate the crisis gave Nazarbayev an opportunity to present himself as a "forward thinking visionary" which clearly embedded his personalized power in the country.[374] After the crisis, which substantially weakened the financial base of the opposition, the government approved legislation in 2010 that proclaimed Nazarbayev as the "Leader of the Nation" ("El Basy") and granting him lifetime powers and a seat in the Constitutional Court and Security Council after he retires from the presidency. The primary motive behind the move seems privileges, the lifetime immunity, and protection from prosecution for Nazarbayev and his family, including their business empires.[375] In the same year, Nazarbayev's supporters in parliament voted unanimously to hold a referendum that would allow him to stay in office until 2020, forgoing the two scheduled elections. However, while vetoing the bill, he called a snap election in 2011 and claimed victory. The speculation was that "any of the possible successors will bring risk of conflict. He will not be in favor of some groups. This is how the system works."[376]

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[372] Bissenova, "Construction Boom and Banking Crisis in Kazakhstan."
[373] Edward Schatz, "Transnational Image Making and Soft Authoritarian Kazakhstan," *Slavic Review* 67, no. 1 (2008): 53, https://doi.org/10.2307/27652766.
[374] Schatz and Maltseva, "Kazakhstan's Authoritarian 'Persuasion,'" 56.
[375] Jim Nichol, "Kazakhstan: Recent Developments and U.S. Interests" (CRS Report for Congress, 2011), 2.
[376] Peter Plenta, "Kazakhstan After President Nazarbayev - Unclear Future of the Central Asian Success Story," in eds. Peter Bator and Robert Ondrejcsak *Panorama of Global Security Environment 2015-2016* (Bratislava: Stratpol, 2016), 245.

In short, by 2012 Nazarbayev reestablished a personalized authoritarian regime in which he personally dominated the political scene with the ruling Nur-Otan party and monopolized decision making. He successfully built a regime coalition consisting of a loyal crew of individuals and made the legislature and judiciary subservient to his will while bringing the media under state control through repression. It was only in 2019 when, after winning another election in 2015, Nazarbayev realized the problems that his personalized system could pose to the long-term stability of the regime and stepped down, giving the post to a handpicked successor.

Economic nationalism 2.0 and dualistic state capitalism. The domestic political changes soon brought corresponding changes in the economic sphere, leading to greater state control over key sectors. Nazarbayev began centralizing national assets under his control not only to avoid further elite fragmentation but also to prevent the emergence of challengers. This culminated in the second wave of changes to the subsoil law, the renationalization of oil businesses that belonged to the president's family members, as well as in the merger of two state funds and his control of the National Fund. The shift in power positions enabled the regime to exercise bargaining power against both challengers and foreign investors. As a result of these changes Nazarbayev centralized a system of economic decision making which cemented a new economic arrangement, dualistic state capitalism.

In 2007, the Kazakh parliament passed a new law that granted the government the right to renegotiate, amend, or annul past contracts deemed a threat to Kazakhstan's national security.[377] While officials denied that it had anything to do with resource nationalism, there began a gradual toughening of conditions for international oil companies. In his annual State of the Nation address in 2008, Nazarbayev said that "the main focus in the oil and gas sector is the consolidation of the state's position as an influential and responsible player in international petroleum and energy markets . . . by strengthening the state's influence in strategic industries."[378]

[377] Kennedy and Nurmakov, "Working Paper: Resource Nationalism Trends in Kazakhstan, 2004–2009."
[378] Indra Overland, Heidi Kjaernet, and Andrea Kendall-Taylor, *Caspian Energy Politics: Azerbaijan, Kazakhstan and Turkmenistan* (Routledge, 2010), 22.

The purpose behind the possible changes regarding government-business relations was the Kashagan and Mangistaumunaigaz (MMG).[379] Interestingly, both companies were an important part of the business empire of Nazarbayev's daughter and her husband Aliev.[380] After the political conflict that Aliev caused, Nazarbayev ordered the nationalization of MMG through the buyout by KMG in 2008, similarly to the Yukos case in Russia. Shares of MMG were then divided between KMG and Chinese national oil company CNPC in 2009. Similarly, Karachaganak consortium was accused of violations of tax and environmental regulations. In 2007, about 100 contracts with foreign investors were cancelled.

The public sector, however, expanded not only in oil and gas, but also in power utilities, mining, and financial sectors. For example, in 2007 and 2008 the regime attacked foreign companies with assets in the coal extraction industry and partially renationalized the non-ferrous metals group Kazakhmys. The financial crisis in 2008 further supported the regime's push toward nationalization. As the country's banking system, which was relatively developed and globally integrated, was hit by the crisis, the regime had to renationalize several large banks, several of which belonged to first generation of oligarchs.[381]

Like Russia, since 2007 the Kazakh political regime completed its personalization of power, and the state became a more active player in the economy. As a result of political personalization, the regime increased state ownership and control in key sectors by changing many contracts with foreign companies in oil and gas and strengthening state presence in energy, metallurgy, mining, and finance. Creation of Samruk Kazyna helped Nazarbayev consolidate state power in the economy and strengthen the regime's control over domestic business. Greater state presence in the economy left business even less room to operate. Formal strengthening of the state became the most direct and effective way to maintain control over the economy. Informal mechanisms became insufficient when business was undergoing differentiation and further development while energy prices continued to rise and offer lavish opportunities for rent-seeking. As in Russia, the assertion of state's economic power was mostly about establishing its will against other groups, including political and economic oligarchs, and

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[379] Orazgaliyev, "State Intervention in Kazakhstan's Energy Sector," 146.
[380] "Central Asia Petroleum Buys Kazak Oil Stake," *New York Times*, 1997, https://www.nytimes.com/1997/05/13/business/central-asia-petroleum-buys-kazak-oil-stake.html.
[381] Alexander Libman, "Government-Business Relations in Post-Soviet Space: The Case of Central Asia," *MPRA* No. 11874 (2008): 18.

therefore empowering the regime rather than pursuing development as a resource that serves the public good.

In short, as was the case in Russia, the regime's intention in pursuing increased control over key sectors of the economy through state ownership and intervention in Kazakhstan was a response to consolidate and maintain its power in the face of perceived challenges coming from various economic actors with substantial power. Thus, the logic of maintaining political power in the regime demanded the establishment of a new state capitalist economy in Kazakhstan in which the regime held control over key sectors of the economy while allowing independent economic activity in the rest.

Figure 13.

Chapter 4. The state sector: state control in the commanding heights of the economy in Russia and Kazakhstan

The previous chapter provided a comprehensive analysis of Russia's political economy from 1986 to 2018 under three presidents, Mikhail Gorbachev, Boris Yeltsin and Vladimir Putin and the political economy of Kazakhstan from 1991 to 2016 under President Nursultan Nazarbayev. The chapter discussed how the historical account of the political and economic transitions in both Russia and Kazakhstan paved the way to the emergence of new politico-economic system. In line with previous chapter's analysis, this chapter analyzes in detail the state sector of the dualistic capitalist systems in Russia and Kazakhstan, including hydrocarbons, heavy industries, and finance with a focus on industry-specific companies of strategic sectors in both countries. Through an analysis of the state-controlled companies in both countries, this chapter argues that control over the state sector helps the regime maintain its stability through three important mechanisms: 1) the provision of revenue and economic growth necessary for the regime to stay in power, 2) a provision of necessary patronage for the ruling coalition, including the political elite, while also controlling the emergence of new wealth centers and 3) avoiding an economic crisis that threatens the regime collapse.

4.1 The structural origin of dualistic state capitalism in Russia and Kazakhstan

The original sin behind the current statist economic arrangement in both Russia and Kazakhstan lies in the structural legacy of the Soviet economy.[382] Following Marxist-Leninist creed, Soviet leadership based the new economic system on the state ownership of the means of production and centralized control through directives. The essential principles of the Soviet system were laid down in Lenin's New Economic Policy, or NEP in 1921. At first, facing the crumbling state of the economy following the civil war, the Soviets adopted its institutions to allow privatization of small companies, the farmers' autonomy, and profit motivation. Also lacking the requisite money necessary for state survival, Lenin introduced a "concessions policy" to foreign investors in big industries, including oil, that aimed to provide the state with resources

[382] Fiona Hill and Clifford G. Gaddy, *The Siberian Curse: How Communist Planners Left Russia Out in the Cold* (Brookings Institution Press, 2003).

to help modernize the economy.[383] However, as the project failed to materialize amid resistance from the party's radical wing, Lenin instead emphasized control of the commanding heights of economy. The idea was that the state had to forcibly restructure its revenue base into gigantic productive units from which wealth could be directly squeezed out.[384]

After the death of Lenin, Stalin espoused a brutal forced industrialization policy to create "socialism in one country", which, however, crystallized into the "directive-planning" system.[385] The imperative of forced industrialization through hierarchical command-cum-planning established a "centralized system of production planning and supply allocation."[386] Such a system aimed to help facilitate the Soviet Growth Model (SGM) or "extensive growth" model. Yet, certain priorities of SGM that were meant to meet political goals regardless of economic feasibility came to shape the deformed *sectoral structure* of Soviet industries.[387] The priorities of extensive growth included a bias towards investment over consumption, heavy industry, especially steel and arms production, over light industry and the "productive" sector of material goods over "unproductive" service and consumer goods.[388] To facilitate the choice of the priority industries that favored extensive growth Soviets used a centralized authoritarian control. The Soviet economy also favored giant firms over small ones due to blind belief that "being big" is a good thing in terms of economies of scale and large capital expenditure.[389] The fact that giant firms tended to be located in a single town, especially in inhospitable places, produced a distorted economic geography with economically barren regions feeding on rich ones. According to some estimates, the Soviet Union put the share of heavy industry of the USSR's total investments at 84% between 1917 and 1976.[390] As for the household consumption,

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383 Anthony Heywood, "Soviet Economic Concessions Policy and Industrial Development in the 1920s: The Case of the Moscow Railway Repair Factory," *Europe-Asia Studies* 52, no. 3 (May 2000): 551–52, https://doi.org/10.1080/713663063.
384 Robinson, *The Political Economy of Russia*, 30.
385 Daniel Yergin and Stanislaw Joseph, *The Commanding Heights: The Battle Between Government and the Marketplace That Is Remaking the Modern World* (Simon & Schuster, 1998), 23.
386 Nat Moser, *Oil and the Economy of Russia: From the Late-Tsarist to the Post-Soviet Period* (Routledge, 2017), 51.
387 Brigitte Granville and Peter Oppenheimer, eds., *Russia's Post-Communist Economy* (Oxford, New York: Oxford University Press, 2001).
388 Kornai, *The Socialist System*, 153.
389 Gur Ofer, "Soviet Economic Growth: 1928-1985," *Journal of Economic Literature* 25, no. 4 (1987): 1772.
390 Kornai, *The Socialist System*, 94.

its share of GNP accounted for 50 to 55% in comparison to 60-65% Western consumption levels.[391]

Other distorting characteristics of the Soviet industrial structure included its orientation towards hyper-militarization that favored gigantic enterprises. Defense spending rose from less than 10% in the late 1950s to 17% for the early 1980, and the defense industries tended to be gigantic in size. More than one third of all enterprises in Russia that had more than 5000 employees were arms manufacturers.[392] In terms of geography, among the satellite countries of Soviet Union Russia had concentrated almost all defense-related industries, accounting for 71% of defense sector employment, demonstrating the extent of its sectoral structure. In short, because growth priorities were biased towards heavy industries, "unproductive" sectors that produced consumer goods and service considerably fell behind, further distorting the industrial structure. As Levine puts it, the Soviet Union did not produce any finished exportable to other countries outside the block other than wooden dolls, vodka, and weapons.[393]

After the death of Stalin, the Soviet economy, though remaining a command economy, underwent a series of administrative reforms under subsequent party leadership that brought changes.[394] Over the years, the Soviet economy came to present three competing domains with different logics, as represented in figure 14 below. In the first sphere, the party dominated decision making where the political, rather than economic, criteria prevailed. In the second sphere, decision making was dominated by ministerial bureaucracy who acted within the structure of the planned economy. However, according to Rutland, the bureaucracy had developed into "deeply-entrenched structures" where the departmental self-interest became "distinctive characteristic of the system's functioning."[395] The last sphere accommodated free economic exchanges that took place according to supply and demand. The main market activity in this sphere was the consumption sector that operated under semi-market conditions. It is the widening of the intersection of the market and plan sectors where market forces penetrated the

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391 Ofer, "Soviet Economic Growth: 1928-1985."

392 Hill and Gaddy, *The Siberian Curse: How Communist Planners Left Russia Out in the Cold*, 78.

393 Steve Levine, *The Oil and the Glory: The Pursuit of Empire and Fortune on the Caspian Sea* (Random House, 2007), 82.

394 Philip Hanson, *The Rise and Fall of the The Soviet Economy: An Economic History of the USSR 1945 - 1991*, 1st ed. (London: Routledge, 2003), 52.

395 Peter Rutland, "Party Control of Economic Management in the USSR," *National Council for Soviet and East European Research*, 1991, 3–5.

planned economy, leading to the creation of a black market and ultimately the collapse of the whole economy.

Figure 14.

The sectoral structure of the Soviet Union bequeathed a legacy to the transition countries of Russia and Kazakhstan after its collapse. In Russia, the shock therapy experiment of the "market Bolsheviks" under Yeltsin's leadership aimed to change the mechanism of economic exchange along with the power balance between the state and anti-reform vestiges of the old elite.[396] The measures of outright price liberalization and asset privatization were the means of furthering the end of *etatization*, tentacles of state ownership and control. These reforms ostensibly aimed to curb the power of the old elite by taking away the enterprises they run and creating an alternative group of economic actors who had a stake in supporting the market mechanism.[397] However, quite contrary to the expectations, the botched reform package produced negative outcomes for the nascent economic and political system due to the reasons discussed in previous chapter. The main deformity involved the concentration of economic assets into a few hands, namely oligarch-controlled financial-industrial groups, whose economic clout came to privatize the state and hijack the political process, leading to the collapse in state budgets and social order. In contrast, Kazakhstani regime had to endure economic recession due to the economic dependency that Soviet system of economic regionalization created.

4.2 The *state sector* in Russian economy

As previous chapters described, Russia's dualistic state capitalism is a politico-economic order in which market principles coexist with, or sometimes is subject to, the personalized power system. This peculiar mode of state capitalist economy that was subordinated to the needs of political regimes in Russian context features an important element; private businesses have to live on alongside the prerogatives of state interference. An important *sectoral* player under the dualistic state capitalism of Russia is the state, which is itself in fact

[396] Dmitri Glinski Vassiliev, Peter Reddaway, and Dmitri Glinski, *The Tragedy of Russia's Reforms: Market Bolshevism Against Democracy* (US Institute of Peace Press, 2001).
[397] Robinson, *The Political Economy of Russia*, 28.

seen as an economic resource to be consumed.[398] The state completely dominates the key sectors of the economy in the form of large state-owned enterprises (SOE) or state corporations with the goal of modernizing Russian economy and making it great power. The rise of state-owned shares from 20% in 2003 to 35% in 2007 in the stock market reveal the growing role of the state sector.

SOEs are neither directly managed by the ministries/agencies like in the Soviet era, nor are they regulated by enforceable contracts. Rather they fall into the personal discretion of high-level state actors, or state oligarchs, creating huge opportunities for personal enrichment. To directly supervise and ensure policy compliance in strategic companies, the Kremlin appoints officials from the presidential administration along with professional directors. Political calculations rather than economic efficiency dictate the rationale behind the commercial operations of SOEs and their interactions with other private businesses. For instance, according to Sakwa, seven political appointees controlled nine state companies with a combined value of US$222 billion, or 40% of Russian GDP.[399] In early February 2008, Russia's business journal *Vedomosti* estimated that the political allies of the president headed the boards of companies that together accounted for 40 % of the country's economy. The assets controlled by long-term associates of Putin from his days in the KGB and the St. Petersburg mayor's office include Gazprom; Rosneft oil company; Channel One (the largest television network); railways; a key cellphone company; and the oil-export monopoly. According to the Russian antimonopoly committee, the state share of Russia's GDP increased from 35% in 2005 to 70% in 2015, although the figure seems a bit unlikely.[400]

An interesting characteristic of the state sector is that its leadership did not renationalize the commanding heights completely, rather, after creating a degree of enough *deprivatization*, the regime brought another set of players in or around the state sector in alignment with its strategic goals. It means that a limited access to some strategic and non-strategic sectors might be granted to these players, or the subordinate oligarchs, on the condition of loyalty to the regime and fulfillment of certain state obligations.[401] However, the delineation of public and private is often blurred and usually goes in favor of the state. As Easter argues, oligarchic assets

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[398] Easter, *Capital, Coercion, and Postcommunist States*, 24.
[399] Sakwa, "Putin's Leadership."
[400] Aslund, *Russia's Crony Capitalism*, 98.
[401] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 215.

are given as "concessions", in which the private property rights of owners are not formalized with recognizable protective boundary.[402]

As this chapter will discuss further, the role of the state is an important factor that shapes the extent to which business can influence public policy. In other words, the economic power of the state plays three important roles for the regime's political power. First, the state can influence how business groups can form and to what extent they can gain strength. Second, the state can influence the economic orientation of business groups. Finally, the state can influence the arena in which business can exert its influence.[403]

What is the purpose behind the existence of and control of the state sector? The short answer is that control over the state sector along with its players, both SOEs and oligarchs, that operate within it helps the regime maintain stability and prevent the emergence of trouble through three important mechanisms; 1) a provision of revenue and economic growth necessary for the regime to stay in power, 2) a provision of necessary patronage for the ruling coalition, including the political elite and oligarchs, while controlling the emergence of new wealth centers and 3) an avoidance of economic crises that may threaten regime collapse. Below, the chapter discusses the commanding heights of the Russian economy where the state has firm control to further above-mentioned tasks.

4.2.1 Energy sector: NOC Rosneft and NGC Gazprom; national champions or cash dispensers?

The most important sector for Russian state capitalism under Putin is the hydrocarbon industry, composed mainly of oil and gas. Possessing over 6% of world's oil and 25% of proved gas reserves, Russia became an "energy superpower" since 2000, topping global oil and gas production at various points in history.[404] In 2007, Russia produced 9.8 million barrel a day, 12% global oil supply. As for gas, Russia supplies 40% of gas used by the European Union.[405] However, it is only in the 1960s that Soviets realized the importance of hydrocarbons, beginning with the major exporter of oil and gas with new discoveries in Siberia. Crude oil along with

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[402] Gerald M. Easter, "The Russian State in the Time of Putin: Post-Soviet Affairs: Vol 24, No 3," *Post-Soviet Affairs* 24, no. 3 (2008): 199–230.
[403] L. Sim, *The Rise and Fall of Privatization in the Russian Oil Industry* (Springer, 2008), 7–8.
[404] Marshall I Goldman, "Russian Energy: A Blessing and a Curse," *Journal of International Affairs* 51, no. 1 (1999): 73–74.
[405] Peter Rutland, "Russia as an Energy Superpower," *New Political Economy* 13, no. 2 (June 2008): 203, https://doi.org/10.1080/13563460802018547.

other natural resources were an important link that connected the Soviet economy to the world. Export earnings also served as a source of hard currency that the economy desperately needed. Similarly, the natural gas industry started to grow rapidly by the early 1970s after Brezhnev called for a new energy mix strategy to fuel growth.[406] The Soviet Union became the largest natural gas producer by 1984 and largest exporter by 1993, accounting for 40% of the global production.[407]

The Soviet's reliance on hydrocarbons grew more dire after the economy started to show signs of decay and become unable to sustain its growth model. Thanks to a drastic rise in oil price because of the Arab oil embargo and revolution in Iran, the exhausted Soviet economy could survive another decade without reforming itself within. Russian economist Yegor Gaidar, a mastermind of neoliberal reforms during Yeltsin presidency, once mentioned that the hard currency that oil exports provided were the bloodline of ebbing economy, which increased import of equipment and consumer goods and guaranteed a financial basis for the arms face.[408] According to Li Chen, oil exports accounted for 28% of Soviet hard currency during 1971-1975, a share that increased 60% or US$12.7 billion during 1981-1985. By contrast, gas exports made up only 17% of Soviet hard currency revenues during 1981-1985.[409]

The structure of the hydrocarbon industry in Soviet Union followed a different organizational form from its Western counterparts. Following the nationalization of industries by Bolsheviks, the hydrocarbon industry came to be organized whereby the Politburo and *Gosplan*, central economic bureaucracy, stood at the top with political directives, oil and gas ministries in the middle with industrial control, and production associations that comprised enterprises become subordinates at the bottom.[410] Yet, the control over the industry, from upstream to downstream, was organized horizontally with extraction, production, and distribution coming under different ministries. This meant that the whole industry consisted of a diverse set of structures that operated under different economic and political interests. Later,

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[406] David Lane, "The Political Economy of Russian Oil," in *Business and State in Contemporary Russia* ed. Peter Rutland (London: New York: Routledge, 2001), 101–5.
[407] Agnia Grigas, *The New Geopolitics of Natural Gas* (Cambridge MA: Harvard University Press, 2017), 42
[408] Daniel Yergin, *The Quest: Energy, Security, and the Remaking of the Modern World* (Penguin, 2011), 23–24.
[409] Sim, *The Rise and Fall of Privatization in the Russian Oil Industry*, 2.
[410] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 32.

with reform to the economic system under Khrushchev and Gorbachev, control over the industry first shifted away from ministers towards regional party leaders and then enterprise managers.

Although the Soviet Union had large reserves (around 10 billion tons), production was subject to "crisis amid plenty" by the end of Soviet Union. Although oil production was steady through 1970s, it began to stagnate from 1980 to 1985, before slightly recovering in 1987 and 1988 that amounted to 624 million tons a year.[411] Facing an ever-increasing costs and price drops, hydrocarbon export revenues sharply declined. As Thane stated, oil and gas rents dropped from $270 billion in 1980 to $100 billion in 1986 due to both factors.[412] The steady deterioration of the oil and gas industry reflected the systemic problems within the Soviet economy; false and inaccurate information, irrational incentives, and distortions in execution.

After the collapse of the Soviet Union, the market reformers of the Yeltsin administration introduced a radical restructuring of the oil industry. The economic and political chaos that swept the entire country affected the oil industry, creating a "free-for-all" process of asset redistribution from state ownership to "no one at the control".[413] With the state losing its political control over industries, the enterprises management and regional administrations started to create independent companies, violently taking over state assets and thus unleashing spontaneous privatization.[414] Although the new government replaced Soviet ministries with a single Ministry of Fuel and Power to regulate the energy industry, in reality it could not wield any control over the production units.[415] In the face of disintegration, oil production fell from 11.3 million barrels per day in 1986 to 7.12 million in 1993, and to 5.04 million in 1996.

Figure 15.

Amid this dire situation, the government adopted a program to transform the energy industry towards a market system in 1992 that aimed at gradually achieving two important tasks: decontrol the prices as well as export quota and privatization of oil enterprises. The government

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[411] Thane Gustafson, *Crisis amid Plenty: The Politics of Soviet Energy under Brezhnev and Gorbachev* (Princeton, New Jersey: Princeton University Press, 1989), 64–66.
[412] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 36.
[413] Goldman, *Petrostate*, 55–60.
[414] Fortescue, *Russia's Oil Barons and Metal Magnates*, 30.
[415] David Lane, "The Political Economy of Russian Oil," in *Business and State in Contemporary Russia Ed. Peter Rutland* (London: New York: Routledge, 2001), 102–105.

organized the industry, made up of almost 300 enterprises upstream and downstream, into a dozen holding companies and subsidiaries with the aim of creating vertically integrated companies that would encourage competition and efficiency. Yet, the program allowed the state to maintain majority ownership with 51% of shares in holding companies as well as two pipeline monopolies, for at least three transitional years, so that it could bring the new companies under federal jurisdiction and ensure control over the taxes accrued to the increasingly decrepit budget. The state established an important vehicle, state oil enterprise Rosneft (previously called Rosneftegaz), to park its ownership shares.[416]

However, the government's program of holding state control over the industry failed to materialize. Taking advantage of the increasing budgetary deficit, neoliberal reformers pushed for de-monopolization of state control over oil and gas industry in line with their vision of creating a market economy.[417] The need to use the privatization of the energy sector to collect budget revenue came to be known as the "loans-for-shares" program in which bankers agreed to offer loans in exchange of shares of major oil companies as a collateral.[418] As the government failed to repay the debt, it had to relinquish its ownership rights in oil companies to a few oligarchs, who came to form financial-industrial groups; Alfa Bank bought 40 percent of Tyumen Oil (TNK), Oneksimbank 85 percent of Sidanko, Menatep 85 percent of Yukos and Berezovskii 99 percent of Sibneft.[419] Years later TNK joined with British Petroleum (BP) to form TNK-BP 50-50 partnership. As a result, the largest private oil companies, including LUKoil, Yukos, Surgutneftegaz, Tatneft, and Sidanko came to collectively control 75% of Russia's total oil output, 70–80% of oil exports and 60% of Russia's oil reserves.[420] Out of the top 20 companies that roughly controlled 30% of Russia's GDP, 13 were in the energy industry.[421]

Unlike the oil industry, the gas industry was reorganized in quite a different fashion due to its monopoly position. Following Gorbachev's reform of transferring ministerial power to the enterprises, the production and distribution of gas was totally run by a centralized Gazprom

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[416] Goldman, *Petrostate*.
[417] Sim, *The Rise and Fall of Privatization in the Russian Oil Industry*, 10.
[418] Fortescue, *Russia's Oil Barons and Metal Magnates*, 54–55.
[419] Goldman, *Petrostate*, 63–64.
[420] Sim, *The Rise and Fall of Privatization in the Russian Oil Industry*, 31–35.
[421] Peter Rutland, "Putin's Economic Record: Is the Oil Boom Sustainable?" *Europe-Asia Studies* 60, no. 6 (August 1, 2008): 1051–72, https://doi.org/10.1080/09668130802180975.

State Gas Concern, first state-corporate enterprise that was created out of Ministry of Gas in 1989 under then minister Viktor Chernomyrdin.[422] With the onset of the privatization spree in 1992, Gazprom was converted to a joint-stock company and 35% of its shares was sold to workers and outside shareholders. Gazprom, the largest gas company in the world, was valued at around $US16.5 billion in 1997 with the sales of around US$20 billion.[423] With the massive economic power that yields political influence, it was "hard to stay where Gazprom ends and the Russian state begins."[424] Deemed as a natural monopoly, the state kept 40% controlling shares until 2005. However, during these years Gazprom practically came under the personal domain of Deputy Minister Rem Vyakhirev; his son dominated its export division and his daughter owned large shares in the gas pipeline builder, Stroitransgaz.[425]

The story of the restructuring of the oil industry during transition can best epitomize the emerging Russian politico-economic system which Lane calls as "chaotic capitalism" in which there was a lack of coordination between state and business.[426] Here, an internally weak state fell prey to the economic interests of oligarchic groups which, after flawed privatization, politicized the policymaking, giving rise to disorganized economy with deregulated industries. They were not active in lobbying through a party system; instead lobbying took the form of an informal personal contacts between directors and government bureaucrats.

The energy industry once again experienced a complete overhaul in the ownership structure when Putin came to power in 2000. At first, Putin appeared to be a market liberal who advocated market reforms and reached a noninterference consensus with the Yeltsin era oligarchs.[427] By that time, both domestic and international oil companies became hyperactive with new investment projects in building supply lines and exploring reserves in former Soviet territory. However, the need to consolidate power coupled with the recent rise in oil prices loomed large, and oligarchs' oil empires became irresistible prizes for a new player in the

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[422] Goldman, *Petrostate*, 59.
[423] Peter Rutland, "The Political Economy of Energy in Russia," in *The International Political Economy of Oil and Gas*, ed. Slawomir Raszewski, International Political Economy Series (Cham: Springer International Publishing, 2018), 23–39, https://doi.org/10.1007/978-3-319-62557-7_3.
[424] Peter Rutland, "Lost Opportunities: Energy and Politics in Russia," *The National Bureau of Asian Research* 8, no. 5 (1997): 7–9.
[425] Miller, *Putinomics*, 48.
[426] Lane, "From Chaotic to State-Led Capitalism."
[427] Hill and Gaddy, *Mr. Putin*, 143.

economy, the state that grew powerful under young president Putin.[428] The assertion of state control over the energy sector that yielded power and wealth became an essential part of regime consolidation.

Putin's vision to bring the energy sector under the state control, under a system eventually crystallized as state capitalism, was based on a few tenets, described in his thesis. For Putin, markets, and private owners *per se,* are unable to enhance industrial development and restore the economic growth; it needs proper guidance and necessary intervention by the state which can collect revenues and distribute them across strategic sectors.[429] Putin stated that "regardless of who is the legal owner of the country's natural resources and in particular the mineral resources, the state has the right to regulate the process of their development and use."[430] Oil and gas industries in this process, provide not only a source of capital but also serve as an instrument of political control at home and geopolitical influence abroad.[431] For that, large state-owned companies, or national champions, instead of oligarchic corporations, should remain as the primary vehicle for handling energy rents, as the only latter can ensure state's interest. After all, the natural resources, as defense minister Sergei Ivanov claimed, "belongs to the state, they are not private property."[432] Yet, private oil companies can coexist alongside national champions provided that they comply with the state guidance. As for foreigners, the ownership, except a few PSA, is highly restrictive in the energy sector.

The shift to *etatization* of the energy sector commenced in 2003 after government adopted subsoil law to classify the oil, gas, and defense-related industries as "strategic". Soon, the state, via the vehicles of Gazprom and Rosneft, began to claim controlling shares in major oil companies owned by oligarchs through a mixture of political persuasion and coercion.[433] As previous chapter explained, after the arrest of oil tycoon Mikhail Khodorkovsky who attempted to challenge Putin's power through his oil wealth, the state-owned Rosneft took over the assets

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[428] Thane Gustafson, "Putin's Petroleum Problem: How Oil Is Holding Russia Back - and How It Could Save It Essay," *Foreign Affairs* 91 (2012): [i]-96.
[429] Tsygankov, *The Strong State in Russia*, 139.
[430] Goldman, *Petrostate*, 75.
[431] Rutland, "Russia as an Energy Superpower."
[432] Easter, "The Russian State in the Time of Putin: Post-Soviet Affairs: Vol 24, No 3."e
[433] Michael Bradshaw, "The Kremlin, National Champions and the International Oil the Global Importance of Russian Oil and Gas Companies: The Political Economy of the Russian Oil and Gas Industry," *Geopolitics of Energy* 31, no. 5 (2009): 5–8.

of his company Yukos, the largest private oil company, in 2003 for its march to become the national champion.[434]

Following nationalization of Yukos, the second in line was Sibneft, the third-largest oil company that was jointly owned by other oligarchs, Boris Berezovsky and Roman Abramovich. In 2005, the company was forced to sell 72% of the company to Gazprom for US$16 billion.[435] Another attack was launched against the owner of Russneft through a Kremlin-linked oligarch, Oleg Deripaska. At the same time, interestingly, Putin allowed another major private oil company TNK to merge with BP on 50-50 ownership. However, in 2013 Rosneft bought TNK from BP in exchange of US$17.1 billion and 19.7% share in Rosneft.[436] The deal made Rosneft the largest oil company in the world.[437]

Having observed the takeovers, the remaining major private oil companies, including LUKoil (Vahet Alekpegov), Surgutneftegaz (Vladimir Bogdanov) and Slavneft willingly submitted themselves to state power.[438] The few existing foreigners that were operating under PSA in Sakhalin also started to face an increasing pressure by the state. Prominent examples include the sale of 50 percent share of Sakhalin II project developed by Shell, Mitsui, and Mitsubishi to Gazprom in 2006 for a modest $7.5 billion.[439], as well as national oil company Roseft's buyout of 34 percent of Selkupneftegaz in 2005 and 51 percent of Udmurtneft' in June 2006 from the Chinese state company Sinopec. As a result of the takeovers, within a few years Putin had restored state control over 70 percent of Russia's oil industry. While state-controlled companies accounted for about 16.0% of oil production in 2003, the figure reached to 40% by early 2007 and still rising.[440]

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[434] Stephen Fortescue, "Private Enterprise in the Russian Oil Sector," in *Russian Energy and Security up to 2030*, ed. Susanne Oxenstierna and Veli-Pekka Tynkkynen (London: Routledge, 2013).
[435] STEPHEN FORTESCUE, "Private Enterprise in the Russian Oil Sector," in *Russian Energy and Security up to 2030*, ed. Susanne Oxenstierna and Veli-Pekka Tynkkynen (London: Routledge, 2013).
[436] Shamil Yenikeyeff, "BP, Russian Billionaires and the Kremlin: A Power Triangle That Never Was," *Oxford Energy Comment*, 2011.
[437] Ahmed Mehdi and Shamil Yenikeyeff, "Governors, Oligarchs, and Siloviki: Oil and Power in Russia," *Russie.Nei. Visions* 68 (2013): 12–14.
[438] Goldman, *Petrostate*, 135.
[439] Michael Bradshaw, "A New Energy Age in Pacific Russia: Lessons from the Sakhalin Oil and Gas Projects," *Eurasian Geography and Economics* 51, no. 3 (May 2010): 330–59, https://doi.org/10.2747/1539-7216.51.3.330.
[440] Tompson, "Back to the Future?"

In addition to the oil industry, Putin began to construct another national champion, "the holy" Gazprom, ranked the second largest company in the world by 2007, in the gas industry by purging the company management that stripped the assets for years. As Marshall mentions, although Gazprom generated $2 billion throughout 1995 and 1996, it only paid $3.5 million to the state that owned 38.4 percent of the company's stock.[441] In 2001, Putin replaced Rem Vyakhirev as Gazprom CEO with Alexei Miller, who worked closely with Putin at the St. Petersburg city. By 2003, Miller fulfilled the task of purging the old leadership and bringing the gas industry under Gazprom and the Kremlin. Also, throughout early 2000, Gazprom acted as the main vehicle in taking over the target assets. In 2005 the state purchased 10.7 % of Gazprom's shares, raising the state's holding to 50.002 percent.[442]

For Putin, the control over Gazprom, a US$160 billion company that controls 85% of gas production, and Rosneft became two arms of the regime in energy industry and serve as the principal instrument of power.[443] Hanson argues that there is partly an ideological dimension behind the rise of vehicles of statist control; the Russian "sovereign" democracy needs a corresponding economy where only Russian "national capital" is allowed to dominate the strategic sectors.[444] However, the logic of personalized power system in Russia entails that the ultimate purpose of control through national companies is to help the regime to sustain its power. The leadership directs the energy giants to pursue the regime's domestic and foreign agenda in myriad ways; at home it involves a source of rents to the state and patronage to the elite and people, while outside it might mean cutting deliveries to countries that depend on Russian energy.

The major role that these two giants played in helping Putin has been the provision of revenue stream to the state budget. During 2000-2008 oil prices rose dramatically; from the low point in 1999, $12 per barrel, it rose four-fold to $51 in 2005 and over $140 in 2008 before it plunged. The recovery in oil prices along with new tax reforms provided the basis for an economic revival where GDP grew by about 70%, going from $200 billion in 2000 to $1.26

[441] Goldman, *Petrostate*, 140.
[442] Rutland, "The Political Economy of Energy in Russia."
[443] Ahmed Mehdi, "Putin's Gazprom Problem," *Foreign Affairs*, 2012, https://www.foreignaffairs.com/articles/russian-federation/2012-05-06/putins-gazprom-problem.
[444] Hanson, "The Resistible Rise of State Control in the Russian Oil Industry."

trillion in 2007.[445] Also important for the regime was that export revenues from oil and gas rose from $28 billion in 1998 to $241 billion in 2005.[446] They also provided 52% of all revenues to state coffers through taxes, up from 25% in 2003. Having fully paid its debt obligation, the government hoarded $598 billion in reserves.[447] The growing economy also substantially improved the living standards of the people who had long suffered from the ills of chaotic era. Poverty declined from 38% in 1998 to 9.5% in 2004. As Thane points out, significant growth in state revenue from energy rents kept Putin in power through some precarious years, helping him secure the support of the regime coalition and reviving a strong fiscal foundation for a strong authoritarian state while maintaining high levels of popularity.[448]

Having brought full control over the energy sectors through Rosneft and Gazprom, the leadership started to open their share for sale in capital markets with the hope of internationalizing their national champions and generating more money. First, Gazprom offered its shares which led its market capitalization to rise above $250 billion, "making it the world's third biggest company by that measure."[449] Although company's value later dropped, Gazprom's profits alone still accounted for around 10 % of Russia's GDP. Then, in 2006 Rosneft launched an initial public offering of its shares on stock markets and raised $10.5 billion for the state.

The importance of the energy sector also lies in the management of rent flows that is crucial for power and control under Putin's regime. Overtaking oligarchic control over energy rents, Putin redesigned a centralized system of rent-sharing under state control, granting the regime flexibility in distributing rents to important sectors and balancing power elites.[450] In this "rent management system", the government receives huge rents from the oil producers through taxes (rent creation sector) and transfers them to the rest of the economy, especially protection-dependent secondary non-oil sectors (rent dependent sector) through subsidies, transfers, and investment programs. The existence of "addicted" sectors, most importantly the defense industrial complex in remote cities, creates even more "rent addiction" as they constitute an

[445] Miller, *Putinomics*, 124.
[446] Rutland, "Putin's Economic Record," 1063.
[447] Aslund, *Russia's Crony Capitalism*, 86.
[448] Gustafson, "Putin's Petroleum Problem."
[449] Mehdi, "Putin's Gazprom Problem."
[450] Clifford G. Gaddy and Barry W. Ickes, "Putin's Rent Management System and the Future of Addiction in Russia," in *The Challenges for Russia's Politicized Economic System*, 1st edition (Routledge, 2015); Robinson, *The Political Economy of Russia*, 81.

important political support group with vested interests.[451] The figure 16 below describes raising oil and gas tax revenues to the state.

Finally, control over energy rents served as an important means of patronage that Putin uses to reward the elite loyalty and control their ambition. Under Putin's rule, there emerged *silovarchy* (a combination of *siloviki* and oligarchs), a new class of personal allies of Putin in secret service who, fusing the state power with financial capital, dominated both politics and big business.[452] Following state control over energy, the new champions, Gazprom and Rosneft, started to become corporate bases for two regime factions, economic liberals and statist *siloviki*, whose support Putin relied on.[453] After Putin cane to power, energy affairs was given to Igor Sechin, a close ally of Putin who is known to be the leader of *siloviki* faction in Kremlin and a central figure behind the rise of Rosneft.[454] As for Gazprom, Medvedev became the chairman of Gazprom, representing the liberalist faction within Putinist regime.[455] Miller became director, having originally started out in Anatolii Chubais's circle of liberal reformers before joining the mayoralty. Miller was viewed by his former colleagues as a competent and loyal administrator but not a leader. Although the idea of merging Rosneft and Gazprom emerged in the early years, it was soon crushed. It is for this reason that the idea of merging the two champions did not go well as it "would undermine the balance of power within Putin's inner circle."[456]As a separate entity, both companies were tasked with improving their respective sectors. But there is also ample opportunity to make personal wealth within the loose organization, although they are under the constant observation of the president.

Figure 16.

4.2.2 Profit or policy: Heavy, high-tech industries and financial sector

Another important state sector that constitutes the core of Russia's state capitalism involves a set of heavy industries and financial institutions. Since the mid-2000s, the

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[451] Tompson William, "The Political Economy of Contemporary Russia," in *Routledge Handbook of Russian Politics and Society*, ed. Gill Graeme and James Young (London: Routledge, 2012).
[452] Treisman, "Putin's Silovarchs."
[453] Mehdi and Yenikeyeff, "Governors, Oligarchs, and Siloviki: Oil and Power in Russia."
[454] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 248.
[455] Bremmer and Charap, "The Siloviki in Putin's Russia."
[456] Mehdi and Yenikeyeff, "Governors, Oligarchs, and Siloviki: Oil and Power in Russia."

strengthening of the state's role in the economy manifested in the formulation of a strategic industrial policy that targeted politically favored high-technology sectors, including armament, aviation, shipbuilding, and the nuclear industry.[457] Being huge remnants of the Soviet industrial legacy, these heavy industries in the state sector constitute a major share of the structure of the contemporary Russian economy. Designated as strategic by federal law in 2008, these sectors constitute a core part of Putin's strategic industrial policy that aims to modernize and grow Russia's state capitalism.

The structure of Russian industry today is more concentrated, a condition that was shaped primarily by the legacy of the Soviet policymaking. As mentioned above, Soviet industry was characterized by over-investment in defense industry and the production of investment goods that atrophied the development of the commodity sector along with insufficient production of consumer goods.[458] There was an ideological importance for prioritizing heavy industry that included power generation, coal mining, oil and gas, metallurgy, machine-building and metalworking, chemical, and some other industries.[459] Influenced by Preobrazhensky's vision of rapid industrialization, early Soviet economic policy focused on the fastest possible development of those industrial sectors would could protect political and economic stability during wartime.[460] As a result, the priority of heavy industry, a defining feature of industrialization, became a permanent characteristic of the Soviet growth strategy that accounted for 71.8% of Soviet industrial output in 1959.

The transition period during the 1990s reduced the systemic disproportions significantly, but not entirely. During the turbulent transition years, Russian enterprises suffered from severe disinvestment that led to negative growth rates for both the corporate sector and the whole economy. The economic decline is generally attributed to mismanaged privatization that led to

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[457] Keith Crane and Artur Usanov, "Role of High-Technology Industries," in *Russia After the Global Economic Crisis*, ed. Anders Aslund, Sergei Guriev, and Andrew Kuchins (New York: Columbia University Press, 2010), 95–99.
[458] Vladimir Kontorovich, "The Military Origins of Soviet Industrialization," *Comparative Economic Studies* 57, no. 4 (December 1, 2015): 669–92, https://doi.org/10.1057/ces.2015.8.
[459] Yuri Simachev and Mikhail Kuzyk, "Industrial Development, Structural Changes, and Industrial Policy in Russia," in *Exploring the Future of Russia's Economy and Markets: Towards Sustainable Economic Development*, ed. Bruno S. Sergi (Emerald Group Publishing Limited, 2019), 69–106, https://doi.org/10.1108/978-1-78769-397-520181005.
[460] I Moravick, "The Priority of Heavy Industry as an Objective of Soviet Economic Policy," *Soviet Studies* 17, no. 2 (1965), https://www.tandfonline.com/doi/abs/10.1080/09668136508410466?journalCode=ceas19.

a massive redistribution of national wealth by insiders, which in turn led to deindustrialization and "resourcialization" of economy.[461] While few dozen oligarchs acquired around a third of all state property, former state enterprise managers liquidated the state assets and illicitly transferred them overseas.[462] Such disruptions accompanied major changes to the industrial and manufacturing bases of the economy; being already in deep depression, these sectors were disconnected from finance and mired in a virtual economy.[463] As Dutkiewicz argues, the share of mineral products, metals, and diamonds in Russian exports increased from 52 percent in 1990 (USSR) to 67 percent in 1995 and to 81 percent in 2007, whereas the share of machinery and equipment in exports fell from 18 percent in 1990 (USSR) to 10 percent in 1995 and to below 6 percent in 2007.[464] Aerospace and armaments were hit especially hard, as domestic procurement fell by 80 percent in the 1990s.[465] Although Russia started to experience high economic growth in the early 2000s, its industrial structure still remained almost unchanged. The GDP growth rate in 2005 and 2006 was 6.4%, and 6.7%, while the growth in manufacturing industries was 5.7% and 4.9% respectively.[466]

It is this economic context that Putin, after coming to power, restored the state role as central engine of development for the Russian economy. As explained in the previous chapter, Putin's first term through 2000 and 2004 saw a significant expansion of executive influence in the economy. His political leadership managed to create a stable political environment with a series of structural reforms to encourage economic activity and stimulate growth.[467] Having successfully established strong vertical power, in the second stage from 2004, Putin was poised to transform Russia into a technology–based and advanced economy in manufacturing and service under the guidance of a developmental state program by leveraging on the rise in energy

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[461] Piotr Dutkiewicz, "Missing in Translation: Re-Conceptualizing Russia's Developmental State," in *Russia: The Challenges of Transformation*, ed. Piotr Dutkiewicz and Dmitri Trenin (New York: NYU Press, 2011), 15, https://www.degruyter.com/document/doi/10.18574/9780814785010-005/html.
[462] Black, Kraakman, and Tarassova, "Russian Privatization and Corporate Governance."
[463] Clifford G. Gaddy and Barry William Ickes, *Russia's Virtual Economy* (Brookings Institution Press, 2002).
[464] Dutkiewicz, "Missing in Translation: Re-Conceptualizing Russia's Developmental State," 11–12.
[465] Crane and Usanov, "Role of High-Technology Industries."
[466] FUSHITA Hironori, "A Study of Russian High-Tech Industrial Policy," *KIER Discussion Paper* No. 667 (2009): 2.
[467] Yuri Simachev et al., "Russia on the Path towards a New Technology Industrial Policy: Exciting Prospects and Fatal Traps," *Foresight-Russia* 8, no. 4 (2014): 6–23.

prices that provided financial resource to the state.[468] The agenda for such a vision was formulated under Putin's administration as Concept for the Long-Term Socio-economic Development of the Russian Federation to 2020 in 2007.[469]

There seem to have been two important considerations behind the developmental agenda; a spike in income from commodity exports after 2002 that offered more investment possibilities and an increasing dissatisfaction over Russia's reliance on energy and raw material exports.[470] According to Volkov, out of $340 billion oil super profits, $102 billion was available for public spending. Having been convinced that state's existing tools to promote economic development through innovative industries was inadequate, political leadership adopted a set of important decisions that granted the state an expanded capacity to go beyond regulatory frameworks and carry out economic modernization. With the available oil money, Putin's leadership went further to formulate and implement a strategic industrial policy that aimed to modernize Russian economy by developing high-tech industries and improve the competitiveness of manufacturing industry.[471] Figure below shows the positions of key industries in strategic sectors.

Controlled under the auspices of the presidential administration, state-led industrial policy is characterized by multiple priorities.[472] The priority is that strategic industrial policy is under strict control of the state prerogative that leaves small room for the market mechanisms.[473] The strengthened role of the state took the form of its intervention through ownership and investments. Of course, designing industrial policy in such a way where the state, instead of private actors, plays a key role is connected to the political calculations of elite interests.[474] This

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[468] Richard E. Ericson, "The Russian Economy in 2008: Testing the 'Market Economy,'" *Post-Soviet Affairs*, May 16, 2013, 210

[469] Richard Connolly, "Financial Constraints on the Modernization of the Russian Economy," *Eurasian Geography and Economics* 52, no. 3 (May 1, 2011): 428–59, https://doi.org/10.2747/1539-7216.52.3.428.

[470] Lowry, "Russia's Post-Neoliberal Development Strategy and High-Technology Considerations," 129.

[471] Hironori, "A Study of Russian High-Tech Industrial Policy."

[472] Connolly, "Financial Constraints on the Modernization of the Russian Economy."

[473] Nadir Kinossian and Kevin Morgan, "Development by Decree: The Limits of 'Authoritarian Modernization' in the Russian Federation," *International Journal of Urban and Regional Research* 38, no. 5 (2014): 1678–96, https://doi.org/10.1111/1468-2427.12159.

[474] Lowry, "Russia's Post-Neoliberal Development Strategy and High-Technology Considerations," 130.

can be seen from the fact that there was a strong preference for vertical industrial policy in which the state directs its industrializing impetus to politically favored industrial sectors. The state's particular preference were the sectors that would not only rejuvenate struggling industries that once underlined Soviet technological success but also generate the highest value added and export revenue earning. Designated by law in 2008 as strategic, the sectors included four high-tech industries, especially aerospace, armaments, nuclear technology, and shipbuilding and several manufacturing industries that have economic and security importance for Russia. These industries were accompanied by critical intermediating and infrastructural sectors, such as transportation, communications that hold the economy together.[475] The figure below describes critical manufacturing industries in which the state has a direct interest and decisive say regarding the foreign interactions. In strategic sectors, the state allowed foreign companies to own less than 50% of shares. However, if the ownership reaches 50% or over, a foreign company needs permission from the prime minister-led commission. Also, foreign companies need permission from the prime minister-led commission to own more than 25% of a strategic company.[476]

Figure 17.

Another important priority of the Putin's strategic industrial policy that aimed to strengthen state capitalism was the creation of new entities, so-called "state corporations" in key industries that served as new vehicles of nationalizations and realizing national developmental projects.[477] The establishment of state corporations that combined business and governance was an innovative breakthrough for Russian state capitalism under Putin after 2005. In the long run, state corporations were meant to transform into "institutions of development". However, the organizational concept and rationale behind these establishments raised doubts as to the real intentions behind them. Unlike other state-owned enterprises, state corporations were

[475] Ericson, "The Russian Economy in 2008."
[476] Kari Liuhto, "Genesis of Economic Nationalism in Russia," *Electronic Publications of Pan-European Institute*, 2008, 3–6.
[477] R. G. Gidadhubli, "Putin's Economic Formula for Russia," *Economic and Political Weekly* 42, no. 49 (2007): 20–21.

set up as NGO-type nongovernmental organization with property ownership, each of whose goals, functions and funding sources were defined by separate individual law.[478]

There are several features of state corporations that make them distinct from ordinary state-owned enterprises.[479] First, when state property is transferred to state corporations, they automatically absorb the property as its own, after which the control over these assets will fall under the corporations' supervisory boards and the president's prerogative who appoints their CEOs. According to Aslund, production assets transferred to these entities accounted for $80 billion worth of state assets along with $36 billion capital infusion, which, then Ministry of Finance Alexei Kudrin says, amounted to the massive privatization of state assets.[480] Second, state corporations are not obliged to generate a surplus for the state, but they instead operate under a "closed circuit system" in which generated surpluses will be directed to the organization itself. Finally, unlike other non-profit organizations, state corporations were not subject to the compulsory oversight.[481]

Such policies were, however, the deliberate strategy of the state-led economic modernization scheme that political leadership designed. The official reasoning was that subjecting developmental policy to multiple government organizations will slow down the process and disperse responsibilities. Thus, the creation of state corporations as entities to direct state assets and funds under an executive team subordinated to the president became an ultimate means of realizing industrial developmental objectives.[482] Acting as national champions and bypassing the stage of imitative development, these corporations meant to promote the diversification of Russia's economic structure and develop high-technology industries. By mid-2008 there were eight such major state corporations with different contents and legal forms: four cash funds and four industrial assets, six of which were noncommercial NGO type corporations and two were open joint stock companies. United Aircraft Building and United Shipbuilding Corporations became open joint-stock companies in which the state held majority

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[478] Aslund, *Russia's Crony Capitalism*, 105.
[479] Liuhto, "Genesis of Economic Nationalism in Russia," 2008.
[480] Aslund, *Russia's Crony Capitalism*, 134.
[481] Joseph Dresen, "The Role of State Corporations in the Russian Economy," Wilson Center, 2012, https://www.wilsoncenter.org/publication/the-role-state-corporations-the-russian-economy.
[482] Alexander Rodygin, "Russia En Route to State Capitalism?" Russia in Global Affairs, 2004, https://eng.globalaffairs.ru/articles/russia-en-route-to-state-capitalism/.

ownership.[483] Russian Technologies (Rostec) and Russian Nuclear Corporation (Rosatom) were two noncommercial corporations with consolidated industrial assets in defense and nuclear industries, while state development bank VEB, Russian Corporation for Nanotechnologies (Rosnanotec), Russian Olympics Construction (Olimpstroi), and the Housing Municipal Infrastructure Development Fund became the cash funds that aimed to invest in significant public projects, including infrastructure, communications and R&D.

The establishment of United Aircraft Corporation (OAK) and United Shipbuilding Corporation (OSK) as early state-owned holdings in 2006 and 2007 was a manifestation of Russia's transition towards state capitalism in heavy industries.[484] OAK was established as a mega-aircraft construction company in 2006 following a presidential decree of Putin with the aim of uniting all aircraft producers under a single structure and increase Russia's share in global aviation from 3 to 9 percent by 2025.[485] The core of the company consisted of the merger of private corporation Irkut with other low efficient state-owned enterprises, including airline producer Sukhoi, MiG, Tupolev and Ilyushin. The decree stipulated that the state would own at least 75% authorized capital, while making the remaining shares available for sale on Russian and foreign exchanges.[486] Other than the drive for re-nationalization, the consolidation of assets in the aircraft industry also appeared to be a successful lobbying attempt that aimed to bring subsidies and save inefficient and low-profitable enterprises that went through serious contraction after the Soviet collapse.[487] It made considerable sense from the perspective of strategic policy; as the largest percentage of revenue from foreign military sales comes from OAK's fighter aircraft, political leadership wanted to keep state holdings competitive against other global leaders such as Boeing and Airbus. Similarly, OSK aimed to consolidate primarily

[483] Vadim Volkov, "Russia's New 'State Corporations': Locomotives of Modernization or Covert Privatizations Schemes?," *PONARS Eurasia*, 2012, https://www.ponarseurasia.org/russia-s-new-state-corporations-locomotives-of-modernization-or-covert-privatizations-schemes/.

[484] Helge Blakkisrud and Daniel Fjærtoft, "Exit State Corporations? Exploring the Legacy of Putin's 'State Capitalism'" (Working Paper 2009-001, Norwegian Institute of International Affairs, 2009)

[485] Konstantin Lantratov, "The planes were shown the right path," *Kommersant.ru*, 2007, https://www.kommersant.ru/doc/795693.

[486] Anna Lowry, "Between Neopatrimonialism and Developmentalism: Exploring the Causes of Nationalization in Russia" (Bloomington, Indiana University, 2014), 172, https://www.proquest.com/openview/fd3cf480a97ecb0c0ca899ff471fe0c6/1.pdf?pq-origsite=gscholar&cbl=18750.

[487] Helge Blakkisrud and Daniel Fjærtoft, "Exit State Corporations? Exploring the Legacy of Putin's 'State Capitalism'" (Working Paper 2009-001, Norwegian Institute of International Affairs, 2009), 12

state-owned shipbuilding industries that were scattered around different regions in three major centers.[488] In this way, OSK appeared to devour existing enterprises, including private ones, in its new structure for the sake of efficiency. Although Russian ships had not been competitive in the civilian sector, OSK aimed to target a niche market that provided military ships and nuclear-powered icebreakers for offshore platforms and oil and gas exploration.

Following the industrial restructuring of aviation and shipbuilding, political leadership designed a new structure for state sector in defense, nuclear and nanotechnology industries.[489] All civil nuclear power plants and construction companies, as well as nuclear enrichment facilities were transferred to the newly created state corporation Rosatom, while Rusnano was granted to be the first state corporation to executive state policy nanotechnology and develop infrastructure in the sector.[490] However the final brick in the house of Russian state capitalism, was the establishment of noncommercial state corporation Russian Technologies (later changed to Rostec) in 2007 through the transfer of state-owned assets in defense-related industries that formerly belonged to Rosoboronexport, the intermediary agency for military arms exports (izvestia). Rosoboroneksport (ROE) became an industrial behemoth on behalf of state, having a monopoly over the export Russian military products over 80 countries.[491] ROE had earlier conducted "de-privatization" by acquiring several strategically important private enterprises in heavy industries, including AvtoVAZ, the automobile manufacturer and VSMPO-AVISMA, the world's largest manufacturer of titanium and aluminum alloys.[492] Since then, Rostec aggressively acquired similar state assets in other sectors such as machine-building, chemical, engineering and other industrial enterprises. In 2008, President Medvedev granted Rostec ownership of 426 enterprises in different industries, 246 of which were largely privately owned. Of these, some 280 were on the list of Russian strategic companies and 20 were single or

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[488] Aleksei Aronov, "Shipbuilding Will Be Consolidated into a Corporation," *Current Digest of the Post-Soviet Press*, April 11, 2007.
[489] Liuhto, "Genesis of Economic Nationalism in Russia," 2008.
[490] Connolly, "The Empire Strikes Back."
[491] Stephen Blank, "Ivanov, Chemezov, and State Capture of the Russian Defense Sector," *Problems of Post-Communism* 55, no. 1 (January 2008): 49–60, https://doi.org/10.2753/PPC1075-8216550105.
[492] André Nilsen, "Russian Capitalism," *The Oxford Council on Good Governance*, Economy Briefing, no. 2 (2006): 2–4.

dominant employers in one-company towns.[493] Currently Rostec owns stakes in 663 companies, which are part of 13 holdings, including 8 in the military-industrial complex and 5 in civilian sectors that include Oboronprom (a monopoly in the field of helicopter construction), Defense Systems (a manufacturer of air defense systems), VSMPO-AVISMA Corporation (the world's main supplier of titanium), and CJSC Russpetsstal (a manufacturer of special steels and alloys for MIC).[494] Through these acquisitions, Rostec aimed to assist in the development, production, and export of strategic high-tech civilian and military industrial products by attracting investment from and forming cooperation with other industrial actors and states. These efforts would then strengthen the economy and increase Russia's bargaining power in dealing with foreign companies.[495]

An important sector that Rostec aimed to reinvigorate was the defense industry whose survival came to depend on the exports of arms and military equipment.[496] The military-industrial complex was the backbone of hyper-militarized economy of the Soviet Union. However, the share of the industry dropped from 25 percent of GDP during Soviet times to 5 percent in 1997, with arms exports earning only one-tenth the income of energy exports.[497] Against this backdrop, Putin himself once mentioned that the military-industrial complex must "serve as fuel to feed the engines of modernization in Russia's economy."[498] Rostec was meant to play an important role as rescuing machine. As the former deputy head of Rosoboronexport and current head of Rostec Sergei Chemezov said "our mineral deposits are finite… and

[493] STEPHEN BLANK, "A Work in Regress? Russian Defense Industry and the Unending Crisis of the Russian State: Stephen Blank," in *The Russian Armed Forces in Transition*, ed. Roger McDermott, Bertil Nygren, and Carolina Pallin (London: Routledge, 2011).
[494] Lowry, "Between Neopatrimonialism and Developmentalism: Exploring the Causes of Nationalization in Russia," 129.
[495] Susanne Oxenstierna and Fredrik Westerlund, "Arms Procurement and the Russian Defense Industry: Challenges Up to 2020," *The Journal of Slavic Military Studies* 26, no. 1 (January 2013): 1–24, https://doi.org/10.1080/13518046.2013.757135.
[496] Julian Cooper, "From USSR to Russia: The Fate of the Military Economy," in *Handbook of the Economics and Political Economy of Transition*, ed. Paul Hare and Gerard Turley (London: Routledge, 2013), 245.
[497] Sim, *The Rise and Fall of Privatization in the Russian Oil Industry*, 2.
[498] Richard Connolly and Cecilie Sendstad, "Russia's Role as an Arms Exporter: The Strategic and Economic Importance of Arms Exports for Russia," Research Paper (Chatham House Royal Institute of International Affairs, 2017), 3.

fluctuates… but high technology, including for military use, can be refined without end."[499] According to him, the Russian defense sector indirectly involves 70% of all industry in the country. Within several years the corporation's exports increased by 50%, reporting 38.5 billion rubles in net profit in 2012. It was estimated that three corporations, Rostec, United Aircraft Corporation, and United Shipbuilding accounted for around three-quarters of the defense-industrial production in Russia. Within these structures, Rostec makes up 23% of all sales in the defense sector that provide hard currency for the state.[500]

State intervention in strategic sectors of economy through the ownership of corporations also came hand in hand with the channeling of state investment into these sectors that reflects the state's increased influence over the financial sector under Putin's leadership. Similar to the real sector re-nationalizations described above, public ownership rebounded in the financial sector as well where the state gave priority to national champions in banking or the state developmental banks that facilitate the state's industrial developmental model.[501] Rather than the physical allocation of assets as with the command economy, the current approach to implementing this developmental model under Putin took the form of state investment through state banks (Elena). Thus, significant economic activity has been directed from financial commanding heights, built around several key state banks.

The financial sector in post-Soviet Russia has been in a state of flux; over two decades, the ownership pattern in banking "made a dramatic shift from a complete state monopoly to a highly dispersed and mainly privately-owned financial sector and back to state control again."[502] Although the state withdrew from the commercial banking sector in the wake of shock therapy reform during 1990s, the main branches of state monobank Gosbank, including Sberbank (state saving bank) and Vneshtorgbank (foreign trade bank), were not subject to genuine

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[499] Anastasia Stognei, "One to Watch: Rostec's Sergei Chemezov Makes Political Waves," *The Bell*, 2019, sec. Weekly, https://thebell.io/en/one-to-watch-rostec-s-sergei-chemezov-makes-political-waves/.
[500] Stephen Blank, *Rosoboroneksport: Arms Sales and the Structure of Russian Defense Industry* (Strategic Studies Institute, U.S. Army War College, 2007), 13.
[501] Andrei V. Vernikov, "Russian Banking: The State Makes a Comeback?," *BOFIT Discussion Papers*, no. 24 (2009): 15–20, https://doi.org/10.2139/ssrn.1539988.
[502] Svetlana Kirdina and Andrei Vernikov, "Evolution of the Banking System in the Russian Context: An Institutional View," *Journal of Economic Issues* 47, no. 2 (June 2013): 480, https://doi.org/10.2753/JEI0021-3624470221.

privatization.[503] Yet, the weakening state control amid total absence of institutional and legal environment led to the chaotic setting where the insiders of various *spetsbanki*, specialized state-owned banks covering various field of activity, plundered the assets and physical infrastructure of banks. Also, market reform and privatization ensued rapid growth of private commercial banks. There were several thousand private banks operating by the end of 1990s, which shrank the market share of the state sector 30% by 1998.[504] However, these banks, as Conolly argues, did not function as an intermediary to facilitate savings and investment and acted instead as "pocket banks" to unscrupulous oligarchs, becoming parasites that sucked resources from the state and used their illicit gains to facilitate the acquisition of state property during privatization.[505] Subsequently, the Russian ruble crisis in 1998 that resulted from state default on its domestic debt, dealt a blow to the precarious financial system, evaporating many of these phantom banks.

A gradual but continuous reengagement of government with the banking industry began only after the financial crisis. The reform policies of Putin's new government during early 2000s adopted measures that strengthened the institutional foundations of the financial system.[506] Along with improved bank regulations and supervision, the government announced full capital account liberalization in 2007 that led to the equity market boom. However, the financial system remained relatively small, too much bank-centric, and dependent on the foreign capital.[507] These internal weaknesses were revealed in the 2008 financial crisis that drained the budget surplus as government was forced to buy capital shares of several struggling banks and credit organizations.[508] Later in 2013, worries that the problematic banking system would fail led authorities in the Russian Central Bank (CBR) to start a massive cleanup of the system that

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[503] Koen Schoors, "The Fate of Russia's Former State Banks: Chronicle of a Restructuring Postponed and a Crisis Foretold," *Europe-Asia Studies* 55, no. 1 (January 2003): 78, https://doi.org/10.1080/713663445.
[504] Pekka Sutela, *The Political Economy of Putin's Russia* (Routledge, 2013), 169
[505] Richard Connolly, *Russia's Response to Sanctions: How Western Economic Statecraft Is Reshaping Political Economy in Russia* (Cambridge: Cambridge University Press, 2018), 157–58
[506] Erik Berglof and Alexander Lehmann, "Sustaining Russia's Growth: The Role of Financial Reform," *Journal of Comparative Economics*, Special Symposium in Honor of Padma Desai, 37, no. 2 (June 1, 2009): 198–206, https://doi.org/10.1016/j.jce.2009.01.003.
[507] Connolly, "Financial Constraints on the Modernization of the Russian Economy," 435.
[508] Pekka Sutela, "Financial and Credit Markets," in *The Oxford Handbook of the Russian Economy*, ed. Michael Alexeev and Shlomo Weber (London ; New York: Oxford University Press, 2013),

revoked licenses of several small banks. As a result, a number of banks in Russian decreased from 1,058 to 484 from 2010 to 2019.[509]

Figure 18.

The core characteristics of the Russian financial system designed under Putin's leadership feature several important traits. On the macro level, the banking sector amounts to what Vernikov describes as "three tier system": apart from the central bank and regular commercial banks, the backbone of the banking sector consists of state-controlled banks.[510] As with the real sector, state ownership became an important pillar in the banking system.[511] The ownership structure of banks is quite complicated in the Russian legal system and disguises who wields real influence. All banks with state participation can be classified into three broad categories; *state-owned banks* in which the state (or SOE) owns majority stake, *state-controlled banks* where the state, though owning a minority stake, influences decision making via direct or indirect governance and finally *state-influenced banks* in which the state exert political influence through different channels other than ownership and governance.[512]

Expansion of state-owned and controlled banks in the market share started in 1999 from around 36%; over the years, the market share of these banks swelled up through a combination of dynamic growth and acquisition of other financial institutions, including private banks and public funds. State ownership of banks also grew after the financial crisis in 2008 when state-owned banks absorbed several medium-sized private banks near bankruptcy.[513] Furthermore, four of top six private banks, including Otkrytie and Promsvyazbank were nationalized following the clean-up efforts. The original database by Vernikov gives a precise measure for the scope of state-controlled banks in Russia. According to him, the assets of state-controlled banks grew over 62% between 2000 and 2011, while those of other banks grew only by 29%.[514]

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[509] David Szakonyi, "Banking on Politics: How Russia's Banking Sector Clean-Up Affects Regime Stability" (PONARS Eurasia, 2019), 4–5, https://www.ponarseurasia.org/banking-on-politics-how-russia-s-banking-sector-clean-up-affects-regime-stability/.

[510] Kirdina and Vernikov, "Evolution of the Banking System in the Russian Context."

[511] Victor Gorshkov, "The State in Russia's Banking Sector," *KIER Discussion Paper* 1015 (2019): 1–12.

[512] Ekaterina Glushkova and Andrei Vernikov, "How Big Is the Visible Hand of the State in the Russian Banking Industry?," *MPRA Paper* No.15563 (2009): 5–6.

[513] Sutela, *The Political Economy of Putin's Russia*, 172.

[514] Vernikov, "The Impact of State-Controlled Banks on the Russian Banking Sector."

As of 2014, there were 854 registered banks in Russia and state-controlled banks, directly or indirectly, held almost 60% of all assets and liabilities in banking system.[515]

An important characteristic of the banking system in Russia is the presence of "national champions", several state-owned core banks with a focus on a particular sector such as agriculture, construction, and foreign trade.[516] The state has long nurtured these banks through special treatment such as direct cash injections and regulations. These banks operating as third-tier banks in the intermediate layer of the system include state corporation Vnesheconombank (VEB), the VTB Group banks (Foreign Trade Bank), Sberbank, Rosselkhozbank (Russian Agricultural Bank), and Gazprombank (indirectly owned by the state through gas giant Gazprom). Of these banks, VEB is an outlier; though it does not have a commercial bank license, VEB acts as a 100% state-owned development bank with the aim of stimulating investment activities in those projects that cannot receive funding from private investors. VEB's establishment in 2007 as a nongovernmental state corporation replaced the role of the former Bank for Foreign Economic Affairs in USSR. With assets amounting to $60 billion as of 2017, VEB provides special loans to large scale state projects and support large enterprises in Russia.[517]

Other important national champions are the commercial bank VTB and Sberbank. The VTB Group banks were established to service foreign trade and facilitate Russia's global economic integration. Over the years, the bank became the main instrument for foreign expansion of the Russia's capital overseas through its purchases and investments. According to Vernikov, VTB acquired twelve banks from 2002 to 2012: four in Russia, three in Europe, and five in former Soviet countries.[518] In Russia, VTB's major acquisition in 2011 included controlling stakes of Bank of Moscow and Transkreditbank. Another bank, Sberbank, majority-owned by the central bank, is an undisputed leader in the financial market. The bank handles the transactions of over half of Russian wages and pensions and nearly half of the market share for household deposits and housing loans.[519] Another is Rosselkhozbank, which assists the state

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[515] Connolly, "Financial Constraints on the Modernization of the Russian Economy," 437.
[516] Vernikov, "Russian Banking."
[517] Aslund, *Russia's Crony Capitalism*, 124.
[518] A. Vernikov, "'National Champions' in Russia's Banking Services Market," *Problems of Economic Transition* 57, no. 4 (August 1, 2014): 12, https://doi.org/10.2753/PET1061-1991570401.
[519] BOFIT, "State Banks Dominate Russian Banking Sector," BOFIT, accessed December 9, 2020, https://www.bofit.fi/en/monitoring/weekly/2019/vw201901_2/.

in systematically financing agricultural projects. Sberbank, the VTB and Rosselkhozbank, the so-called "Big Troika", account for almost half of the country's banking assets (Vernikov national champions). In contrast, Russia's largest private bank, Alfa Bank, owned by oligarch Mikhail Fridman, controls only 4% of assets.

The analysis of statism in heavy industry and finance begs a question; what role does state control over these strategic sectors play for the regime's stability? The takeovers were always justified in some ways through official rhetoric; the reasoning behind active state control in heavy industry was justified by the need to develop value-added high-tech industry, while in finance the pretense was to ensure economic stability by tackling money laundering and enforcing transparency. The genuine desire to reproduce the regime's economic capability and long-term stability through technological innovation, diversification, and competitiveness under Putin's statist inclination can make sense.[520] Such a developmentalist agenda, in fact, can provide powerful rhetoric for the regime to renew its legitimacy.[521] However, strengthening state control over strategic sectors through new structures and acquisitions under the guise of developmentalism transcends economic rationale; rather it is a planned course of action in line with the personalization of power that will advance other political objectives.[522] Importantly, following the turbulent years, state control over key sectors aims to concentrate political control over key economic activities and maintain elite loyalty through patronage rents.

Table 11.

The state plans to make state corporations the power centers in each sector based on the consolidated assets of scattered state enterprises. This policy in turn allows the regime to maintain control over the biggest natural monopolies and certain strategic industries that provide revenue stream to the state. President Putin, for instance, personally names the supervisory and management boards as well as the general directors in these corporations, who tend to be from

[520] Katri Pynnöniemi, "Russia's National Security Strategy: Analysis of Conceptual Evolution," *The Journal of Slavic Military Studies* 31, no. 2 (April 3, 2018): 245, https://doi.org/10.1080/13518046.2018.1451091.
[521] Vladimir Gel'man, *Authoritarian Modernization in Russia: Ideas, Institutions, and Policies* (Routledge, 2016), 16.
[522] Blank, *Rosoboroneksport*.

his own inner circle. Through this control, the regime can also down the operations of non-Kremlin loyal Russian corporation, while increasing the bargaining power of Russia in dealing with foreign companies.[523] During the election cycle, these corporations can become important political machines by mobilizing their workers in the polls.[524]

Table 12.

As for the financial system, the special political role that banks play makes them essential for the political economy of the country. The main goal for state control over finance is to monitor independent financial activity that might produce political diversity. As shown in the case of developing countries, private ownership in banks tends to promote political competition as private actors with access to financial capital might fund opposition. Apart from political stabilization, these banks assist the state with providing liquidity channels and bailing out struggling institutions during the crisis, especially in 2008.[525] In normal times, they act as a financial glue that helps the state channel energy rents to other strategically important, but inefficient, sectors of the economy.[526] With an ability to tap on international financial markets, state banks act as an important vehicle for financing the state's developmental projects, implementing social programs, or conducting its geopolitical goals. For instance, the largest state banks account for almost 75 percent of all investments in infrastructure and strategic industries.[527] Famous examples include allocation of $50 billion from the National Welfare Fund to VEB for the construction of the Sochi Winter Olympics as well as the APEC summit, and 2022 FIFA World Cup.[528] Recently, state banks have enlarged their presence in emerging IT and retail industry as well, indirectly expanding the state's footprint in sectors that have political implications. The active player is Sberbank which is transforming from a bank an internet company through the buyout of shares from giant internet companies. Table 12 above provides a list of Sberbank's recent acquisitions. Although such moves might appear to be an

[523] Rodygin, "Russia En Route to State Capitalism?"
[524] Szakonyi, "Banking on Politics: How Russia's Banking Sector Clean-Up Affects Regime Stability," 7.
[525] Kalyuzhnova and Nygaard, "Special Vehicles of State Intervention in Russia and Kazakhstan," 58.
[526] Gaddy and Ickes, "Putin's Rent Management System and the Future of Addiction in Russia."
[527] Vernikov, "The Impact of State-Controlled Banks on the Russian Banking Sector."
[528] Aslund, *Russia's Crony Capitalism*, 125–26.

attempt for diversification, Sberbank's specific targeting of major IT companies signifies the absorption of big tech into the state's hand.[529]

4.3 The *state sector* in Kazakhstani economy under Nazarbayev

The previous section briefly delved into the state sector in Russia with a focus on strategic industries in which the state has prerogative. Following the same framework, this section analyzes the state sector in Kazakhstan, showing how Nazarbayev established his personal control over the energy and nuclear industries after consolidating his power. As the previous chapter showed, the state in Kazakhstan became an important player in economy after independence. Such a role increased even further following 2008 where the state started to act as an engine for the economy with several industrial policies. What is specifically interesting in Kazakhstan is that political leaders introduced the concept of state holding companies in the economy which absorbed the assets of dozens of SOEs and became the main instrument for state involvement in economy.

With the collapse of the Soviet Union, Kazakhstan inherited a highly centralized state-controlled economy with about 37,000 registered state-owned enterprises in literally all sectors of the economy. As elaborated in detail in the previous chapter, the political leadership in Kazakhstan prioritized two important pillars of the economy during the transition period: creating a market economy by inviting foreign direct investment through liberalization-cum-privatization.[530] Although FDI in Kazakhstan has been directed mainly towards its energy resources, it has had positive effect on economic growth after 2000 and has helped to develop the economy.[531] Scholars note that liberalization reforms of the 1990s paved the way for attracting FDI. At the same time, shock-style privatization shrank the size of the state in the economy. Privatization completed by 2004 by which time many firms went into private

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[529] Szakonyi, "Banking on Politics: How Russia's Banking Sector Clean-Up Affects Regime Stability," 9–10.
[530] Ken Charman, "Kazakhstan: A State-Led Liberalized Market Economy?," in *Varieties of Capitalism in Post-Communist Countries*, ed. David Lane and Martin Myant, Studies in Economic Transition (London: Palgrave Macmillan UK, 2007), 169, https://doi.org/10.1057/9780230627574_9.
[531] Avinash Waikar et al., "Impact of Foreign Direct Investment on Kazakhstan's Economy: A Boon or a Curse," *International Journal of Business and Social Science* 2 (January 1, 2011): 93–94.

hands.[532] The private sector grew to contribute 65% of GDP in 2004 moving closer to, although still below the level of, developed market economies.[533]

However, leadership never downplayed the importance of an active state role in the economic reform processes. The role of the state was important for promoting a mixed economy with a strong focus on social policies, combining the competitive self-regulation of production and the state regulation of economic processes. President Nazarbayev himself called for an economic model that required state participation, stating that "our strategy of healthy economic growth is based upon strong market economy, active state's role and attraction of significant foreign investments."[534] Along with designing a stable political structure that provided a strategic direction in the exploitation of Kazakhstan's natural resources, the government clearly played a significant role in the creation of laws and regulations and developing policies for to improve the business environment.

Apart from a regulatory role during the transition, the state retained limited influence over certain sectors of the economy through ownership of state-owned enterprises. The corporate structure of these enterprises that remained as legacy of Soviet central planning necessitated the active involvement of the state.[535] After the completion of privatization in 2005, the state retained 100% ownership of fifteen joint-stock enterprises in natural monopolies and strategic sectors, each one reporting to a ministry. There also remained a large number of state enterprises that did not issue shares.

However, since 2005 the role of the state has become central not only in coordinating the parts of economy it dominates, but also in shaping the country's overall economic direction towards state-led capitalism.[536] First, the state started to regain its dominance over strategic sectors such as energy through economic nationalism amid the pervasive presence of international companies. Soon after, the financial crisis in 2008 set the stage for Kazakhstan to become a state capitalist economy in which the state expanded its interventionist role over not only strategic sectors, but also other severely affected industries, including finance, real estate,

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[532] Olcott, *Kazakhstan*, 143.
[533] "Transition Report 2005: Business in Transition" (London: EBRD, 2005), 142–45.
[534] IBP Inc, *Kazakhstan Investment and Business Guide Volume 1 Strategic and Practical Information* (Washington, D.C: International Business Publications, 2016), 100–101.
[535] Roman Vakulchuk, *Kazakhstan's Emerging Economy: Between State and Market* (Bremer: Internationaler Verlag der Wissenschaften, 2014),
[536] Charman, "Kazakhstan."

agriculture, and construction.[537] Following the 2008 financial crisis, the government shifted the emphasis in its development strategy in 2010–11 toward growth from non-oil sources through diversification, innovation, investment in human capital, and international trade integration for job creation.[538] In order to stabilize the situation, the state retained its control over the economy through a newly established holding company, Samruk-Kazyna, that aimed to promote fiscal stimulus and industrialization over 2010-2015. As this chapter explains in detail, Samruk-Kazyna came to control enterprises in the country's leading sectors, including the extractive sector, transport and storage, and information and telecommunications, either in whole or in part. Altogether, Samruk-Kazyna and its subsidiaries account for an estimated 30% of total employment and more than 50% of economy.[539]

There were 27,6728 registered state-owned legal entities in Kazakhstan as of 1 January 2015, of which 1,002 employed more than 250 people. Defining SOEs broadly, including all public entities rather than only corporatized enterprises, brings the total more than 25,000 entities (although around 13,000 of these are schools and hospitals). According to the Department on the Policy of Managing State Assets, the total number of SOEs in Kazakhstan is 6,948, including 679 JSC's and LLP's, the rest being state enterprises under the right of economic management, 1,258 entities or operational management, 5,011 entities. The assets of the more than 750 national and municipal corporatized SOEs in operation are valued at 30–40 percent of GDP. As the numbers show, SOEs still dominate the Kazakh economy. In an economy heavily dependent on extractives, a large role for SOEs may not surprising, but interestingly, SOEs are pervasive in all sectors, including in critical network services like electricity and in products and services that have traditionally supported a broad set of diverse suppliers at all enterprise levels. The major SOEs represent mostly natural resource industries, including oil, gas, and metals mining, as well as the financial and transportation sectors. Seven companies out of ten were involved in the production of mineral resources. The remaining three are Kazakh Temir Joly (railway), the BTA Bank and Kazkommercbank.

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[537] V. Mikheev, "Prospects for Relations Within the Russia-China-Kazakhstan Triangle Under Conditions of Global Crisis," *Problems of Economic Transition* 53, no. 5 (September 1, 2010): 10, https://doi.org/10.2753/PET1061-1991530501.
[538] T Luly, "The Varieties of Capitalism Dichotomy (and Beyond) in Post-Communist States," *Vestnik* 11 (2012).
[539] Pomfret, *The Central Asian Economies in the Twenty-First Century*, 123.

These major and almost all other minor 700 SOEs are combined under three state holding companies, including Samruk Kazyna, KazAgro, and Baiterek Holdings. These holding structures dominate the economy and control energy, transport, utilities, SME financing, agriculture finance, and product development.[540] These holding entities and the SOEs under their management dominate state sector industries which are normally open to private participation, such as oil and gas production, electricity, transport, and telecoms. According to the OECD's Index of State Control, Kazakhstan has a greater presence of SOEs in the economy than any OECD member and most large non-OECD economies.[541] These state-owned economic structures can influence policies and competition in both individual sectors and economy wide. SOEs are in a strong position to influence government policy in all sectors of the economy, either though government participation in management boards, or other means. SOEs have influence not only through their direct presence, but also through their ability to influence policy, such as through their privileged access to government, which participates directly in their management boards.

When it comes to economic sectors where state companies are involved, manufacturing remains highly concentrated in resource-based and capital-intensive sectors. Manufacturing is very concentrated in resource and capital heavy activities, with petroleum-based products and basic metals and minerals accounting for close to two-thirds of manufacturing output. The minerals sector has large potential, although investment has been unimpressive. Kazakhstan is the world's leading producer of various minerals, including 40 percent of global uranium reserves, 30 percent of the world's reserves of chrome, 25 percent of manganese, 13 percent of lead and zinc, 10 percent of iron ore, and 10 percent of copper.[542] According to an EITI report, Kazakhstan received a revenue of USD$19 billion from the extractive industry in 2017. More

[540] World Bank, "A New Growth Model for Building a Secure Middle Class : Kazakhstan Systematic Country Diagnostic" (World Bank Group, 2018), 43–46, https://openknowledge.worldbank.org/handle/10986/29792.
[541] EBRD, "Kazakhstan Country Assessment," In Life in Transition: A Decade of Measuring Transition (London: EBRD, 2016).
[542] World Bank, "A New Growth Model for Building a Secure Middle Class : Kazakhstan Systematic Country Diagnostic," 37.

than half of these revenues came from hydrocarbons, and the remaining revenues were derived from mining, with iron, copper, and gold as the major commodities.[543]

Figure 19.

4.3.1 The oil industry: the rent source in between the family, elite and the people

Although Kazakhstan flirted with the idea of democracy and political participation in the early years following transition, the country ended up being more like a family run business under president Nursultan Nazarbayev than a liberal democracy.[544] In fact, scholars admit that any narrative about the regime and its trajectory after independence without a reference to the personality of Nazarbayev would be incomplete. Nazarbayev ruled the country for over 26 years since he was elected as its president in 1991 through a combination of formal and informal mechanisms; the former included institutional manipulation and increased centralization while the latter required patronage politics.[545] According to Peyrouse, Nazarbayev's patronal system is based on "principles of loyalty to one's superior, that is, to the one who distributes administrative status and financial resources to his subordinates in accordance with his or her own strategies of promotion."[546] In this type of patronage politics, Hale maintains, only the ruler, who is able to align the competing interests of the elite, can sustain the stability of his regime because the elite might at any time cooperate to oust the ruler.[547]

However, for Nazarbayev to maintain the stability of his regime, building up his patronage system and ultimately asserting political legitimacy over it would be impossible if not for the ample wealth beneath Kazakhstan's soil. In the Kazakh *rentier state*, the conservation of power accompanies the embedding of the elites in family, business, and cliental structure. But the bigger puzzle of how exactly oil wealth helped Kazakh regime to maintain stability still calls for a thorough explication. Delving into the puzzle necessitates a general overview of the oil industry in Kazakhstan.

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[543] EITI, "The 13th National Report: On the Implementation of the Extractive Industries Transparency Initiative in the Republic of Kazakhstan for 2017" (Oslo: Extractive Industries Transparency Initiative, 2017).
[544] Franke, Gawrich, and Alakbarov, "Kazakhstan and Azerbaijan as Post-Soviet Rentier States."
[545] Cummings, *Kazakhstan*, 2005, 43.
[546] Peyrouse, "The Kazakh Neopatrimonial Regime," 356.
[547] Henry E. Hale, *Patronal Politics: Eurasian Regime Dynamics in Comparative Perspective* (Cambridge: Cambridge University Press, 2015), 72

Following independence, oil has served as the blood in both the political and economic life of Kazakhstan due to the wealth it generates and the conflicting interests that accompany that wealth. The regime trajectory in the wake of independence and its subsequent consolidation under the fist of Nazarbayev are hence intrinsically linked to economic development in which hydrocarbon reserves played substantial role.[548] In fact, the IMF labeled Kazakhstan as a hydrocarbon rich country since crude petroleum accounts for more than one third of state revenue and 60% of total exports as of 2012. With proven hydrocarbon reserves of around 30 billion barrels, Kazakhstan is among the 12 largest oil-exporting countries in the world.[549] Based on the importance of oil in its economy, Ostrowski calls Kazakhstan a classic *rentier state* in Central Asia.[550]

Historically speaking, Kazakh oil remained underdeveloped for decades under Soviet rule, though still deemed the jewel of the Caspian with its potential. Although meager production of oil started during the 1960s, the Soviets only made a breakthrough in the 1980s with the discoveries of huge oil reserves such as Tengiz (6 to 9 billion barrels of oil), Karachaganak (1,300 bcm of gas and 6.8 billion barrels of condensate and some crude oil), and Kumkol (400 million tons of oil).[551] Yet the full potential of these oilfields went unrealized at the time due to the technical difficulties and availability of other fields in Siberia and Baku. Before independence, Kazakhstan's local oil production fields were run by state-owned enterprises and most of the country's oil output came from the five largest state enterprises: Aktobemunaigas, Embamunaigas, Mangistaumunaigas, Tengiznunaigas, and Yuzhneftegas, which can be seen below in figure 20.[552] During Soviet times, the oil industry in Kazakhstan was controlled and run by responsible ministries and institutions in Moscow. Nonetheless, the institutional vacuum was sometimes filled by so-called *neftyannik*, a group of nascent oilmen in the country who served as middlemen between the center and region.[553]

[548] Hoffman, "Oil and State-Building in Post-Soviet Azerbaijan and Kazakhstan," 129.
[549] Asian Development Bank, *Kazakhstan: Accelerating Economic Diversification* (Asian Development Bank, 2018), 33, https://www.adb.org/publications/kazakhstan-economic-diversification.
[550] Wojciech Ostrowski, "Rentierism, Dependency and Sovereignty in Central Asia," in *Sovereignty after Empire: Comparing the Middle East and Central Asia*, ed. Raymond Hinnebusch and Sally Cummings (Edinburgh University Press, 2011), 282–303
[551] Cummings, *Oil, Transition and Security in Central Asia*, 78.
[552] Pauline Jones Luong and Erika Weinthal, *Oil Is Not a Curse: Ownership Structure and Institutions in Soviet Successor States* (Cambridge University Press, 2010).
[553] Ostrowski, *Politics and Oil in Kazakhstan*, 63.

Figure 20.

Despite the largesse of resources, the fate of the economy at large and particularly the oil industry was in a shambles with the fall of Soviet Union. As Olcott states, in the wake of independence Kazakhstan's energy grids, industrial plants, and oil refineries were entirely interlinked with the other Soviet republics, especially Russia.[554] The government, being literally broke, had no other option than the privatization of major industries and the attraction of foreign investment. Therefore, the government, as a part of its privatization program, started to aggressively privatize the oil and gas industry from 1993 under Prime Minister Kazhegeldin, allowing investors to hold up to 100 percent equity.[555] As a result, the country's major oil reserves went to the hands of private investors, such as Chevron and Mobil, which brought around $14 billion in investment to the industry. Interestingly in this process, the regime needed a strong institutional bastion to administer the oil industry and carry out contract negotiations with foreign investors on behalf of the government, leading to the dissolution of Soviet style ministerial control over the oil industry and giving rise to the new institution, Kazakhoil, National Oil and Gas Company in 1995, which later allowed Nazarbayev to assert his grip not only on the industry but also on the regime itself.[556]

Rent from natural resources, particularly the hydrocarbon windfall, was manna from the heaven for the ailing economy of Kazakhstan after the collapse of Soviet Union. The president was aware that oil wealth would be the primary source of government revenue and for the spoils we would need for the patronage network he was about to build for his consolidation of power. However, to reap the full oil bonanza, Nazarbayev first had to ensure his firm grip on the industry, which was based on the old Soviet style corporatist structure. In the wake of independence, this structure resulted from the horizontally-organized Soviet oil industry with a mixture of ministries responsible for different parts and various groups that represented their interests.[557] In keeping with the Soviet legacy, in 1992 Kazakhstan established three institutions for organizational matters; the National Oil Company (NOC) Kazakhstanmunaigaz to engage

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[554] Olcott, *Kazakhstan*, 121.
[555] Ostrowski, *Politics and Oil in Kazakhstan*, 49.
[556] Hoffman, "Oil and State-Building in Post-Soviet Azerbaijan and Kazakhstan," 177.
[557] Gustafson, *Crisis amid Plenty: The Politics of Soviet Energy under Brezhnev and Gorbachev*, 10.

in oil development, production and transportation, the Ministry of Energy and Fuel Resources to regulate oil production, and finally the Ministry of Geology and Protection of Mineral Resources to determine the direction of the industry.[558] Initially, Kazakhstanmunaigaz was modeled on its Russian counterpart, Rosneft, that aimed to become the central oil body in charge of directing the industry in the world market independently. However, in the beginning Kazakhstanmunaigaz merely assisted with the sell-off of its assets to foreign oil companies. Instead, the stronger role was given to the Ministry of Oil and Gas, to which the company was subordinate.

In the early years, Nazarbayev felt the need to retain a corporatist structure for the sake of balancing different interests and to not antagonize the oilmen in the country.[559] However, the corporatist structure deteriorated in the face of the ongoing privatization programs that swept the country. Furthermore, this corporatist structure would inevitably strip up competition for influence following the emergence of strongman. Nazarbayev's concern with the emergence of strongman manifested in the example of Ravil Cherdabaev, an oilman from western oil city of Atyrau, after he became the Minister of Oil and Gas. Cherdabaev's move in the ministry was directed to the creation of a single national oil company, Kazakh Oil, which would be responsible for the production and refining of oil under his ministry. This new structure required that the whole industry would be brought under Cherdabaev's control, the very scenario that Nazarbayev wanted to avoid from the outset. Furthermore, with the help of power accumulated during privatization, Cherdabaev also started positioning his brothers in important posts in other oil companies and regions. The same scenario followed years later with Akezhan Kazhegeldin, a former KGB officer whom Nazarbayev appointed as prime minister to spur the privatization program.[560] Over the years of privatization, Kazhegeldin built influence over the oil industry as well as his own independent power base which he used to challenge the president in later years.[561]

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[558] A.D. Koen, "Kazakh State Oil Enterprises Move toward Privatization," *Oil and Gas Journal* 93, no. 34 (August 1995): 48–52.
[559] Martha Brill Olcott, "Pipelines and Pipe Dreams: Energy Development and Caspian Society," *Journal of International Affairs* 53, no. 1 (1999): 314.
[560] Sally N. Cummings, "Kazakhstan: An Uneasy Relationship – Power and Authority in the Nazarbaev Regime," in *Power and Change in Central Asia*, n.d., 228.
[561] Ostrowski, *Politics and Oil in Kazakhstan*, 36–37.

Alarmed by the threat posed by these potential challenges as well as his fear of losing control over the industry, Nazarbayev took charge by dismissing all responsible ministries and establishing in their place NOC KazakhOil in 1995. With the transfer of nearly all ministry functions to KazakhOil, Nazarbayev "shifted control over the country's oil industry, firmly to within the presidential apparatus, and away from the jurisdiction of the Prime Minister."[562] KazakhOil accounted for about one-fifth of oil produced in Kazakhstan in 2001, while oil revenues made up one-third of Kazakhstan's budget. Soon in 2002, the oil industry saw another institutional change; as a result of the merger with Kaztransneftegaz (national oil and gas pipeline company), Kazakhoil was transformed into the Joint Stock Company KazMunaiGaz (KMG), the principal backbone of the economy that today controls the state's interest in the whole oil and gas sector.[563]

Created along the lines of western management style, KMG aimed to streamline relations between the government and foreign oil companies.[564] From the beginning, officials promoted the rhetoric that KMG would become a "national champion" in the strategic oil industry that protects government interests as the budget came to rely heavily on oil rents. Also, the resource nationalism that emerged through legal changes in 2005 allowed the state to exercise preemption rights on any oil assets put up for sale where KMG has to acquire mandatory 50 percent share in all new oil and gas projects.[565] Using these preemptive rights, KMG was able to increase its stake in almost all major oil and gas projects in the country and thus consolidate assets in the energy sector since 2005.[566] The famous cases of takeovers and acquisitions by KMG, as described in previous chapter, include MangistauMunaiGas (MMG), PetroKazakhstan, and the most recent dispute in Karachaganak.[567] Currently, the company owns shares in three major oil fields; 16.8% in Kashagan, 20% in Tengiz and 10% in Karachaganak. As a result of these acquisitions, KMG emerged as the second leading oil producer by 2008, owning about 30% of production and 40% of proved reserves in Kazakhstan

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[562] Hoffman, "Oil and State-Building in Post-Soviet Azerbaijan and Kazakhstan," 282.
[563] Ostrowski, *Politics and Oil in Kazakhstan*, 183.
[564] Martha Brill Olcott and Carnegie Endowment, "Kazmunaigaz: Kazakhstan's National Oil and Gas Company," *The James A. Baker III Institute for Public Policy, Rice University: Huston*, 2007, 13.
[565] Kennedy and Nurmakov, "Working Paper: Resource Nationalism Trends in Kazakhstan, 2004–2009."
[566] Orazgaliyev, "State Intervention in Kazakhstan's Energy Sector."
[567] Serik Orazgaliyev, "State Ownership and Nationalization in Energy Sector: The Case of Kazakhstan's Oil Industry," *ADBI Working Paper Series* No. 1042 (2019).

that earned the company $21 billion in 2008.[568] KMG was directly owned by the government of Kazakhstan until 2006, after which point the government-initiated reforms, concentrating state shares in KMG along with other state enterprises in the newly created Samruk holding company.

The analysis above begs a question: how has the control over oil industry helped Nazarbayev regime? The development of the energy industry and subsequent installation of state control over its rents proved important for the regime in three ways: 1) the provision of revenue for the struggling budget, 2) a rent source for elite co-optation and patronage and 3) provision of public spending. Most importantly, the oil industry provided the main source of revenue for the struggling state following the transition shock. The country's growth was fueled primarily by the hydrocarbon sector, which accounted for roughly 30 percent of the country's GDP and over half its total export revenue, USD$17.4 billion in 2005.[569] The share of oil-and-gas revenue to total government revenue grew from 17% in 1999 to 54% in 2011, while their share in the value of national exports grew from 8% to 63% during 1994–2014.[570]

Apart from revenue for the state, rents from oil industry became the family's privileged asset and a major source of self-enrichment. As the Kazakhgate scandal revealed, Nazarbayev's family received hundreds of millions of dollars ins their offshore accounts from contracts with global oil companies.[571] Starting from the consolidation of power, Nazarbayev introducing his network of relatives and family members into higher positions in the oil sector to ensure personal monitoring and supervision. Timur Kulibaev, a representative of one grouping of his "family" (his son-in-law), an important political formation in his circle, became the financial director and vice-president of KMG until 2005. His presence in the company was to ensure the protection of Nazarbayev and his family's interests. For a long time Kulibaev's grouping had focused on important spheres of the economy such as the oil industry, banking, and

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[568] Kennedy and Nurmakov, "Working Paper: Resource Nationalism Trends in Kazakhstan, 2004–2009."
[569] Adil Nurmakov, "Resource Nationalism in Kazakhstan's Petroleum Sector: Curse or Blessing?," in *Caspian Energy Politics : Azerbaijan, Kazakhstan and Turkmenistan*, Caspian Energy Politics : Azerbaijan, Kazakhstan and Turkmenistan. - London [u.a.] : Routledge, ISBN 0-415-69320-9. - 2010, p. 20-37 (London: Routledge, 2010), 29.
[570] Orazgaliyev, "State Ownership and Nationalization in Energy Sector: The Case of Kazakhstan's Oil Industry."
[571] Levine, *The Oil and the Glory*, 224.

communications. Besides the Kulibaev grouping, other groupings of the family emerged in other lucrative sectors of the economy that developed due to the oil boom.[572]

Apart from providing revenue for the state coffers that stabilized the economy, oil rents helped Nazarbayev knit together the elite under his control and built up the patronage system. Acknowledging the importance of elite support beyond his family and relatives, Nazarbayev began focusing on, creating a reliable and loyal network of his clients in the hydrocarbon sector and other lucrative sectors of economy that developed with the oil boom and privatization.[573] In authoritarian regimes like Kazakhstan, the grave threat to power often comes from within the inner circles of the president.[574] This efficient strategy of deterring the threat while simultaneously securing their loyalty is usually by means of spending the rents of resources that the regime possesses. The view of a professor in an interview basically expresses the situation in Kazakhstan: "When people are doing well financially, or owe their position to you, they don't want to see you out of office. If they see someone who is threatening to Nazarbayev, then they are inclined to go after that person."[575]

Establishing KMG was also important in two ways; first, it helped the regime get a larger portion of the rents from energy production with an expanded role in oil production while setting a precedent for country's uranium industry.[576] Second, it would end the elite struggle and establish a strong patronage around the oil industry. Observing the context of this change it can be argued that the preference for state ownership should be seen as a strategy to consolidate political power, not only because it provides the state with access to a greater portion of oil rents but also it increases its discretionary control over such income streams. Regardless, the national oil company KMG was the first messenger of the emerging state capitalism in the commanding heights, which would be personal cash machine for the president and tool for political patronage.

Furthermore, KMG also functioned as the principal mechanism in co-opting the emerging young oilmen (the insiders) and professionals (outsiders).[577] First in the oil sector, he

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[572] Peyrouse, "The Kazakh Neopatrimonial Regime."
[573] Junisbai, "A Tale of Two Kazakhstans."
[574] Geddes, Wright, and Frantz, "Autocratic Breakdown and Regime Transitions."
[575] Andrea Kendall-Taylor, "Full Article: Purchasing Power: Oil, Elections and Regime Durability in Azerbaijan and Kazakhstan," *Europe-Asia Studies* 64, no. 4 (2012): 755.
[576] Domjan and Stone, "A Comparative Study of Resource Nationalism in Russia and Kazakhstan 2004–2008."
[577] Ostrowski, *Politics and Oil in Kazakhstan*, 49.

commenced this process by appointing "the sons and daughters of ex-communist apparatchiks to the top positions through Kulibaev, primarily from Almaty in order to guarantee a young, efficient and professional generation of loyal fellowship."[578] These young technocrats kept their alliances with the president and served as bastions for him prior to consolidation of his power: chief among them were Kanat Bozumbayev (vice-president of KazTransOil), Berik Kanivey (vice-president KazakhOil) and others. The other important group, whose cooperation was inevitable, was the influential oilmen in oil rich regions of the country. Nazarbayev ensured their loyalty and support through providing them various lucrative projects with foreign companies. Through rewards in the form of positions in energy companies, Kazakh oilmen did not participate in political struggles against the president and supported their patron. Through the construction of a patron–client relationship built around the oil industry; the regime managed to successfully reproduce itself over the years. However, not all of them were satisfied with the status quo: oil rich peripheries proved challenging to the Nazarbayev regime with signs of dissent. So-called local interest groups in oil rich regions felt left out of the benefits of the oil boom, as they could not receive any contracts from major oil companies with regard to construction and supply.[579] To appease the increasing dissatisfaction of these groups, Nazarbayev utilized a so-called local content policy that required foreign oil companies to obtain service contracts from local companies.

Finally, the oil revenues helped the regime to ease public discontent through spending. The inherent nature of authoritarian rule demands that some portion of wealth is directed to the citizenry in addition to the ruling coalition, often referred to as the "targeted instrumentalization of oil rents." This redistribution usually takes the form of welfare benefits, social assistance, subsidies, and large-scale spending on infrastructure.[580] As a rule, through this targeted spending, the *rentier* authoritarian regime attempts to depoliticize society and legitimize its power in the eyes of the population and solicit popular support.

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[578] Anja Franke and Andrea Gawrich, "Autocratic Stability and Post-Soviet Rentierism: The Cases of Azerbaijan and Kazakhstan," *Are Resources a Curse*, 2011, 78.
[579] Pauline Jones Luong, "The 'Use and Abuse' of Russia's Energy Resources: Implications for State-Society Relations," in *Building the Russian State*, ed. Valerie Sperling (New York: Routledge, 2000), 27–30.
[580] Franke and Gawrich, "Autocratic Stability and Post-Soviet Rentierism: The Cases of Azerbaijan and Kazakhstan."

Nazarbayev's regime was well aware of the fact that it had been in dire need for popular support and power legitimization following independence. In fact, with painful policies of privatization and economic liberalization, until recently people have felt widespread inequality and poverty.[581] At the same time, people think that they have been left off from the benefits of oil boom.[582] Furthermore, with economic liberalization, the regime had to dismantle the social protection system that was benevolent during Soviet times. In this dire situation, Nazarbayev utilized oil wealth to come up with *strategic social policy* as an instrument to seek public support. Anja Franke argues that following strategic social policies maintains the regime's stability: social policy as a reflection of the paternalistic understanding of ruling, social policy as a compensation for low democratic legitimacy, and social policy as an instrument to build up a loyal middle class.[583] This paternalistic understanding of rule signifies various targeted welfare and social spending on the improvement of the impoverished group. The construction of loyal middle class involves the creation of well-educated intelligentsia that work in support of the regime in the age of a globalized world. The so-called *Bolashak* program props up this effort by providing scholarship support for those who pursue education abroad.[584]

The other targeted spending for popular support that Nazarbayev employed is the pre-election expenditure. This policy proves to be an effective strategy for the regime stability "because it conformed to public expectations of how a 'good' government should behave in the midst of a sizeable oil boom."[585] For instance, Kahveci concurs that prior to the 2004 elections, salaries were raised 30% as a way of buying people's support.[586] This is part of the so-called "self-legitimation" process where massive spending is channeled on infrastructure development, extravagant buildings, and various events that attempt to justify the leader's rule in the eyes of

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[581] Pomfret, *The Economies of Central Asia*.
[582] Andrea Kendall-Taylor, "Purchasing Power: Oil, Elections and Regime Durability in Azerbaijan and Kazakhstan," *Europe-Asia Studies* 64, no. 4 (2012).
[583] Franke and Gawrich, "Autocratic Stability and Post-Soviet Rentierism: The Cases of Azerbaijan and Kazakhstan."
[584] Adele Del Sordi, "Sponsoring Student Mobility for Development and Authoritarian Stability: Kazakhstan's Bolashak Programme," *Globalizations* 15, no. 2 (2018): 215–31.
[585] Andrea Kendall-Taylor, "Purchasing Power: Oil, Elections and Regime Durability in Azerbaijan and Kazakhstan," *Europe-Asia Studies* 64, no. 4 (2012): 752.k
[586] Hayriye Kahveci, "The Political Economy of Oil in Kazakhstan" (Turkey, Middle East Technical University, 2007), 139.

the population.[587] Interestingly, the other oil companies in the country share the burden of similar objectives. These oil companies were active agents, in cooperation with the regime, in delivering various services, local jobs and social development objectives in destitute regions under the banner of Corporate Social Responsibility (CSR).[588] The operating company TengizChevronOil, for instance, funded various social infrastructure projects, such as schools and hospitals, in the Atyrau region, and spent USD$61 million to repair the water system in Kulsary near the Tengiz oilfield.[589] Analyzing the deeds of the oil companies, Carlson argues that these companies are "buying off the public hence reducing the public's demand on the state, creating a new form of rentierism – social rentierism."[590]

In short, following the privatization program that greatly weakened the state power vis-à-vis the emerging elites, Nazarbayev managed a twofold task: the control of all potential dissent from within the elite, and the reinforcement of the presidential family's stranglehold over the country's assets. The oil industry and relevant sectors that developed with it provided sources of rent for political and business elites, who in turn accepted and supported Nazarbayev as the sole patron. He, in return, functions threefold to sustain the stability of system and make sure that everyone is satisfied with the system; he is a strongman to guarantee the elite's access to rents, a balancer of interests among these competing groups, and finally, a final arbiter to resolve conflict among groups, employing coercion as necessary.

4.3.2 National Oil Fund and state holding companies: developmentalism or vehicles for personal control?

As briefly introduced in the previous chapter, the Kazakh government had to introduce principles of a market economy amid the transitional downturn that required a limited scope for the state activism. In the early years, a blueprint that the government issued in 1997 for economic development, called *Strategy 2030*, embraced as free-market economy that

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587 Adrien Fauve, "Global Astana: Nation Branding as a Legitimization Tool for Authoritarian Regimes," *Central Asian Survey* 34, no. 1 (2015): 110–24.

588 Sevket Akyildiz and Richard Carlson, *Social and Cultural Change in Central Asia: The Soviet Legacy* (London: New York: Routledge, 2013).

589 Halil Burak Sakal, "Natural Resource Policies and Standard of Living in Kazakhstan," *Central Asian Survey* 34, no. 2 (April 3, 2015): 243, https://doi.org/10.1080/02634937.2014.987970.

590 Sevket Akyildiz and Richard Carlson, *Social and Cultural Change in Central Asia: The Soviet Legacy* (London: New York: Routledge, 2013), 140–44.

emphasized macroeconomic stability and open markets with limited state intervention.[591] Nazarbayev himself declared that the state should play an important role in the economy "though limited part in creating legitimate limits of the market in which the private sector is offered a leading part."[592] The role for that state was limited to forming legal bases for the ownership rights, shaping competitive markets and maintaining fiscal and monetary policy, all in line with the recommendations of international organizations.[593] Thus, for years Nazarbayev's liberal economic policies in Kazakhstan "allowed much economic freedom to the country's budding entrepreneurs and offered rapid career mobility to the growing class of skilled professionals, technocrats and top bureaucrats."[594]

However, as the economy recovered, developmental policies in the name of economic growth and industrial diversification swept in as the new rhetoric alongside the government's commitment to liberal market reforms. As in Russia, revenues from the resource boom of the early 2000s, along with the regime dynamics described in previous chapter, were pretext for a steady increase in state activism. Using the oil windfall, political leadership under Nazarbayev became proactive in centralizing economic decision-making, while promoting a rhetoric of saving oil money for the future and diversifying industrial structure. In line with this developmentalist vision, the government established several institutions such as the National Fund of the Republic of Kazakhstan (NFRK), the Development Bank of Kazakhstan in 2001, and the Investment Fund of Kazakhstan and the National Innovation Fund in 2003.

In 2006, Nazarbayev declared his ambition of transforming Kazakhstan into one of the 50 most competitive and dynamically developing countries in the world in next decade.[595] The president also instructed the government to work out Program of 30 Corporate Leaders. The objective was to create thirty national champions that will play a leading role in increasing the

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[591] Richard Pomfret, "Kazakhstan's 2030 Strategy: Goals, Instruments and Performance" (American Economic Association Annual Conference, Philadelphia, 2013)
[592] Press Akorda, "Address of the President of the Republic of Kazakhstan, Nursultan Nazarbayev, to the People of Kazakhstan, October 10, 1997 — Official Website of the President of the Republic of Kazakhstan," Akorda.kz, 1997, https://www.akorda.kz/en/addresses/addresses_of_president/address-of-the-president-of-the-republic-of-kazakhstan-nursultan-nazarbayev-to-the-people-of-kazakhstan-october-10-1997.
[593] Ahrens and Stark, "Emulating Developmental States?"
[594] Dave Bhavna, "Kazakhstan," in *Nations in Transit 2007: Democratization from Central Europe to Eurasia*, ed. Jeannette Goehring (Washington, D.C: Freedom House, 2007), 325–30.
[595] Aktoty Aitzhanova et al., "Kazakhstan 2050: Towards a Modern Society for All," *Emerging Market Forum*, 2013, 1–2.

country's competitiveness. In short, the government applied two instruments in its active industrial policy: generating corporate leaders in several branches of the economy and creating state holding companies. It is against this backdrop that the government set up three new institutions, "Samruk" State Holding Company, "Kazyna" Sustainable Development Fund, and Regional Financial Centre to promote this goal.[596] The agenda behind Kazakhstan's reformist vision with the help of active state involvement gathered further momentum as a result of the financial crisis in 2008 that plagued the economy.[597] 2008 crisis obviously provided further pretext for ongoing nationalization: when the relatively developed and globally integrated banking system of Kazakhstan was hit by the crisis, the government had to partly re-nationalize several large banks. Now, the question is, are these state instruments for the developmentalism or personal control?

The National Fund of the Republic of Kazakhstan. Since the first years of energy windfall revenues, Kazakh leadership has invested in innovative and value-added industries and attempted to preserve wealth for future generations. Sovereign wealth funds (SWF), such as the National Oil Fund, are important tools for preserving and increasing national wealth, and their management and strategy deserve attention at the highest levels. To the state commodity revenue is a double-edged sword; it can be a great source of income for enhancing economic development, but at the same time, when mismanaged, it can be a genesis of economic destruction with its high price volatility and unpredictability.[598] Those countries which are hugely dependent on commodity revenues thus establish SWFs to handle the problems associated with such revenues: to control price shocks and Dutch disease, to stabilize high volatility in public spending, and to save part of the revenues for future generations.[599] Beyond their role as merely a stabilization or savings fund, SWFs can indeed be a political panacea in

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[596] Yelena Kalyuzhnova and Christian A Nygaard, "Resource Nationalism and Credit Growth in FSU Countries," *Energy Policy* 37, no. 11 (2009): 4700–4710.
[597] Charles J. Sullivan, "State-Building in the Steppe: Challenges to Kazakhstan's Modernizing Aspirations," *Strategic Analysis* 41, no. 3 (May 4, 2017): 273–84, https://doi.org/10.1080/09700161.2017.1295606.
[598] Gordon L. Clark, Adam D. Dixon, and Ashby H. B. Monk, *Sovereign Wealth Funds: Legitimacy, Governance, and Global Power* (Princeton University Press, 2013), 16–20.
[599] Y. Kalyuzhnova, *Economics of the Caspian Oil and Gas Wealth: Companies, Governments, Policies*, 1st ed. (New York: Palgrave Macmillan, 2008), 45.

authoritarian regimes, usually being utilized to save the domestic economy in the case of financial crisis and maintain the regime's political power and stability.[600]

Obviously susceptible to oil price shocks, Kazakhstan established its oil fund, the NFRK, in 2001 to "save resources for future generations, and avoid undue pressure on the domestic economy."[601] For this purpose, political leadership established the National Fund of the Republic of Kazakhstan (NFRK) under the model of the Norwegian SWF. Managed by the National Bank of Kazakhstan, the fund consists of two portfolios, stabilizations (25%) and savings (75%), to which certain portions of revenues from gas, oil, and mining were directed according to a strict formula.[602] These portfolios are then entirely invested abroad to sanitize the economy from the destabilizing effects of oil, such as Dutch disease and price volatility. Since its creation, the government has accumulated approximately $90 billion as of 2014, a sharp increase from over $21.5 billion in 2008.[603] The number is small compared to endowments in energy producers like Norway and Saudi Arabia (Norway's fund is worth over a trillion dollars), the National Oil Fund, along with Samruk-Kazyna still fall in the top 25 funds (by size of assets), according to Sovereign Wealth Fund Institute.[604]

National Holding Company Samruk Kazyna. Apart from NFRK, Kazakhstan's Ministry of Finance, as the sole shareholder, set up another important sovereign wealth fund, National Holding Company Samruk Kazyna (SK), which acts as a fund focusing on development objectives, especially in non-extractive industries. The fund came about as a merger of joint stock company Samruk and joint stock company Kazyna Sustainable Development Fund. Established in 2006, Samruk aimed to improve the efficiency of the government's asset management and enhance the activities of the national companies through corporate

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[600] Richard Carney, *Authoritarian Capitalism Sovereign Wealth Funds and State Owned Enterprises East Asia and Beyond* (Cambridge; New York: Cambridge University Press, 2018), 1-10.
[601] Yelena Kalyuzhnova, "Overcoming the Curse of Hydrocarbon: Goals and Governance in the Oil Funds of Kazakhstan and Azerbaijan," *Comparative Economic Studies* 48 (2006): 607.
[602] Matthias Lücke, "Stabilization and Savings Funds to Manage Natural Resource Revenues: Kazakhstan and Azerbaijan vs. Norway," *Kiel Working Paper* No. 1652 (2010): 26.
[603] Andrea Kendall-Taylor, "Instability and Oil: How Political Time Horizons Affect Oil Revenue Management," *Studies in Comparative International Development* 46, no. 3 (July 28, 2011): 321, https://doi.org/10.1007/s12116-011-9089-9.
[604] Institute Sovereign Wealth Fund, "Top 100 Largest Sovereign Wealth Fund Rankings by Total Assets," accessed October 6, 2021, https://www.swfinstitute.org/fund-rankings/sovereign-wealth-fund.

governance.[605] The move seemed to imitate the institutional change that China initiated in 2003 by establishing a special commission, State-owned Assets Supervision and Administration Commission of the State Council (SASAC) which, separating government's regulatory function from its investor function, manages the assets of the state companies. In contrast, Kazyna Fund aimed to achieve sustainable development by improving the system of state administration and corporate management and stimulating investment and innovative activity in different sectors of the economy.

Amid the financial crisis in 2008 that hit the country hard, the government merged Samruk with Kazyna to form a sovereign wealth fund, under which assets of major national companies were consolidated.[606] Created in the image SWFs in Singapore and Malaysia, SK fund, according to official rhetoric, aims to enhance the competitiveness and sustainability of the economy while safeguarding it from the harmful changes in the world market. It also aims to the modernize the economy by attracting foreign investors. As of today, SK manages the work of nearly 600 members of its system of state companies in the key sectors of economy, including oil and gas, electrical and power, transport, telecommunication, and others. The companies under SK's control include oil giant KazMunaiGaz, railway giant Temir Zholy, government Air Freight Air Astana, telecommunications company Kazakhtelecom and the nuclear energy giant Kazatomprom.[607] SK also has minority stake in the copper giant Kazakhmys (11%) and several commercial banks, including Halyk Bank (21%) and KazKommerts Bank (21.2%). The total value of these assets is estimated to exceed over US$78 billion or 60 percent of GDP in 2010, a sharp increase from around 45% in 2007.[608] In 2013, SK, which accounts for about 30% of total employment in the country, announced a profit of

[605] Keun Jung Lee, *The Effects of Privatization and Corporate Governance of SOEs in Transition Economy: The Case of Kazakhstan* (Tokyo: Asian Development Bank Institute, 2020), 2–5, https://www.adb.org/publications/privatization-corporate-governance-soes-transition-economy-kazakhstan.
[606] Franke and Gawrich, "Autocratic Stability and Post-Soviet Rentierism: The Cases of Azerbaijan and Kazakhstan."
[607] World Bank, "A New Growth Model for Building a Secure Middle Class: Kazakhstan Systematic Country Diagnostic" (World Bank Group, 2018), 25–30, https://openknowledge.worldbank.org/handle/10986/29792.
[608] M K Absametov et al., "Assessment Report on Classification of Energy and Mineral Resources and Its Management in the Republic of Kazakhstan" (Kazakh National Research Technical University, 2019).

3.5 billion dollars.[609] In 2012, the fund was divided into two entities: the first structure ensures that the profitability of the company that remains under the control of the Samruk-Kazyna are administered efficiently with costs optimized. The second structure, established as new state holding company "Baiterek", will focus on the management of the national financial institutes to promote economic development, such as the Development Bank of Kazakhstan and the Investment Fund.

While the ownership of banking assets is noteworthy, political consolidation is also underway. Arguably one could claim that the Nazarbayev regime pursued greater control of the country's financial resources following the global economic crisis in 2008; however, a number of interesting moves have taken place starting with the creation of National Holding Company Baiterek in May 2013. As noted above, Baiterek was created after Samruk-Kazyna's financial interests were separated from the fund.[610] Created in 2008, Samruk-Kazyna was meant to be the "fund of funds" after the state merged JSC Sustainable Development Fund Kazyna and Kazakhstan Holding for Management of State Assets Samruk. It therefore seems odd that the split in 2013 essentially returned the holding company to its original form. It is noteworthy that since its creation, Samruk-Kazyna has been dogged by allegations of corruption and poor corporate governance. Separating the fund's financial assets seemed like a logical move to break from its previous record but given that with the exception of the independent directors, both companies have almost the same Board of Directors.[611] More importantly, Baiterek has fallen under the influence of members of the president's family who have successfully placed protégés within company management, allowing for greater political control of the financial industry.

Figure 21.

[609] G. Sansyzbayeva and Zh Ametova, "The Role of 'Samruk-Kazyna' Sovereign Wealth Fund in Implementation of State Programs of the Republic of Kazakhstan," *Asian Social Science* 11, no. 2 (December 20, 2014), https://doi.org/10.5539/ass.v11n2p1.
[610] Michael Mesquita, "Kazakhstan's Presidential Transition and the Evolution of Elite Networks," *Demokratizatsiya: The Journal of Post-Soviet Democratization* 24, no. 3 (2016): 371–97.
[611] Analytica Oxford, "New Kazakhstan Privatisations Will Interest Investors," Expert Briefings (Oxford Analytica, 2015), https://www.emerald.com/insight/content/doi/10.1108/OXAN-DB206948/full/html.

Beyond the hydrocarbon industry, another lucrative sector that SK manages is mining and metallurgy. In fact, mining, and metallurgy in the industrial sector of Kazakhstan is the second most important after oil production. According to the estimates, Kazakhstan produced 13% of the world's chromite, 6% of titanium sponge and 3% of magnesium.[612] According to EITI Report Kazakhstan had a revenue of USD19 billion from the extractive industry in 2017. While, more 52.4% of these revenues came from hydrocarbons, the remaining revenues were derived from mining, with iron, copper, and gold as the major commodities.[613] Apart from other private companies, two national champions, KazAtomProm and Tau-Ken Samruk are strategic companies in the mining industry. The national company Kazatomprom is the largest player in the nuclear power industry in the country, which accounts for 40% of global uranium production in the world. While partially privatized during the transition, the state successfully re-nationalized Kazatomprom in 1997.[614] The uranium industry in the country is seen as both commercial and strategic. Kazakhstan's government took direct control over the industry through Kazatomprom, which represents the country's interests at the first stages of the nuclear fuel production cycle.[615] Kazatomprom's production more than doubled in just a few years, making Kazakhstan the largest uranium ore producer in 2009. Another national champion in the mining industry is Tau-Ken Samruk, a vertically integrated company tasked with managing the government's stakes in some of the country's largest metals and mining companies. Established in 2009, Tau-Ken Samruk aims to consolidate the government's mining holdings under the auspices of one entity, while ensuring efficient mining operations in the field of exploration, extraction, processing, and sale of solid minerals.[616]

The analysis above raises a question: what was the political rationale behind the creation of SK, which became a central pillar in Nazarbayev's economic and political system? Seemingly, the objective behind the merger was to buttress the state's role in the economy by incorporating the state's control over strategic assets with its investment power. In other words,

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[612] Absametov et al., "Assessment Report on Classification of Energy and Mineral Resources and Its Management in the Republic of Kazakhstan."
[613] Aalto Marianne, "Reform of the Mining Sector in Kazakhstan: Investment, Sustainability, Competitiveness" (London: OECD, 2018), 12.
[614] Libman, "Government-Business Relations in Post-Soviet Space: The Case of Central Asia."
[615] Association World Nuclear, "Uranium in Kazakhstan | Nuclear Power in Kazakhstan," 2021, https://world-nuclear.org/information-library/country-profiles/countries-g-n/kazakhstan.aspx.
[616] Marianne, "Reform of the Mining Sector in Kazakhstan: Investment, Sustainability, Competitiveness."

SK sovereign wealth fund was designed to become the “entrepreneurial hand” of the state, managing strategic SOEs, funding Nazarbayev’s important pet-projects, and reinvesting the government’s capital.[617] The argument that several observers propose also shows a tendency that the state started to store the oil wealth in sovereign fund rather than redistribute it to the general populace. However, although the regime's strategic aim of hoarding and creating oil wealth during turbulent times through SK was an important consideration, the political context and timing of SK’s onset deserves further attention. An important watershed here is that the financial crisis in 2008 coupled with a politically challenging domestic environment provided an opportunity for Nazarbayev to centralize the control over state assets and install vertical power in the domain of resource management. In other words, the creation of SK formalized the informal mechanism that Nazarbayev relied on for years through his family after Rakhat Aliev, his former son-in-law, attempted to challenge him and reinforced the preponderant role of the state in the management of the economy. Specifically, the reasoning behind the creation of fund appears to advance several political objectives of the Nazarbayev regime: 1) establish personal control and centralize economic decision making over strategic assets and important source of revenue, 2) monitor the activities of regime elite, both political and economic, and 3) contain the impacts of economic turbulences that might jeopardize the political stability.

The birth of SK in 2008 was an extension of the ongoing political centralization and personalization of power under Nazarbayev to the economic realm.[618] As mentioned in the previous chapter, Nazarbayev had successfully laid the groundwork to personalize power by mid-2000 after eliminating domestic political challenges. The pinnacle of his personality cult was manifested in the title of “president for life” and “leader of the nation” that the parliament granted in 2007 and 2010. In this personalized regime, SK has turned to become an important “instrument used by the president to advance his personal interests, including the domination of the economic (as well as political) spheres of Kazakhstan.”[619] In leaked U.S. cables, political analyst Dosym Satpaev describes Samruk-Kazyna as the “controlling structure” that put direct

[617] Bohnenberger-Rich, “China and Kazakhstan,” 122.
[618] Peyrouse, “The Kazakh Neopatrimonial Regime.”
[619] Simon Goodley, “Court Documents Allege ‘corrupt’ Kazakhstan Regime’s Link to FTSE Firms,” *The Guardian*, 2010, https://www.theguardian.com/business/2010/dec/02/kazakhstan-regime-link-to-ftse-firms.

control over the industries that generate the main sources of revenue for the country.[620] The law regarding national funds stipulates that the president of Kazakhstan can unilaterally intervene in the fund's operational activities. To ensure firm control over the entity, Nazarbayev appointed Timur Kulibayev, his son-in-law, as the chairman of the board of directors and his trusted Prime Minister Karim Massimov to the Board. In 2012 Massimov was replaced with Umirzak Shukeyev, who also had close relations with Nazarbayev, after having served as the deputy head of the presidential administration and vice prime minister. In 2017, Akhmetzhan Esimov, the nephew of the president, was appointed as new head of Samruk-Kazyna. These appointments were to ensure that all "state-run" is de facto "family-run".

The centralization of state assets under one entity, SK, arguably allowed Nazarbayev not only to exert firm control over important revenue sources that state companies generate, but also deal with potential investments coming from abroad to acquire assets under SK. It is because of its centralized structure that SK has "created a single point of contact (or target) for foreign investors who want to acquire Kazakhstani assets." [621] Following its opening for investment, Kazakhstan has become an important destination for Chinese state companies that seek to exploit its geographical proximity and secure natural resources to fuel its economic growth.[622] In 2018, before he announced his resignation from presidency, Nazarbayev initiated a change that moved SK fund away from the direct subordination to the government and transformed it into an "extra-constitutional economic body" directly subordinate to him. Indicating his vision for the fund, he said that "the task that I have always visualized is to manage Kazakhstan as they manage a company or enterprise, from a single center."[623] Along with the Security Council, the move made SK an economic powerhouse under Nazarbayev's personal supervision, handling the task of accelerating the national economy and stabilizing the regime. Apart from its role to act as cashier for the family and enabler of centralized control over assets, the subsidiaries of SK became an important instrument of patronage rents in the

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[620] Mesquita, "Kazakhstan's Presidential Transition and the Evolution of Elite Networks."
[621] Bohnenberger-Rich, "China and Kazakhstan," 134.
[622] Daniel C. O'Neill, "Risky Business: The Political Economy of Chinese Investment in Kazakhstan," *Journal of Eurasian Studies* 5, no. 2 (July 1, 2014): 145–56, https://doi.org/10.1016/j.euras.2014.05.007.
[623] KazakhSTAN 2.0, "Nazarbayev Is 'Redesigning' the Power Centers," Kz.expert, 2019, https://kz.expert/en/news/analitika/1231_nazarbayev_is_redesigning_the_power_centers.

form of joint ventures, contract agreements, or lucrative management positions that the regime uses to co-opt the regime elite, while monitoring their activity.

Table 13. The market value of major companies under Samruk Kazyna

Major companies	Sector	Revenue, $
JSC KazMunayGas	Oil	$6.7 bln
GAO YJSC Kazakhstan Temir Zholy	Transportation	$28 mln
JSC KazAtomProm	Uranium	$989 mln
JSC Tau-Ken Samruk National Mining	Mining	$322 mln
JSC KazakhTelecom	Telecommunication	$396 mln
JSC Air Astana	Aviation	$840 mln
JSC United Chemical Company	Chemical	$3 mln
JSC Kazakhstan Engineering National	Defense	$2.3 bln

(Source: Samruk Kazyna, www.sk.kz)

As mentioned above, Nazarbayev also nationalized Kazakhstan's then-biggest bank, BTA, which had run into financial difficulties.[624] Many of Nazarbayev's challengers have emerged from Kazakhstan's banking and financial sectors and the nationalization of BTA can be viewed as a move to control the emergence of challengers. The state also strengthened its formal role in the sector during the second decade of independence, eventually creating the national mining company Tau-Ken Samruk in January 2009. Tauken Samruk is to be the formal analogue of Kazmunaigaz in the sector: it cannot regulate the sector yet helps consolidate state assets and fulfill some controlling functions. People who are close to Timur Kulibaev are running the company.

So, what are the political roles that the above-mentioned entities play in Kazakh regime? Although the economic rationale behind the oil fund is by all means reasonable for the stability of the national economy, its political significance cannot be ignored. Presumably, SWFs envision addressing so-called economic issues such as inflation, real exchange rates, price shocks and volatility; yet, at the same time, they are designated to save the regime from political

[624] "BTA Bank: A Sigh of Relief?," Global Trade Review (GTR), January 21, 2010, https://www.gtreview.com/news/europe/bta-bank-a-sigh-of-relief/.

instability that these issues usually bring.[625] The examples of SWFs in Kazakhstan, both Oil Fund and Samruk Kazyna, during several watershed moments can illustrate this assumption.

An important scenario that required the assistance of the oil fund was the financial crisis in 2008, which was catastrophic for the economy of Kazakhstan. The banking system was on the verge of crisis due to banks borrowing from international capital markets and the real estate market was adversely affected. In response, the government, utilizing an enormous sum from the oil fund, established an anti-crisis plan to save the economy: the government in total received US$10 billion or 9.5% of GDP from the oil fund.[626]

The other critical point was a sudden drop of oil prices following the financial crisis, which left the economy vulnerable to collapse.[627] This time the government availed the sovereign fund Samruk Kazyna for assistance. Samruk Kazyna was in charge of executing a stabilization program of USD18.3 billion (USD10 billion came from the oil fund), "the core of which was to soften the negative socio-economic consequences of the economic decline in Kazakhstan as well as to provide a basis for future economic growth."[628] It essentially bought shares of troubled banks and the national oil company and assisted businesses with necessary funding. In short, it is a safe claim that the accumulated oil windfall has been utilized as an effective contrivance to securing political power in Kazakhstan during crises. It was because of effective policy-learning by the Nazarbayev regime, namely the economic institutions of the oil fund and Samruk Kazyna, that the regime survived amid catastrophic crises.

In summary, this section attempted to apply the theoretical framework of political resource curse to the case study to observe what mechanisms the Nazarbayev regime employed when it faced the financial crisis of 2008 and recent drops in oil prices. Primarily, the chapter's main argument is concerned with the assumption that the creation of important economic agents, NOC KazMunaiGaz, NFRK and Samruk Kazyna, enable the regime to stabilize political power during oil-induced economic crises. In particular, the NOC KazMunaiGaz has been an important economic instrument at hand for the regime in addition to its assistance for elite co-

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[625] Carney, *Authoritarian Capitalism Sovereign Wealth Funds and State Owned Enterprises East Asia and Beyond*.
[626] Kalyuzhnova and Nygaard, "Special Vehicles of State Intervention in Russia and Kazakhstan."
[627] Marlene Laruelle and Sebastien Peyrouse, *Globalizing Central Asia: Geopolitics and the Challenges of Economic Development* (Armonk, N.Y: Routledge, 2013).
[628] Kalyuzhnova and Nygaard, "Special Vehicles of State Intervention in Russia and Kazakhstan," 62.

optation. Apart from the company's principal role in developing the oil industry and its contribution to social and economic development, the chapter argued that KazMunaiGaz has played important political role of being a virtual cash dispenser to ameliorate the effects of economic downturn. The remainder of the chapter was dedicated to other important bodies at the disposal of the country, namely the Oil Fund and Samruk Kazyna. The chapter argued that beyond an actual role as merely a stabilization or savings fund, the oil fund was indeed the political panacea in authoritarian regimes, saving the domestic economy with accumulated oil money during the financial crisis of 2008. Samruk Kazyna has served as the government's intervening vehicle during crisis, purchasing stakes of most of the state-owned companies, especially NOC KazMunaiGaz.

Chapter 5. Market sector in Russia and Kazakhstan: in between oligarchs and entrepreneurs

The previous chapter provided in-depth analyses of the ways in which the state and market sectors operate in the dualistic capitalist systems of Russia and Kazakhstan. It specifically examined the rise of state control and asset consolidation in several strategic sectors of Russia and Kazakhstan, including hydrocarbon, heavy industries, and finance, with a special focus on the specific companies deemed national champions. In a similar fashion, this chapter discusses the existing market sectors in two countries, putting an emphasis on the oligarchic businesses in metallurgy and mining, as well as small businesses in retail and manufacturing. The current chapter argues that oligarchs in both economies have played an intermediary role between the state sector and market economy, achieving a *modus vivendi* whereby complete loyalty and service to the state's objectives grant access to state support and voice in the policy decisions. At the same time, the chapter discusses how small businesses have become an independent force outside of the state purview in the second-tier market sectors of both countries.

5.1 The introduction to market sector: oligarchs and entrepreneurs

The interest into oligarchic businesses in post-Soviet economies has not lost its thrust in academic circles. Oligarchs can be defined as actors who have formal economic power and informal political power.[629] The gauge of oligarchic success can be seen in his "patronal allegiance", the ability to secure favors from patrons, through which they may receive profit and incur loss.[630] An oligarchy, as discussed in classic political literature such as Plato's *Republic* and Aristotle's *Politics*, is a form of government by wealthy minority group.[631] In the post-Soviet area, the term oligarch usually meant a wealthy and politically well-connected businessman who possesses sufficient resources to wield political influence on many aspects of society and politics. Some argue that the oligarchs are firmly embedded in the political and economic system of the regime and circles of the elite.[632]

[629] Jeffrey A. Winters, *Oligarchy* (Cambridge University Press, 2011), 4–10.
[630] Bálint Magyar and Balint Madlovics, *The Anatomy of Post-Communist Regimes: A Conceptual Framework* (Budapest-New York: Central European University Press, 2020), 162–66, https://ceupress.com/book/anatomy-post-communist-regimes.
[631] Guriev and Rachinsky, "The Role of Oligarchs in Russian Capitalism," 132.
[632] Babajan Tigran, "Oligarchs, State Power and Mass Opinion – A Study of the Role of Oligarchs in Post-Soviet Pseudo-Democracies" (Sweden, Linnaeus University, 2018), 20.

The definition above might raise question regarding the difference between a wealthy entrepreneur and an oligarch. There are several important features that set the oligarchic economy apart from that of entrepreneurs: the nature of wealth accumulation, the nature of political connection and favors, and the nature of business activity and its success.[633] The entrepreneur is the one who possesses businesses that might produce economic power. For this, the entrepreneur bears certain market risks which generate an incentive mechanism whereby he wants to make profits and prevent losses. As the definition shows, the entrepreneur does not enjoy a close political connection with the political elite, although such relations might take place within formally defined legal limits. At the same time, the gauge of success for an entrepreneur is simply the marketability of their business coming from their ability to balance consumer demand and product supply. However, the oligarch is the opposite of the business entrepreneurs, as the table below can demonstrate.

5.2 Oligarchic businesses in Russia: the economy in between the state and market

The formation of independent businesses in Russia traces back its origin in the last days of Soviet empire. The phases of the botched privatization program, which aimed to end the politicization of economic decision making through private ownership, in fact produced the oligarchic class. They acquired their property through political connections and illicit means and mostly focused on rent-seeking rather than profit-making. By aborting the birth of competitive forces in market economy, these capitalists maximized their rent-seeking activity. Also, due to the lack of legal framework amid state weakness and political chaos, these business owners mainly resorted to physical force of criminal groups to enforce contracts and secure their property rights.[634]

Against this backdrop, when inherited the power Putin went on to rebuild the central state and establish the presidential administration as the dominant political institution.[635] Yet, in early 2000, economic forces were still strong enough to manipulate government policies to

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[633] Magyar and Madlovics, *The Anatomy of Post-Communist Regimes: A Conceptual Framework*, 163–68.
[634] Vadim Volkov, *Violent Entrepreneurs: The Use of Force in the Making of Russian Capitalism* (Cornell University Press, 2016).
[635] Hanson and Teague, “Big Business and the State in Russia.”

their advantage or to ignore laws when it suited them.[636] Hence, when Putin was politically weak, he had to work with the oligarchs by attempting to redefine and formalize state-business relations, which can be described as quasi-corporatism with state and big business becoming mutually hostage to each other. This temporary agreement stipulated that Putin does not provoke property redistribution by vaguely ending the question of privatization while oligarchs stay out of politics and fulfill their economic obligation to the state.[637] The bargain suited the needs of oligarchs perfectly since they wanted state-building and structural reform to fortify their victories won in 1990s and protect their property. Yet, the pact did not last long because Putin did not credibly commit to keeping the pact in the face of a growing power imbalance and the absence of a third party. The informal bargain was completely dead when the assertive regime punished several oligarchs who flaunted their power and did not submit to high authority and expropriated their assets.

Figure 22.

Since mid-2000 the regime outlined basic rules to govern the regime-business relations that reflected the changing financial and administrative capacity of an assertive state. Put simple, the new model swung back from the seizure of the state by rent-seeking business to the seizure of business by a predatory state because of the vertical power Putin designed.[638] As Russian observers usually put it, "before 2003, officials took a cut of the profits. After Yukos, they started taking the firms themselves."[639] This is mainly because the power structures of the state became a machine capable of destroying unwanted competitors and monopolizing power to bring order and solve business problems. Although the contents changed over time based on the needs of the regime, the fundamental rules that still govern the state and big businesses relations feature several core tenets: a) the role of oligarchic capital transforming from being

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[636] Stephen Fortescue, "The Russian Economy and Business–Government Relations," in *Routledge Handbook of Russian Politics and Society*, ed. Graeme Gill and James Young, 1st ed. (London: Routledge, 2012), 278.
[637] Fortescue, 278.
[638] Vladimir Gel'man et al., "Authoritarian Modernization in Post-Soviet Russia : Structures, Agencies, and Choices," in *Russian Modernization*, ed. Markku Kivinen and Brendan Humphreys, 1st ed. (London: Routledge, 2020), 115.
[639] Philip Hanson, "Networks, Cronies and Business Plans: Business–State Relations in Russia," in *Russia as a Network State: What Works in Russia When State Institutions Do Not?*, ed. Vadim Kononenko and Arkady Moshes (London: Palgrave Macmillan UK, 2011), 113–38, https://doi.org/10.1057/9780230306707_6.

the state's master to be its servant, b) the existing oligarchs now having "conditional tenure" over their assets, c) as a constituent of state capitalist economy, oligarchs finding themselves the obligation to stay loyal, serve the regime and its rhetoric in exchange for preferential treatment and d) fulfilling conditions above, the big business can play under the rules of a market economy and are free to make profits.

After Putin consolidated his power, his economic policies made it clear that the state would go in the direction of a state-led economy to establish the basis for Russia's restoration as a great power. In this model, the state shaped the economy by dominating strategic industries and promoting national champions in those sectors. The new political rules made Russia's oligarchic capitalism transform into a new system.[640] He told the oligarchic community that there is only one game in town: "a popular, competent, but also merciless government that faces no real alternatives to its hold on power."[641] To tie the oligarchs more closely to the fate of the regime, Putin manipulated the use of carrots and sticks.

Although the oligarchic economy remained highly concentrated, they assumed a new role in the economy. Putin defined that the first task for oligarchic businesses was their role in assisting the state in its new mission and to ensure that big business was socially responsible.[642] Although the regime did not change the results of privatization, oligarchs' proprietary claims over assets took different shape. During the Putin era, not only did the line between private and public become blurred, it also shifted to the advantage of the state.[643] Rather than seen as autonomous private actors with enormous property, the regime started to consider the oligarchs as "trusted" partners who are given conditional tenure over their property.[644] As Igor Sechin, current head of Rosneft, puts it "what difference does it make whether something is state

[640] Sakwa, *Putin*, 176.
[641] David Szakonyi, "Why Russian Oligarchs Remain Loyal to Putin," The Moscow Times, December 1, 2017, https://www.themoscowtimes.com/2017/12/01/centrifugal-forces-why-russian-oligarchs-remain-loyal-to-the-putin-government-op-ed-a59760.
[642] Ilya Matveev, "Big Business in Putin's Russia: Structural and Instrumental Power," *Demokratizatsiya: The Journal of Post-Soviet Democratization* 27, no. 4 (2019): 401–22.
[643] Easter, *Capital, Coercion, and Postcommunist States*, 172.
[644] Simon Pirani, *Change in Putin's Russia: Power, Money and People* (London: Pluto Press, 2009), 62–83

property or private property?"[645] As a concessionaire of the state's valuable assets, the oligarchs are "expected to serve ends defined by the state and to accept that its exercise of certain rights – particularly the right to alienate assets—must be coordinated with the state."[646] Concession rights are granted on the grounds of friendship, loyalty, personal ties, and required tribute. If the owner fails to play by the rules defined by the state, violators are punished with the use of legal and coercive power.

However, such a harsh political reality does not imply the end of market economy. Instead, the market economy coexists with political rules or in fact, is a part of political rationale. Although Putin is nationalist in an economic sense and sees the market as only instrumental, he deems that private ownership in big businesses is an important strategy for developing Russian economy; the regime needs big business to increase the potential of the market. This can be seen in the increasing number of oligarchs after Putin took office: the number of Russian participants in the Forbes rating increased from 17 people in 2003 to 87 in 2007 and 96 in 2017.[647] The advantages of having these "trust managers" to take care of certain regions or sectors is that they thrive with complete freedom and political support given to them by the state to expand.[648] Putin seems to aspire a dynamism of capitalist development, but "without having to deal with the political power of a dynamic capitalist class."[649] The observation of oligarchic businesses in contemporary Russia reveals the presence of at least three big business groupings that run their business emprises on an *ad hoc* basis with the regime: 1) regime cronies that have close connections with Putin, 2) the oligarchic businesses in energy sector, and 3) oligarchic businesses in metallurgy and mining.

5.2.1 The regime cronies around state sector

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[645] Philip Hanson, "Networks, Cronies and Business Plans: Business–State Relations in Russia," in *Russia as a Network State: What Works in Russia When State Institutions Do Not?*, ed. Vadim Kononenko and Arkady Moshes (London: Palgrave Macmillan UK, 2011), 113–38
[646] Hanson and Teague, "Big Business and the State in Russia."
[647] Matveev, "Big Business in Putin's Russia: Structural and Instrumental Power," 413.
[648] Rodygin, "Russia En Route to State Capitalism?"
[649] William Tompson, "Putin and the 'Oligarchs': A Two-sided Commitment Problem," in *Leading Russia: Putin in Perspective* (Oxford: Oxford University Press, 2005), https://doi.org/10.1093/0199276145.003.0010.

Membership of the crony circle includes billionaire oligarchs who are in Putin's inner circle: longtime close friends, relatives, and associates from the security services.[650] The source of the cronies' wealth is usually viewed as government-sanctioned theft and directly connected to the trade deals with state-owned companies in natural resources sectors, including oil, gas, and minerals.[651] Although there are numerous cronies with ties to Kremlin, the prime ones include Yuri Kovalchuk, the Rotenburg brothers, and Gennady Timchenko.[652] Born in the same city and having known Putin for a long time, these figures entered the business world at the start of Putin's political career at St Petersburg in the mid-1990s. However, their businesses only successfully took off during Putin's second presidential term when they started "converting friendship with Putin into billion-dollar fortunes."[653]

One of the cronies with close ties to Putin is Yuri Kovalchuk who set up Ozero Dacha Cooperative and a small bank at St Petersburg, Bank Rossiya, along with Putin and his cliques in early 1990.[654] Kovalchuk is believed to be an important figure in managing the financial and media empire of Putin's regime.[655] He owns 30% of the Bank Rossiya that is ranked as the 17th largest bank with assets of $10 billion. Since 2004, the regime transferred controls of Gazprom's financial, including Gazprombank, insurance company Sogaz, and important media subsidiaries such as NTV, TNT and Gazprom Media, which were expropriated from the oligarchs to the hand of Kovalchuk under Bank Rossiya.[656] Kovalchuk is believed to be the personal cashier and media minister for Putin. According to the U.S. Treasury, his bank is the personal bank for

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[650] Organized Crime and Corruption Reporting Project, "Putin and the Proxies," OCCRP, accessed April 19, 2021, https://www.occrp.org/en/putinandtheproxies/.
[651] Andrew E. Kramer and David M. Herszenhorn, "Midas Touch in St. Petersburg: Friends of Putin Glow Brightly," *The New York Times*, March 1, 2012, sec. World, https://www.nytimes.com/2012/03/02/world/europe/ties-to-vladimir-putin-generate-fabulous-wealth-for-a-select-few-in-russia.html.
[652] Iwona Wisniewska, "Priceless Friendship. The Kremlin's Support for Vladimir Putin's Cronies," Point of View (OSW Center for Easter Studies, 2018), 18–20, https://www.osw.waw.pl/en/publikacje/point-view/2018-10-26/priceless-friendship.
[653] Chris Miller, "Anders Aslund Examines Russia's 'Authoritarian Kleptocracy,'" Russia Matters, 2019, https://www.russiamatters.org/analysis/anders-aslund-examines-russias-authoritarian-kleptocracy.
[654] Dawisha, *Putin's Kleptocracy*, 30–50.
[655] Anders Aslund, *Russia's Crony Capitalism* (Yale University Press, 2019), 143.
[656] Cameron Johnston, "Sanctions against Russia: Evasion, Compensation and Overcompliance." (Briefs 13, The European Union Institute for Security Studies, 2015), https://data.europa.eu/doi/10.2815/27414.

Russia's senior officials, including Putin. Forbes puts his personal fortune at $1.9 billion. After Russia annexed Crimea, Kovalchuk became a target of U.S. sanctions because of its ties to Putin.[657]

Other cronies that made their billions in Putin's system of centralized state capitalism through lucrative government contracts are brothers Arkady and Boris Rotenburg, who befriended Putin as teenagers in their judo club.[658] Arkady Rotenberg started his career a meager businessman with interests in real estate, hotels, and restaurants in the late 1990s. However, in a few years, he grew to become one of the "kings" of state orders after they started investing in the banking, construction, and transportation companies that serviced Gazprom. In 2008, Rotenberg received generous construction subsidiaries from Gazprom for $348 million, which later became Stroigazmontazh, the biggest contractor for state orders worth billions in public infrastructure and natural gas pipelines.[659] Since 2010, Arkady Rotenberg came to control Mostotrest, a giant construction company based in Moscow that is specialized in building highways and infrastructure. These pet projects which granted billions to Rotenberg's empire include the construction of infrastructure for the 2014 Sochi Olympics (contract worth $7 billion), Nord Stream gas pipeline through Russia to Germany, Gazprom's Power of Siberia pipeline (no less than $8.3 billion), a new bridge connecting Crimea to mainland Russia.[660] The wave of U.S. sanctions also targeted Arkady and Boris Rotenberg, who were identified as members of the leadership's inner circle.

Figure 23.

[657] Simon Bowers, "Bank Rossiya, Kremlin's Favoured Bank, to Be 'Frozen out of the Dollar,'" *The Guardian*, March 20, 2014, sec. World news, https://www.theguardian.com/world/2014/mar/20/crimea-crisis-kremlin-bank-frozen-out-dollar.
[658] Mark Galeotti, "Putin and His Judo Cronies," *Foreign Policy* (blog), accessed March 18, 2021, https://foreignpolicy.com/2014/05/15/putin-and-his-judo-cronies/.
[659] Joshua Yaffa, "Putin's Shadow Cabinet and the Bridge to Crimea," The New Yorker, accessed March 18, 2021, https://www.newyorker.com/magazine/2017/05/29/putins-shadow-cabinet-and-the-bridge-to-crimea.
[660] Orttung and Zhemukhov, "The 2014 Sochi Olympic Mega-Project and Russia's Political Economy."

The other crony in the line is Gennady Timchenko, a Russian-Finnish billionaire who belongs to a narrow circle of Putin's judo friends along with Arkady and Boris Rotenberg.[661] Timchenko made connections with Putin after he started his oil trading business in early 1990.[662] In 1997, Timchenko set up a trading company called Gunvor, which soon started to export oil from Russia, accounting for almost 40% of oil trade.[663] Having bought oil at discount price from private oil company Surgutneftegaz and state oil companies Rosneft and Gazprom Neft, Gunvor became third largest oil trading company in the world.[664] According to media investigations, Putin is also a shareholder in the trading company. Over the years, Timchenko has acquired multiple assets in Russia, including shares in gas company Novatek, the gas pipeline construction company Stroitransgaz and gas processing, and petrochemical company Sibur Holding.[665] Novatek is a giant private gas company in Russia that was controlled by the politically connected Leonid Mikhelson. When Timchenko bought a 23.5% share of the company in 2008, Novatek started a successful ascend: the company got a production license, was allowed to use Gazprom's gas pipelines, and completed a liquified gas plant on the Arctic Sea.[666] Soon, Novatek hit a sizable value of $47 billion. According to Forbes, Timchenko's assets were worth an estimated USD$16.8 billion in 2018. U.S. sanctions also targeted Timchenko and some of his companies.

The analysis above indicates that cronies' businesses heavily rely on personal relations and the good graces of Putin.[667] By sharing similar sporting interests with the president, such as judo and hockey, the cronies enjoy frequent interaction and friendly relations with Putin which creates a warm environment for lobbying for their interests and influencing economic decisions regarding distribution of public revenues. Observers hint at a reason behind the emergence of these cronies: they are the creation of Putin himself that serve as an additional political base in

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[661] "Timchenko – The Database 'PUTIN'S LIST,'" Putin's List, 2018, https://www.spisok-putina.org/en/personas/gennady/.
[662] Jack Stubbs et al., "The Man Who Married Putin's Daughter and Then Made a Fortune," Reuters Investigates, accessed October 6, 2021, http://www.reuters.com/investigates/special-report/russia-capitalism-shamalov/.
[663] Wisniewska, "Priceless Friendship. The Kremlin's Support for Vladimir Putin's Cronies," 22–26.
[664] Note Editor's, "From Petrograd to Petrodollars," *The Economist*, May 5, 2012, https://www.economist.com/international/2012/05/05/from-petrograd-to-petrodollars.
[665] Project, "Putin and the Proxies."
[666] Anders Aslund, *Russia's Crony Capitalism* (Yale University Press, 2019), 140.
[667] {Citation}

the corporate world against the holdover oligarchs, discussed below. The most famous example includes Timchenko's acquisition of shares in Novatek from its owner Leonid Mikhelson, who had to give up the control over the company to escape under threat of acquisition by Gazprom.[668]

In any case, for Aslund, business transactions and preferential state orders the cronies acquire constitute a form of asset striping: the state companies buy private assets from cronies at very high prices, yet they sell vast assets for a meager value.[669] In other words, the solvent state became an extremely profitable customer for the businesses of cronies that provide supplies for infrastructure and construction. This is manifested particularly after U.S. sanctions were imposed and the regime directed massive resources to cronies to compensate their financial losses.[670] In short, by basing relations on trust and personal loyalty, the cronies will "stick with Putin until the end, to whom he can assign certain tasks, who won't get frightened by external pressure."[671]

5.2.2 Holdover oligarchs in oil and metals sector

The oligarchs in energy (mainly oil) and metal sectors are the holdover oligarchs who got their riches because of their connections to previous presidential administrations.[672] However after Putin took power, only 15% of oligarchs who were thriving during the Yeltsin era retained their influence.[673] As discussed in previous chapters, after the privatization disarray, both industries were dispersed with a mixture of private, quasi-private, and nominally state-owned companies. By 1998, the six largest private companies came to dominate the oil industry, producing nearly two-thirds of Russian oil. Two groups, professional oilmen and financier oligarchs, controlled these companies and developed two different approaches for the oil business. LUKoil and Surgutneftegaz remained under their original oil-general leaders who focused on sustainable production, while Yukos, TNK, and Sibneft came to be owned by the

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[668] Matveev, "Big Business in Putin's Russia: Structural and Instrumental Power," 417.
[669] Aslund, *Russia's Crony Capitalism*, 173.
[670] Szakonyi David, "Centrifugal Forces: Why Russian Oligarchs Remain Loyal to the Putin Government," Russia Matters, 2017, https://www.russiamatters.org/analysis/centrifugal-forces-why-russian-oligarchs-remain-loyal-putin-government.
[671] Yaffa, "Putin's Shadow Cabinet and the Bridge to Crimea."
[672] Szakonyi, "Why Russian Oligarchs Remain Loyal to Putin."
[673] Olga Kryshtanovskaya and Stephen White, "The Rise of the Russian Business Elite," *Communist and Post-Communist Studies* 38, no. 3 (September 1, 2005): 293–307, https://doi.org/10.1016/j.postcomstud.2005.06.002.

new financial oligarchs who focused on inflating the market capitalization of companies through easy oil production.[674]

Similarly, the metal sector went through turbulent changes during the transition. Since the economic nature of the metals sector is close to that of oil industry, ownership and political characteristics in the former came to resemble to the latter. Like crude oil, metals were primarily commodities that were sold on the global market. However, since the Yeltsin administration did not see the metallurgical sector as strategic as oil, state ownership reduced to minimum.[675] Although the state discarded control over the sectors, its attempt to keep control over the energy industry was more salient than in metals. As a result, assets in the metallurgy and mining sectors were distributed among private actors during the first round of privatization and came to be known as "metal magnates."[676] The oligarchs in these sectors shared similar backgrounds: former bureaucrates and proto capitalists that emerged during the late Soviet era and enterprise managers in the industry.[677]

The rise in crude prices in the early 2000s increased the export revenues of companies which in turn helped owners consolidate their assets and buy off smaller oil companies. In contrast, most industry managers in metallurgy and mining lost control and ownership in their enterprises, which were taken over by the incoming traders that were politically connected outsiders to the sector but insiders to Yeltsin's regime. As a result, several groups came to concentrate all assets in nickel, steel, and aluminum.[678] Yet, due to the disarray in sectoral institutions, companies in both sectors operated in an uncertain terrain regarding the ownership, rights of access and regulatory body that allocated rights for production and exploration. In this situation, some oligarchs took advantage of their increased financial position to penetrate the government and create a cozy environment for furthering their corporate growth.[679] The

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674 Nina Poussenkova, "The Global Expansion of Russia's Energy Giants," *Journal of International Affairs* 63, no. 2 (2010): 104–10.
675 Olga Kesarchuk, "Policy Choices of the Post-Soviet States Regarding Foreign Direct Investment in the Key Sectors of Their Economies: The Experience of Kazakhstan, Russia, and Ukraine" (Ph.D., Canada, University of Toronto, 2015), 127, https://search.proquest.com/docview/1759178201/abstract/B073276529E34353PQ/57.
676 Fortescue, *Russia's Oil Barons and Metal Magnates*, 10–20.
677 Fortescue, "The Russian Economy and Business–Government Relations."
678 Fortescue.
679 Catherine Locatelli, "The Russian Oil Industry between Public and Private Governance: Obstacles to International Oil Companies' Investment Strategies," *Energy Policy* 34 (2006): 1077–80.

corporate success of oligarchs, however, came at a cost for the long-term stability of the state due to the oligarchs' focus on short-term profit-making. Cash and asset stripping, transfer pricing and tax avoidance, which were widespread practices in both sectors hallowed out the state, creating fiscal instability within economy.[680] It is against this backdrop that Putin in his first presidential term prioritized the design of a new model for state-oligarchic interactions in these sectors.

In the oil industry, the regime demonstrated its highly assertive nature, claiming a complete prerogative over the industry.[681] Putin's initial policy aim in the industry was to seize the fair share of oil rents from private companies by rectifying state weakness and designing a new tax system. In particular, the new rule set out three objectives for private oil companies: 1) a large chunk of the profits were to be redistributed to consumers in the form of domestic low prices, 2) a significant share of oil windfalls were to be allocated to the state budget to modernize the economy and 3) companies were to invest in exploration and diversification.[682] The refusal to accept the new model came at a significant cost, as seen in the case of hostile takeover of Yukos assets. At the same time, the state started to reassert its dominance in the oil industry in which the new national champion Rosneft became the face of state power, acting as a counterbalance to the influence of the remaining private oil companies.[683]

The metallurgy and mining sector was equally important for the regime since it generated 5 percent of GDP and 14 percent of exports.[684] However, metals were considered less strategic for the regime than the oil and gas industry as the former did bring less budget revenue. Thus, even in the heyday of its assertive expansion after 2005, the state did not make inroads into the sector, leaving it to existing oligarchs whose share in the sector accounted for more than 90%.[685] Thus, the official attitude to the sector became a "rejection of interference while also

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[680] Fortescue, *Russia's Oil Barons and Metal Magnates*, 18.
[681] Hanson, "The Resistible Rise of State Control in the Russian Oil Industry."
[682] Locatelli, "The Russian Oil Industry between Public and Private Governance: Obstacles to International Oil Companies' Investment Strategies"; Goichi Komori and Sanae Kurita, "Change in the Vertical Integration in the Russian Oil Industry and Management Strategies of Vertically-Integrated Oil Companies" (The Institute of Energy Economics, 2004).
[683] Richard Connolly, *Russia's Response to Sanctions: How Western Economic Statecraft Is Reshaping Political Economy in Russia* (Cambridge: Cambridge University Press, 2018), 86
[684] Fortescue, "The Russian Economy and Business–Government Relations."
[685] Liuhto, "Genesis of Economic Nationalism in Russia," 2008, 20.

provision of some assistance in solving international issues."[686] Unlike the oil sector, where the state directly intervened to promote growth, the officials limited their role in metals to collecting tax from the companies. In short, due to the less strategic nature of the sector, oligarchs in metallurgy and mining appear to have more room to navigate the state assertion. The regime seems to have granted a few selected oligarchs exclusive rights over the sector, allowing them to have some voice in economic decision making in exchange for political loyalty.[687]

In the oil industry, the regime allowed sizable private interests to run their business if they accepted this mandatory demand, regardless of elite's intent to restructure the industry through state-controlled companies. However, in such a strategic industry only two private oil companies, Lukoil and Surgutneftegaz, managed to survive the turbulent changes of the industry and remained major producers.[688] Lukoil, the largest private and second biggest oil company in Russia after Rosneft, pioneered the private ownership after springing out from the ruins Soviet Petroleum Ministry.[689] Behind the creation of such a giant company lies Vagit Alekperov, then-acting minister of the oil industry, a son of a Soviet bureaucrat from Baku, Azerbaijan. Using his weight in the industry, Alekperov took control of the Langepaz, Urengoi, and Kogalym petroleum fields in Siberia along with several refineries and merged them under one package, called LUKoil.[690] By 2005 Lukoil became a major player in Russian oil industry, accounting for 20% of oil production and 19% of oil exports.[691]

During the late 1990s, Lukoil was described as the state within the state as its hand extended to owning tankers, a drilling company, railroad cisterns, and financial entities. Having a strong foothold in domestic industry during the early 2000s, Lukoil started to become a diversified global business empire, forging international partnerships, and establishing upstream and downstream operations that spanned over 30 countries in Asia, Europe, and Africa. Similar to other multinational companies, Lukoil entered the U.S. market through its purchase of Getty

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[686] Kesarchuk, "Policy Choices of the Post-Soviet States Regarding Foreign Direct Investment in the Key Sectors of Their Economies," 174.
[687] Easter, "The Russian State in the Time of Putin: Post-Soviet Affairs: Vol 24, No 3."
[688] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 99.
[689] Isabel Gorst, "Lukoil: Russia's Largest Oil Company" (The James A. Baker III Institute For Public Policy, Rice University, 2007), 5–9, http://large.stanford.edu/publications/power/references/baker/studies/noc/docs/NOC_Lukoil_Gorst.pdf.
[690] Goldman, *Petrostate*, 123.
[691] Gorst, "Lukoil: Russia's Largest Oil Company," 8–9.

Petroleum Marketing Limited in 2000 along with 2,000 domestic oil stations throughout the country.[692] Starting from mid-2005, Lukoil also entered the gas business in Russia and other former Soviet countries. To gain a foothold in the gas industry, Lukoil managed to sign a strategic partnership with Gazprom in the field of gas explorations. Apart from oil and gas businesses, Lukoil also focused on petrochemicals. According to *Forbes*, Alekperov is 65th richest person in the world, with a net worth of around $24.2 billion.[693]

Table 14.

Another private oil company that managed to survive the aggressive state takeovers in the industry was Surgutneftegaz, a vertically integrated private oil company, famous for its conservative corporate profile. Producing more than 60 million tons of oil per year, Surgutneftegas is the fourth-largest Russian oil company after Rosneft, Lukoil, and Gazprom Neft, another state oil company. Basing its headquarters in Surgut, a small town in western Siberia, the company concentrates its production in western and eastern Siberia. Although the company's shareholder structure remains secretive, the main figure behind the company is Vladimir Bogdanov, a professional oilman that came to head the Surgutneftegas production association in 1984.[694] Having a strong ally in the Kremlin, Bogdanov established firm control over Surgutneftegaz after the privatization spree.[695]

Described as a "dinosaur" in the industry, Bogdanov charted a different path by shunning western technology, international standards, and foreign partnerships.[696] However, unlike other oligarchic oil companies, Surgutneftegaz under Bogdanov was a punctual player in the industry: it never used tax optimization to escape tax, never got involved with criminal

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692 Rachel Maddow, *Blowout Corrupted Democracy, Rogue State Russia, and The Richest, Most Destructive Industry on Earth* (Penguin Press, 2019), 13,

693 Forbes, "Vagit Alekperov," Forbes, accessed October 10, 2021, https://www.forbes.com/profile/vagit-alekperov/.

694 Vladimir Soldatkin, "Only God Knows When My Tenure Will End, Soviet-Era Oil Baron Says," *Reuters*, 2019, June edition, https://www.reuters.com/article/us-russia-surgut-ceo-idUSKCN1TT1YF.

695 Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 121–23.

696 IntelliNews Bne, "Russia's Privately Owned Oil Major Surgutneftegaz Makes More Profit from Its Cash Pile than Producing Oil," *Bne IntelliNews*, May 5, 2019, sec. News, https://www.intellinews.com/russia-s-privately-owned-oil-major-surgutneftegaz-makes-more-profit-from-its-cash-pile-than-producing-oil-160637/.

worlds and never had wage arrears. Until today, Surgutneftegas remains infamous as one of the most closed and least transparent oil companies in Russia. Bogdanov, along with the staff is said to control more than 50% of the company's stock.[697] There is rumor that Gennady Timchenko, the crony of Putin, held some 25% of the company.[698] Currently, Surgutneftegaz produces 1.22 million barrels per day and has cash reserves of almost $50 billion.[699]

In contrast to oligarchic expulsion from the oil industry, the oligarchs in the metals industry felt less threatened by the state's aggressive takeover and were allowed to keep their assets if they played by the new rules of the game.[700] With the turbulent changes in the industry dissipated by early 2000, two groups, former traders and ex-Soviet officials and enterprise managers, concentrated their ownership in the metals industry, namely aluminum, steel, iron ore, copper and nickel.[701] In the aluminum industry, two dominant figures came to establishing their dominance after 2000: young traders Oleg Deripaska and Viktor Vekselberg. Both figures entered the industry with the help of outside investors during privatization. Deripaska made inroads to establish his aluminum empire in Siberia through British trading company TWG, which he later drove out of country, while Vekselberg came to own several aluminum plants in the Ural Mountains and Irkuts region with the help of the U.S.-based investment company Renova.[702] After years of rivalry, the two oligarchs came to merge their aluminum businesses, RUSAL and SUAL, in 2007 and formed United Company RUSAL, then the world's largest aluminum company with a production capacity of about 4 million tons of aluminum and 11 million tons of alumina or 12.5% and 16% world output.[703]

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[697] Goldman, *Petrostate*, 145.
[698] Indra Overland and Nina Poussenkova, "Surgutneftegas: Quiet Conservative," in *Russian Oil Companies in an Evolving World The Challenge of Change*, ed. Indra Overland and Nina Poussenkova (UK: Edward Elgar Publishing, 2020), 136, https://www.elgaronline.com/view/9781788978002.00014.xml.
[699] Soldatkin, "Only God Knows When My Tenure Will End, Soviet-Era Oil Baron Says."
[700] Fortescue, "The Russian Economy and Business–Government Relations," 231.
[701] Ellie Martus, "Russian Industry Responses to Climate Change: The Case of the Metals and Mining Sector," *Climate Policy* 19, no. 1 (January 2, 2019): 19, https://doi.org/10.1080/14693062.2018.1448254.
[702] Fortescue, *Russia's Oil Barons and Metal Magnates*, 41.
[703] Staff Reuters, "RUSAL, SUAL, Glencore Complete Aluminium Merger," *Reuters*, March 27, 2007, sec. Mergers News, https://www.reuters.com/article/aluminium-russia-merger-idUSL2713534620070327.

As for the steel industry, the six biggest steel makers owned by oligarchs came to dominate the industry.[704] Overcoming survival mode during the transition years, the private steel companies entered expansion mode, serving the foreign policy interests of the state with their investment activities.[705] The other giant player in mining with a global scale of operation is Noril'sk Nickel, the world's largest producer of nickel and palladium, and the second largest providers of platinum. Prominent oligarch Vladimir Potanin was the dominant shareholder after his ONEXIM Bank bought the company in loans-for-shares privatization in 1995. However, following the management dispute, Deripaska's RUSAL bought 25 percent of the shares in in April 2008.[706]

The survival of these oligarchic businesses raises a riveting question: how were they able to manage to survive the tectonic changes in Russia after the rise of Putin and successfully entered a new pact with the assertive state? In short, the formula behind the success of these oligarchs lies in the strategies they came to develop in line with the regime's political objectives. They successfully managed to shift their focus from directly privatizing administrative control to giving unconditional loyalty to the regime, while also accepting their socio-economic responsibility.[707] The provisions of state functions by large companies located such as SUAL in mining and metallurgy that are in small towns can illustrate the social obligations that the big businesses have to fulfill.[708] Also, an important part of oligarchic strategy was their adaption to an increasingly personalized political system developed under Putin. Concurrently, the oligarchs changed their methods of operations which took the form of distancing themselves from the Kremlin to moving into the regions, merging with international companies, and teaming up with other partners in ownership to avoid hostile takeovers.[709] Yet, this does not mean that oligarchs became an impotent force in the economy. Matveev argues that due to the

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704 Stephen Fortescue, "The Russian Steel Industry, 1990-2009," *Eurasian Geography and Economics* 50, no. 3 (2009): 257–59.
705 Stephen Fortescue and Philip Hanson, "What Drives Russian Outward Foreign Direct Investment? Some Observations on the Steel Industry," *Post-Communist Economies* 27, no. 3 (2015): 285.
706 Stephen Fortescue and Vesa Rautio, "Noril'sk Nickel: A Global Company?," *Eurasian Geography and Economics* 52, no. 6 (November 1, 2011): 835–56, https://doi.org/10.2747/1539-7216.52.6.835.
707 Aslund, *Russia's Crony Capitalism*, 145.
708 Dmitry Zimin, "The Role of Russian Big Business in Local Development," *Eurasian Geography and Economics* 48, no. 3 (January 1, 2007): 361, https://doi.org/10.2747/1538-7216.48.3.358.
709 Robert W. Orttung, "Business and Politics in the Russian Regions," *Problems of Post-Communism* 51, no. 2 (March 2004): 49–50, https://doi.org/10.1080/10758216.2004.11052162.

structural dependence of the regime on private capital and existence of informal backdoor channels, oligarchic businesses still have influence over the policymaking process in Russia.[710]

In the case of the oil industry, the success of Alekperov and Bogdanov in keeping their businesses running appears to be not only the oil tycoons' constant closeness to the previous administration, but also their highly adaptive nature in accepting the rules set by new regime that demand "loyalty over independence and discipline over debate."[711] At the same time, both figures never show any political ambitions or challenged the state policies which helped them avoid serious confrontations with the elite. In the new regime, they proved to be good at playing a complicated political balance and navigating the infighting among the different factions around the Kremlin. In the eyes of the Kremlin, both Alekperov and Bogdanov were "trusted" allies who can further the political and economic agendas of the elite.[712] As for Lukoil, Alekperov's main line of defense was his track record of loyalty to the state. Lukoil's unique position to become the "soft arm" of Russian diplomacy abroad and his willpower to put the political imperatives of the state ahead of its commercial interests. Alekperov himself once stated that "The efficient development of reserves is directly linked to national security. On the one hand, it preserves the economic integrity of the country; on the other hand, it strengthens national positions in the international arena. The concept has always been the same: in the Russian Empire, in the Soviet Union and in the Russian Federation. It will remain this way, until the 'oil era' is over."[713]

As for Surgutneftegaz, the company acted as if it were a state-controlled company after Putin came to power. As Goldman puts it, the company never deviated from the regime's oil policy or faced any complaints and allegations regarding violations.[714] Bogdanov is still a "hermit" oilman, completely indifferent to his high-profile life and secluded by living in Siberia rather than in Moscow.

As for the oligarchs in metals business, they also accepted the new rules of the regime and declared their allegiance. This includes Deripaska and Potanin, the member of an inner

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[710] Matveev, "Big Business in Putin's Russia: Structural and Instrumental Power."
[711] Gustafson, *Wheel of Fortune: The Battle for Oil and Power in Russia*, 392.
[712] Philip Hanson, "The Resistible Rise of State Control in the Russian Oil Industry," *Eurasian Geography and Economics* 50, no. 1 (January 1, 2009): 14–27.
[713] Isabel Gorst, "Lukoil: Russia's Largest Oil Company" (The James A. Baker III Institute For Public Policy, Rice University, 2007), 12.
[714] Goldman, *Petrostate*, 100–110.

circle in Yeltsin's family and a mastermind figure in designing a grand scheme to grab state assets.[715] The fact that oligarchic businesses in the sector are so greatly linked with political power can be seen in a remark made by Deripaska, who declared that "I do not separate myself from the state."[716] In this quasi-corporatist system, such oligarchic loyalty and readiness to serve the state can give them access to state assistance when they run into trouble. For instance, in the course of the 2008 crisis, it became obvious that the oligarchs in metallurgy would hardly survive without state help. The state became the sector's most important source of capital, which intensified its dependence on the regime. In 2008-2009, the government channeled $9.78 trillion as economic assistance to the largest companies through various vehicles. Such assistance came later in multiple forms too, intensifying oligarchs' dependence on the regime. The companies included aluminium company Rusal, steel and coal producer Evraz and Norilsk Nickel.

In sum, oligarchic businesses in Russia went through a complete transformation under Putin's regime. While a new class of cronies around Putin emerged to play an intermediary role between the state sector and market economy, holdover oligarchs managed to build themselves into the state system and gain access to state contracts. In a new corporatist system, the state and oligarchs have achieved a *modus vivendi* in which complete loyalty and service to the state's objectives grant access to state support and voice in policy decisions.

Figure 24.

5.3 The "second-tier" economy in Russia: the private businesses in market sector

Next to the state and oligarchic sectors of the economy lies the market sector with small and medium-sized private businesses (SMEs) that constitute another pillar of the state capitalist economy in Russia.[717] Focusing on the encroachment of the state in the natural resource sector, scholars have long failed to pay much attention to this "other" economic sector.[718] Some describe this sector as "downstream" or a "second tier" economy because of relative lack of

[715] Stanislav Men'shikov, "Our Capitalism: Between Oligarchic and Bureaucratic," *Russian Politics & Law* 43, no. 6 (December 2005): 22–32, https://doi.org/10.2753/RUP1061-1940430602.
[716] Hanson, "The Resistible Rise of State Control in the Russian Oil Industry," 15.

[717] I use 'small firms' and 'SMEs' interchangeably.

[718] Timothy Frye, Andrei Yakovlev, and Yevgeny Yasin, "The 'Other' Russian Economy: How Everyday Firms View the Rules of the Game in Russia," *An International Quarterly* 76, no. 1 (2009): 29–54.

importance to the state.[719] Since the Soviet collapse, businesses in the market sector have been stuck in between state absence which allowed gangsters to rob businessmen without consequences and state dominance which enabled the state to disregard the rule of law and take over private business assets. Ranging from manufacturing to services, these businesses have operated in a different environment from the state and oligarchic sectors. Unlike "first-tier" sectors where state and oligarchs have exclusive privilege, private firms in the manufacturing, trades and service sectors mostly follow market principles, enjoying greater stability and freedom in operating their businesses. Yet, although the rules of the game between the private businesses and government became solid over the years, the former still appears to be suffering from the informality trap, predatory regulations, and extortions.

5.3.1 Small business development in Russia

Historically, the development of small and medium-sized private enterprises exploded in the post-Soviet countries slightly before during mid 1980s and after the fall of communism and subsequent market policies. Before the Soviet collapse, the private sector in Soviet Russia existed in quite a different form, having such names as "gray", "second", or "underground" economy. By the mid-1980s, Gorbachev's reforms led to a loosing of restrictions on the private sector that resulted in an initial wave of entrepreneurship.[720] Then came the golden age for private business in 1991, in which private businesses rose in numbers and operated varied across countries of former Soviet Union. In the early years of the transition, the breakdown of the a communist system in Russia produced a fragile legal system and bureaucratic chaos which confined a large portion of the businesses in new market economy to an informal sector, a vestige of the Soviet-era "shadow economy", which operated outside the command economy.[721] Shortages of consumer goods and the rigidity of the planned economy produced incentives for entering the black market or engaging with middlemen in the production process. According to some calculations, the share of the informal economy in Russian GDP increased from 14 percent in 1990 to 40 percent in 1995, reaching 2 million.[722] During this time, the main concern of

[719] Taylor, *The Code of Putinism*; Hanson, "The Russian Economic Puzzle."
[720] David Stuart Lane, *Soviet Society Under Perestroika* (Routledge, 1992), 141.
[721] L. Kosals, "The Shadow Economy as a Specific Feature of Russian Capitalism," *Problems of Economic Transition* 41, no. 12 (April 1, 1999): 6–33, https://doi.org/10.2753/PET1061-199141126.
[722] Simon Johnson et al., "The Unofficial Economy in Transition," *Brookings Papers on Economic Activity* 1997, no. 2 (1997): 182, https://doi.org/10.2307/2534688.

private business was to capture state assets at a low price and sell them at market prices at home or export abroad through special trading entities. Although the government initially issued a host of policies to support businesses, in the hands of corrupt officials they turned into privileges to well-connected firms in certain sectors.

Following price decontrol and privatization in the early 1990s, hundreds of thousands of small and medium-sized private firms started to spring up in various areas of the economy, engaging in trade, production, and services. There were four types of entrepreneurs in Russia: private farmers who extended their business beyond the family household, gray individuals who provided economic exchange by connecting individuals, former cadres who opened new businesses using their advantageous positions, and professionals who took advantage of their knowledge to open innovative businesses.[723] By 1993, there were more than 260,000 small enterprises in Russia, which rose to 800,000 in 1996. Unlike agriculture and transportation where the state control was still prevalent, industry, construction, commerce, and trade became the most privatized sectors of the economy.[724] According to government statistics, over half of small enterprises were in trading and services, 21% in construction and 12% in manufacturing.[725] By 2000, these small businesses accounted for 14% of total employment and 12% of GDP.[726] The foundation of this market sector during the1990s was a network-based mechanism, which, relying on accepted beliefs and values, emerged as a response to the lack of a codified legal system in the transition environment.

Despite liberalization, private businesses in Russia, especially in manufacturing, trade, and services hardly took hold. The structurally distorted nature of manufacturing and undeveloped service sector in Soviet economy made the transition hard for private businesses.[727] In addition, the weak institutional environment and harsh economic conditions

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[723] John McMillan and Christopher Woodruff, "The Central Role of Entrepreneurs in Transition Economies," *Journal of Economic Perspectives* 16, no. 3 (September 2002): 153–70, https://doi.org/10.1257/089533002760278767.
[724] Joseph R. Blasi, Maya Kroumova, and Douglas Kruse, *Kremlin Capitalism: Privatizing the Russian Economy* (Ithaca, N.Y: Cornell University Press, 1997), 56, https://www.cornellpress.cornell.edu/book/9780801483967/kremlin-capitalism/.
[725] McMillan and Woodruff, "The Central Role of Entrepreneurs in Transition Economies."
[726] Nonna Barkhatova, "Russian Small Business, Authorities and the State," *Europe-Asia Studies* 52, no. 4 (June 2000): 658, https://doi.org/10.1080/713663075.
[727] Frye, Yakovlev, and Yasin, "The 'Other' Russian Economy: How Everyday Firms View the Rules of the Game in Russia."

were hardly favorable for business development. In the economy, arbitrary taxes, rampant inflation, and the lack of financial credit impeded business investment. In governance, a disorganized and fragmented state led to the so-called "grabbing hand" model in which regional officials to get involved in corrupt licensing, favoritism and arbitrary inspections in order to extract rents from private businesses.[728] Facing predatory regulations and private extortions, many business owners had to resort to alternative forms of property protection: the use of private security organizations that helped to deter predation and enforced contracts.[729] As a result, business in Russia "came to connote gangsterism and shady dealings with officials, which contributed to Russia's "Wild East" image in the 1990s."[730]

Inheriting such a harsh environment, the Putin administration prioritized private business development by creating formal legal institutions with the hope that business growth would promote economic diversification and increase employment.[731] During his first presidency, the administration offered comprehensive policy reform, known as the Gref Plan, which introduced measures to promote a favorable business environment and investment climate, reduce the tax burden for businesses, and improve regulatory environment and financial infrastructure.[732] The government also adopted the "On Development of Small and Medium Entrepreneurship" law in 2007 that provided various policy measures, including special taxes, simplified accounting, and state subsidies for business development. The law defined SMEs as micro enterprises with less than 15 employees, small enterprises with employees between 16 and 100, and medium-sized enterprises with employees between 101 and 250.[733] At the same time, the Putin administration created two business associations, OPORA and Delovaya Rossiya,

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[728] Timothy Frye and Andrei Shleifer, "The Invisible Hand and the Grabbing Hand," Working Paper, Working Paper Series (National Bureau of Economic Research, December 1996), https://doi.org/10.3386/w5856.
[729] Timothy Frye, "Private Protection in Russia and Poland," *American Journal of Political Science* 46, no. 3 (2002): 572–84, https://doi.org/10.2307/3088400.
[730] Brian Aitchison, "Small Business Collective Action and Its Effects on Administrative Modernization in Putin's Russia: From 'Grabbing Hand' to 'Helping Hand'?" (PhD dissertation, London School of Economics and Political Science, 2014), 34, http://etheses.lse.ac.uk/994/.
[731] Sylvie K. Bossoutrot, *Microfinance in Russia: Broadening Access to Finance for Micro and Small Entrepreneurs* (New York: World Bank Publications, 2005), 6.
[732] Lucio Vinhas de Souza, *A Different Country. Russia's Economic Resurgence* (Brussels: Centre for European Policy Studies, 2007), https://www.ceeol.com/search/book-detail?id=509623.
[733] Ruta Aidis, Julia Korosteleva, and Tomasz Mickiewicz, "Entrepreneurship in Russia" (Economics Working Paper No. 88, UCL SSEES, University College London, April 2008), 3–5, http://publications.aston.ac.uk/id/eprint/18859/.

with the aim of bringing these businesses closer to the policymaking process. These reforms created new rules for private businesses in which market principles became the "rules of the game" for operating a business. On top of this, the political stability that followed Putin's presidency brought a sharp decline in threats to private business such as extortion, violence, and racketeering with arbitration courts replacing criminal protections to resolve business disputes.[734]

Figure 25.

The Gref Plan reforms introduced major changes to further economic liberalization, but such measures seem to have brought only small improvements to private business development. Although private business sector has grown in numbers, revenues, and investment activity since Putin came to power, the sector is still much smaller than the world average. Throughout 2008 and 2012, the contribution of small businesses to GDP rose from 17% to approximately 21%, whereas the average share of such businesses in advanced industrial countries was 50-60%. Around 19 million people work in small businesses constituting 27% of all employees, compared to 60-80% average in developed countries.[735] The numbers tell that the big businesses still dominate large part of the Russian economy. According to surveys conducted in 2012, nearly 93% of the Russian population saw no possibility of opening their own businesses, compared with 70% in countries with comparable income.[736] The World Bank's Doing Business ranking, which measures the ease of starting a business in each country, indicates improvements in the business environment in Russia, which went up from the 123rd rank out of 183 economies in 2011 to the 40th out of 189 in 2017. However, the report only focuses on formal requirements and does not reflect issues on the ground, such as corruption and bureaucratic hurdles. The description above of the business environment in Russia call into question as to why private businesses have fallen so far behind from their counterparts in other

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[734] J. Gans-Morse, "Demand for Law and the Security of Property Rights: The Case of Post-Soviet Russia," *American Political Science Review*, 2017, 339–40, https://doi.org/10.1017/S0003055416000691.
[735] Taylor, *The Code of Putinism*, 124.
[736] Artur Radziwill and Yana Vaziakova, "Improving The Business Climate in Russia," Working Papers (London: OECD, 2015), 15.

countries. The answer to this question can improve our understanding of the environment in which small businesses operate in Russia in comparison to big businesses.

Scholars have produced myriad works devoted to explaining the environment in which private businesses operate in Russia today along with the reasons why their performance lags. The crux of the matter reveals lies in the interaction that private businesses have with state officials. Understanding this interaction is important since it provides insight into the survival strategies that businesses develop to establish themselves in Russian markets. In comparison to big business-state interaction that features high-level political involvement, small businesses usually interact with low-level state officials[737]. Due to their *small* size these private businesses are neither the target of state seizure nor do they have resources for bureaucrats to capture. This condition basically places their activities within the bounds of market rules, although the relative weakness of small firms in such a harsh business environment creates one-way dependency on the state officials. Although smaller in size, the private businesses in the market sector are characterized by their efficiency and productivity, compared to the oligarchic or state monopolies that are characterized by cronyism and corrupt procurement.[738] However, as the businesses get bigger in size and amass sufficient power in the market, they tend to draw closer to the "upper realms" where oligarchs or state companies' function, making them vulnerable to takeovers.[739]

The interaction of small business with the state officials usually takes place in the informal realm which normally involves corrupt deals and *blat*, or informal contacts.[740] These informal arrangements are proven strategies for businesspeople to navigate the hurdles that are typically part of this business environment where only state officials can provide access to state resources for convenience that the businesspeople use gain competitive advantage over their competitors.[741] Many entrepreneurs came to see personal connections and informality that

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[737] Courtney Bain, "Entrepreneurship in Russia: Patterns and Problems of Its Development in the Post-Soviet Period" (PhD, University of Glasgow, 2007), 12, https://eleanor.lib.gla.ac.uk/record=b2606603.
[738] Miller, *Putinomics*, 90.
[739] Bell The, "From Mover to Retail Magnate: Sergei Galitsky Opens up to The Bell," The Bell, accessed October 10, 2021, https://thebell.io/en/from-mover-to-retail-magnate-sergei-galitsky-opens-up-to-the-bell/.
[740] Alena V. Ledeneva, *Russia's Economy of Favours Blat, Networking and Informal Exchange* (UK: Cambridge University Press, 1998).
[741] Jordan Morse-Gans, "Threats to Property Rights in Russia: From Private Coercion to State Aggression," *Post-Soviet Affairs* 28, no. 3 (2012): 263–95.

involve corrupt deals to be a preferred mechanism protecting their property rights than formal institutions. According to government statistics, at least 70% of businesspeople gave 50% of their undeclared income to corrupt bureaucrats in 2008.[742] The penetration of these informal arrangements in business-state interactions over the years resulted in a vicious cycle of an "informality trap": firms adopt an informal strategy in the form of paying bribes, which creates a pretext for officials to persecute businesses, which in turn forces businesses to rely on informal arrangements to defend themselves.[743] This indicates that private business became much more dependent on state officials from the local to the federal level to have a business environment that allows them to flourish.

Businesses' dependency on state officials unleashed yet another threat to the viability of private property: the predatory policing of private businesses by low-level state officials.[744] The way that the Russian predatory state drags on business development involves the abuse of regulations that low-level law enforcement officers use to make attacks on property rights and extract profits for personal enrichment.[745] The attacks on the property through the abuse of the legal system might take various forms ranging from commissioned criminal prosecutions in which businesses hire law enforcement to attack a rival's business to corporate raiding where officials use legal loopholes to seize business assets. According to Rotchlitz, there are examples of at least 312 cases of corporate raiding that occurred in different cities of Russia between 2000 and 2010. While many of these attacks were concentrated in the manufacturing sector during early 2000, in later years the trend affected other sectors, including services, retail, transport, and construction.[746]

Observing such attacks on the property of various mid-sized businesses, entrepreneurs came to develop private and public strategies to protect their businesses outside of the legal

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[742] Peter Rutland, "The Business Sector in Post-Soviet Russia," in *Routledge Handbook of Russian Politics and Society*, ed. Graeme Gill and James Young (London : New York: Routledge, 2011), 299–300, https://doi.org/10.4324/9780203804490.ch24.
[743] Alexandra Vasileva, "Trapped in Informality: The Big Role of Small Firms in Russia's Statist-Patrimonial Capitalism," *New Political Economy* 23, no. 3 (May 4, 2018): 314–30, https://doi.org/10.1080/13563467.2017.1349090.
[744] "Public Experiences of Police Violence and Corruption in Contemporary Russia: A Case of Predatory Policing?," *Law and Society Review* 42, no. 1 (2008): 1–44.
[745] Stanislav Markus, *Property, Predation, and Protection: Piranha Capitalism in Russia and Ukraine* (UK: Cambridge University Press, 2015), 10–15.
[746] Michael Rochlitz, "Corporate Raiding and the Role of the State in Russia," *Post-Soviet Affairs* 30, no. 2–3 (May 4, 2014): 92–100, https://doi.org/10.1080/1060586X.2013.856573.

system. In practice, entrepreneurs tend to deploy two informal strategies to prevent attacks on their businesses: the use of political patronage and the payment of bribes to officials.[747] Political patronage involves establishing contacts with high-ranking officials to whom the owners can make informal appeals if any threat emerges. However, usually big businesses with sufficient financial might can preserve such access. Thus, normally the most feasible strategy for small businesses is to pay bribes to state officials. Apart from these individual strategies, entrepreneurs have a collective strategy that usually involves membership in business associations with sufficient capacity to prevent attacks.[748] Such business associations can be defensive organizations which can "protect their members from an unfavorable business environment: bureaucratic red tape, unpredictable and arbitrary regulations, and widespread corruption."[749] According to Dinissova, there is a higher chance for business associations to attract more members in countries where such associations can provide effective ways to protect members against regulatory uncertainty and bureaucratic predation.[750]

In Russia's harsh business environment, the survival of non-oligarchic private business appears to be based on several characteristics: the size of firms, market sector, and a firm's ability to outsource services and use courts.[751] Although large firms tend to be targets for raids by officials, they can navigate regulatory challenges thanks to their resources, consumer support, and products. Also, depending on the business sector (retail and IT), certain firms tend to face less administrative hurdles and avoid frequent interaction with state officials, thus becoming less vulnerable to state-backed extortions. At the same time, these market sectors tend to be relatively open and uncontrolled for the entry of newcomers: seizing and running an online retailer is much more difficult than securing oil wells.[752] Furthermore, firms that provide services to state companies as a government contractor tend to be less susceptible to asset-

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[747] Michael Rochlitz, Anton Kazun, and Andrei Yakovlev, "Property Rights in Russia after 2009: From Business Capture to Centralized Corruption?," *Post-Soviet Affairs* 36, no. 5–6 (November 1, 2020): 434–50, https://doi.org/10.1080/1060586X.2020.1786777.
[748] Stanislav Markus, "Capitalists of All Russia, Unite! Business Mobilization Under Debilitated Dirigisme," *Polity* 39, no. 3 (July 1, 2007): 277–304, https://doi.org/10.1057/palgrave.polity.2300083.
[749] Dima Kortukov, "Bandits, Bankers, Bureaucrats, and Businessmen: Post-Communist Political Economy Twenty-Five Years after Soviet Dissolution," *Comparative Politics* 51, no. 3 (2019): 481.
[750] Dinissa Duvanova, "Firm Lobbying versus Sectoral Organization: The Analysis of Business-State Relations," *Post-Soviet Affairs* 27, no. 4 (2011): 387–409.
[751] Vasileva, "Trapped in Informality."
[752] Miller, *Putinomics*, 90.

grabbing by low-level officials. Another important element in successfully running a business in the white realm comes from the ability to outsource activities that normally requires kickbacks. For instance, renting premises rather than owning them can prevent extortions by state agencies since the actual owners deals with such matters. The discussion below will describe the dynamics of how private business can navigate the challenging business environment in Russia through examples of specific firms in the manufacturing and retail sectors.

5.3.2 Businesses in between misery and success: manufacturing and retail sector

According to state statistics, the majority of SMEs in Russia operate in the trade sector, including wholesale and retail. Manufacturing, construction, real estate, and agriculture are also popular sectors for small enterprises. Following the radical market reforms, many private businesses emerged as successful game changers with new innovative techniques in manufacturing, trade, and services due to the interaction of free market rules and entrepreneur ingenuity rather than political involvement. The decontrol of prices made possible the import of a wide variety of food products, consumer electronics, and luxury cars to the market that long suffered from poor quality goods with limited supply. This in turn provided new opportunities for business-minded people who were ready to accept the challenge.

One such businesses was Euroset, which became famous for its successful business in building a retail network for selling mobile phones during early 2000s. By 2008 it was the market leader in Russia, with a market value of $1.1 billion - $1.2 billion.[753] In 2006, the company claimed that personnel from the Interior Ministry illegally seized 167,000 Motorola telephones.[754] Following that revelation, the ministry launched a criminal case against the owners of Euroset, Boris Levin and Yevgeny Chichvarkin, who were later acquitted due to a lack of evidence. Yevgeny Chichvarkin was an award-winning young entrepreneur in Russia, who, due to his businesses, he became his country's the richest man under 35, with

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[753] Anatoly Zhuplev and Dmitry Shtykhno, "Motivations and Obstacles for Small Business Entrepreneurship in Russia: Fifteen Years in Transition," *Journal of East-West Business* 15, no. 1 (2009): 25–49.

[754] "Payment for Counterfeit," *Kommersant.Ru*, 2006, https://www.kommersant.ru/doc/662801.

approximatively $1.6 billion in wealth.[755] The investigations later revealed that Ministry officials wrote off these phones and sold some of them in the market for personal profit. The company was successful in drawing public attention to the case with their complaints regarding the abuse of officials. As a result, the case of Euroset attracted wide media coverage, making it a successful case of "public defense" of property rights.[756] Yet the owners of Euroset had to sell 100% of shares to one of an oligarch billionaires, Alexander Mamut, in 2008. The case of Euroset showed that corporate raiding by state officials replaced the private violence that haunted the private sector of the economy during the transition years. Asset grabbing and extortions during the raids generated new sources of illegal income for officials.

Another firm that made a successful start during the late 1990s but ultimately ended up becoming a target for state buyout was Magnit, a retail chain that revolutionized Russian shopping with its modern-style supermarkets.[757] Opened by Sergey Galitsky as grocery store in the city of Krasnodar in 1998, Magnit expanded its business throughout Russia, launching 1,500 supermarkets in only seven years of its operation. By 2005, Magnit became the largest retailer in Russia in terms of number of stores that reached 16,000 in 2018. In 2013, it had overtaken its rival retail chain X5 Retail (owned by holdover oligarch Mikhail Fridman through his Alfa Group) as Russia's largest retailer in terms of sales. At its peak, the company was valued at $30 billion, becoming one of the most valuable blue-chip stocks in Russia after releasing its IPO in 2006.[758] In 2017, the company made $19.6 billion revenue.

Having worked as mover and bank employee, Sergey Galitsky launched his business in selling wholesale perfumes and cosmetics. After many years, Magnit's success made Galitsky a multibillionaire, $5 billion according to Forbes, outside of natural resources sector with a private jet and a yacht. However, unlike other billionaire oligarchs or *siloviki* who made their wealth because of their proximity to political power, Galitsky belongs to the capitalist club of the market sector that functions outside of politics. He did not have any political connection,

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[755] Andrei Yakovlev, Anton Sobolev, and Anton Kazun, "Means of Production versus Means of Coercion: Can Russian Business Limit the Violence of a Predatory State?," *Post-Soviet Affairs* 30, no. 2–3 (May 4, 2014): 171–94, https://doi.org/10.1080/1060586X.2013.859434.
[756] Morse-Gans, "Threats to Property Rights in Russia: From Private Coercion to State Aggression."
[757] Miller, *Putinomics*, 124.
[758] Valeria Pozychanyuk and Peter Mironenko, "From Mover to Retail Magnate: Sergei Galitsky Opens up to The Bell," The Bell, April 5, 2019, https://thebell.io/en/from-mover-to-retail-magnate-sergei-galitsky-opens-up-to-the-bell/.

mafia ties, or state help to become a wealthy entrepreneur.[759] Nor did the success of his company come from Soviet-era connections to the Communist Party nor the ferocious battle over the redistribution of property that required mingling with politics. Rather the core of his success lies in his ingenuity in understanding the lack of supermarkets in the country and formulating a business model that provided efficient shopping of inexpensive groceries with the use of innovative technologies. Referring to the general business environment in Russia, Galitsky once said that "an entrepreneur mustn't moan. He shouldn't demand anything from the government. All an entrepreneur needs are private property."[760]

However, starting from 2014 Magnit's sales started to falter as due to the economic slowdown, followed by the financial crisis that affected household income in the country. After a tough business cycle and several mistakes, Galitsky announced a controversial decision to sell a large portion of his shares, 29 % to a potential buyer at $2.72 billion; the buyer was later revealed to be VTB, Russia's second biggest bank and government controlled.[761] What was remarkable about the sale was that the choice did not include domestic private markets or foreign investors. The sale of Magnit to a state-controlled bank reflected the increasing role of the state in the economy to become "a landmark for Putinomics" that marked the expansion of the state into a private sector.[762]

The above-mentioned cases demonstrate the desolate terrain in which successful businesses hit an upper ceiling as they grow, whereby they face the inevitable choice of having to merge with either the oligarchic empire or assertive state. However, successfully growing businesses in certain market sectors can avoid such challenges thanks to the complex nature of the sector. One such markets is online retail or e-commerce that has opened new opportunities

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[759] Konstantin Krotov, "How Russian Tycoon Became a Game Changer in Business and Sport," *Financial Times*, December 4, 2016, https://www.ft.com/content/9423dc80-b04d-11e6-9c37-5787335499a0.
[760] Leonid Bershidsky, "Sergei Galitsky's Magnit Found One Buyer: The Russian State," *Bloomberg.Com*, February 2018, https://www.bloomberg.com/opinion/articles/2018-02-16/sergei-galitsky-s-magnit-found-one-buyer-the-russian-state.
[761] Ben Aris, "Magnit's Galitsky Calls It a Day and Sells 29% Stake to VTB," *Bne IntelliNews*, February 2018, https://secure.livechatinc.com/.
[762] Economist The, "One of Russia's Most Successful Private Entrepreneurs Sells–to the State," *The Economist*, February 2018, https://buy.tinypass.com/checkout/template/cacheableShow?aid=CgenXrprgH&templateId=OTGCXNQSMVD9&templateVariantId=OTVX8JXM86YKN&offerId=fakeOfferId&experienceId=EX20EQL3DANL&iframeId=offer_3c6ec0cd358a77fd7c87-0&displayMode=inline&widget=template&url=https%3A%2F%2Fwww.economist.com.

for new capitalists to make from rags to riches stories. Tatiana Bakalchuk, the owner of "Wildberries", the largest online retailer operating in the Russian market, is Russia's first self-made billionaire women with a net worth of USD$1.4 billion, dethroning Yelena Baturina, the wife of Moscow mayor Luzhkov, in 2020. While Baturina made her riches through her construction empire that she built thanks to her husband's position, Wildberries became a market leader without political patronage or favorable state loans.[763]

Bakalchuk opened her online business while on maternity leave in 2004 with the idea that the internet can provide millions of Russian women in remote cities the opportunity to buy trendy clothes. Since early 2010, the company became the best-selling online retailer in Russia with increasing turnover: in 2015, its revenue amounted to approximately $450 million, and reached $1.5 billion by 2019.[764] With the success of Wildberries, the e-commerce market in Russia also attracted the attention of other market players. For instance, in 2018 Yandex decided to set up a $1 billion joint venture in partnership with state-owned Sberbank to create Russian Amazon. At the same time, as the company grew bigger with massive sales, Bakalchuk began to be approached with financial offers from oligarch-affiliated businesses, including Vladimir Yevtushenkov's Sistema that co-owns Ozon, her main rival.[765] However, Bakalchuk refused to accept such deals, maintaining her independent approach. Wildberries has so far successfully warded off these competitive pressures from oligarchs and state-backed venture businesses to maintain its leading role in Russia's e-commerce market.

5.4 Oligarchic businesses in Kazakhstan: the economy in between the state and market

After the collapse of the Soviet Union, political leadership in Kazakhstan launched reform policies that laid the framework for how private enterprise and state interests would interact in the post-Soviet context. Due to the scope of economic vulnerability that the Soviet collapse created, Kazakhstan became a "rescue state" in which the economic system was decentralized to manage the crisis where the government avoided direct participation in

[763] Bell The, "Beyond PR: How Tatiana Bakalchuk Really Created the 'Russian Amazon,'" *The Bell* (blog), September 8, 2020, https://thebell.io/en/beyond-pr-how-tatiana-bakalchuk-really-created-the-russian-amazon/.
[764] Yekaterina Sinelschikova, "Meet Tatyana Bakalchuk, Russia's New RICHEST Woman," Russia Beyond, May 12, 2021, https://www.rbth.com/business/333776-tatyana-bakalchuk-richest-woman.
[765] Max Seddon, "How Tatyana Bakalchuk Took Russia's Ecommerce Throne," *Financial Times*, May 11, 2020, https://www.ft.com/content/b5d2cfc8-62c2-11ea-abcc-910c5b38d9ed.

enterprise management.[766] The economically weak state had to reorganize the assets of its enterprises and attract immediate capital through privatization that lasted from 1993 until early 2000 in different forms. Prior to the state comeback by the mid-2000s, the economy became a two-tier system with two financial-industrial groups (FIG) carving out important sectors: 1) foreign investors and the *political oligarchs,* including the presidential family and inner circle in strategic sectors and 2) the new capitalist class, *economic oligarchs* in non-strategic sectors.[767]

During the final phase of privatization, or case-by-case privatization, large companies with over 5000 employees in all-important sectors of the economy such as oil, gas, and metallurgy were directly sold not to domestic oligarchs, but to foreign companies.[768] Yet, these lucrative sectors that produced the bulk of revenues were apportioned among not only foreign investors, but also among the president's extended family and his inner circle, or *political oligarchs*. After independence, President Nazarbayev's inner circle has claimed most of the oil, gas, and metals industries, run major banks, and own a number of independent media outlets. The president's daughter Dariga and her husband Rakhat Aliev accumulated enough assets to build their own financial-industrial group in banking and media. Nazarbayev's other son-in-law, Timur Kulibaev, controlled the country's commanding heights, including major oil and gas pipelines and transport networks. Other members of the political oligarchs obtained significant control over banks, metals, and energy infrastructure which will be discussed in detail later in the chapter.[769]

On the other hand, during the second phase of privatization, the mass sell-out, the state sold most land, housing, and SMEs through auctions where enterprises management received at least 10% of the shares.[770] Also, banking reforms and a favorable investment climate provided opportunities for SMEs to flourish in the 1990s. This mass privatization led to the redistribution

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[766] Ichiro Iwasaki and Taku Suzuki, "Transition Strategy, Corporate Exploitation, and State Capture: An Empirical Analysis of the Former Soviet States," *Communist and Post-Communist Studies* 40, no. 4 (December 1, 2007): 395–400, https://doi.org/10.1016/j.postcomstud.2007.10.001.
[767] Junisbai, "Improbable but Potentially Pivotal Oppositions."
[768] Scott Radnitz, "The Color of Money: Privatization, Economic Dispersion, and the Post-Soviet 'Revolutions,'" *Comparative Politics* 42, no. 2 (2010): 127–46.
[769] Dmitrii Furman, "The Regime in Kazakhstan," *Central Asia at the End of the Transition. Armonk, NY: ME Sharp*, 2005, 195–266.
[770] Olcott, *Kazakhstan*, 43.

of state assets to the circle of those opportunists with political influence and created a ground for the emergence of a new capitalist class, or *economic oligarchs,* who either had occupied high-ranking government posts or had ties to state officials.[771] In that sense, economic oligarchs in post-Soviet countries came into being as the state creation. This independent capitalist class were permitted to accrue fortunes by gaining control of privatized assets in non-strategic light industries. However, the economic oligarchs were not allowed to own firms in the most profitable industries, including hydrocarbon or minerals, which remained reserved for political oligarchs. Instead, they could only provide ancillary services around these industries, such as construction, basic manufacturing, or transport.[772]

The above account aligns with the argument that the first generation of economic oligarchs acquired their start-up capital and ultimately set up their first companies or took them over during the privatization process in 1990s.[773] From 1993, all Kazakh citizens received vouchers representing a set value which they were able to invest in various investment privatization funds (IPFs). In turn, fund managers used these vouchers to buy up to 20% of the medium-sized enterprises slated for auction. Most of these economic oligarchs in early years concentrated their business activities in the area of trade, investment, financial operations, and light industries.[774] Some of the members of this group included Kozykorpesh Esenberlin (Aziya-Leasing), Nurlan Smagulov (Astana Motors), Nurlan Kapparov (Aktsept), Nurzhan Subkhanberdin (Kazkommertsbank) and Mukhtar Ablyazov (Astana-Holding, later BTA Bank).

The dubious nature of the distribution of state assets created a distinct type of relations between the regime and economic actors. According to Cummings, by the end of privatization there emerged three set of relations between political and business elites.[775] The first set,

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771 Martin C Spechler, "The Economies of Central Asia: A Survey," *Comparative Economic Studies* 50, no. 1 (March 1, 2008): 30–52, https://doi.org/10.1057/ces.2008.3.

772 Nicholas Jepson, "Extractivist- Oligarchic Type: Angola and Kazakhstan," in *In China's Wake: How the Commodity Boom Transformed Development Strategies in the Global South* (New York: Columbia University Press, 2019), 140

773 Anders Aslund, "Comparative Oligarchy: Russia, Ukraine and the United States" (Europe after the Enlargement, Warsaw: Center for Social and Economic Research, 2005), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1441910.

774 Libman, "Government-Business Relations in Post-Soviet Space: The Case of Central Asia."

775 Sally Cummings, *Kazakhstan: Power and the Elite*, 1st edition (London: New York: I.B.Tauris, 2005), 123.

business elites in the upper echelon become heavily dependent on their political ties to the regime or the president himself for their prosperity, rather than domestic capital like in Yeltsin's Russia. In the early years, an absence of formal protection to property and institutional structure amid an undeveloped legal framework encouraged concealed ownership, informal political interdependency, and guarantees.[776] The big economic gains were only possible with political patronage and ultimate loyalty to the president. Nazarbayev demonstrated several times that the position of oligarchs was dependent upon his personal patronage.[777] The second set, the economically enriched ones, were somehow politically unreliable and not yet co-opted by the regime. Finally, the third set attempted to run their business independently of politics, promoting a normal business environment that encouraged the free flow of capital, civilized western society, transparency, and regulation. Although there were continued struggles among them over the delineation of economic realms, all these economic elites supported the political status quo. Unlike Russia, oligarchic groups in Kazakhstan in the early years did not attempt to develop their own administrations, but rather remained content to have economic power without concomitant political power.[778] They had significantly less power than their counterparts in Russia because the president had exceeding authority and because the main income sources such hydrocarbons and metallurgy were under control of foreign investors.

By the end of 2000, there emerged three oligarchic groupings in Kazakhstan which run their businesses on the basis of different political links and faced different rules: 1) the remaining political oligarchs in the inner circle who had direct links with the president himself, 2) economic oligarchs that had protection in the government and 3) oligarchs who did not have a distinct patron in the government but relied on extensive lobbying to run their business.[779] Depending on the particular sector of the economy, relations between the regime and oligarchic actors are either imposed by the regime elite, usually the president himself, or built through mutually beneficial contracts and exchange of favors.

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[776] Libman, "Government-Business Relations in Post-Soviet Space: The Case of Central Asia."
[777] Isaacs, "Informal Politics and the Uncertain Context of Transition: Revisiting Early Stage Non-Democratic Development in Kazakhstan."
[778] Erlan Karin and Andrei Chebotarev, "The Policy of Kazakhization in State and Government Institutions in Kazakhstan," *The Nationalities Question in Post-Soviet Kazakhstan*, January 1, 2002.
[779] Heidi Kjaernet, Dosym Satpaev, and Stina Torjesen, "Big Business and High-Level Politics in Kazakhstan: An Everlasting Symbiosis?," *China & Eurasia Forum Quarterly* 6, no. 1 (2008): 95–107.

5.4.1 The political oligarchs in the mining and metallurgy

During the 1990s, Kazakhstan's mining and metals industry went through a massive reduction of state ownership through privatization. However, the invisible hand of the market was not immediately allowed to rule the mining sector. Instead, the regime selectively opened the sector to private foreign investment through management contracts where the state gave investors exclusive right to manage the large enterprises while retaining residual shares.[780] Hoping for short-term profit in a country blessed with mineral wealth, including iron ore, chrome, manganese, and gold, many international companies succeeded in acquiring production sites. For instance, in 1995 Ispat International of ArcelorMittal, which belongs to Indian billionaire Lakshmi Mittal, bought KarMet, the largest metallurgical complex in Soviet Kazakhstan where Nazarbayev once worked.[781] However, major foreign investors soon lost the competition for the extraction sector with the emergent local players in the country. In contrast to the oil and gas sector which attracted well-established Western companies, the mining and metallurgy sectors were later to be dominated by offshore companies that originated in Kazakhstan and were personally tied to President Nazarbayev.[782] This is partly because of the belief by the elite that unlike the oil and gas industry which required foreign technology, they could develop their own metallurgy and mining sectors. Two important players that emerged as dominant financial-industrial groups in metallurgy and mining were the Eurasian National Resources Corporation (ENRC), known as Eurasian Group and KazakhMys company.

Established in 2006 by a so-called "trio" of oligarchs - Alexander Mashkevich, Patokh Shodiev and Alijan Ibragimov, ENRC have built one of the largest commercial metallurgy and mining empires in the former Soviet states. The trio was said to have had close relations with the ruling elite, especially the president himself, and once controlled around 40% of the economy.[783] The link between the trio and Nazarbayev dates to the 1990s when they first acquired key mining assets during the privatization process. Alexander (Sasha) Mashkevich, born in Kyrgyzstan, turned from academic to businessman in the wake of perestroika, while

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[780] Sally Cummings, *Kazakhstan: Power and the Elite*, 1st edition (London; New York : New York: I.B.Tauris, 2005), 31.
[781] Laruelle and Peyrouse, *Globalizing Central Asia*, 191.
[782] Peck, *Economic Development in Kazakhstan*, 78.
[783] Tom Burgis, *Kleptopia: How Dirty Money Is Conquering the World* (UK: Harper Collins, 2020), 10, https://www.harpercollins.com/products/kleptopia-tom-burgis.

Shodiev, ethnic Uzbek was a regular diplomat at the Ministry of Foreign Affairs in Moscow. Mashkevich and Shodiev met at Seabeco, a trading company built by Lithuanian Boris Birshtein that helped smuggle state money to the West and added Ibragimov to the team, making their way to Kazakhstan to take over the management of troubled mines and refineries. Ibragimov is the only representative of the "Eurasian troika" that has Kazakh citizenship. He has 14.59% of ENRC, 33.33% of Eurasian Financial and Industrial Corporation that includes Eurasian Bank, IC Eurasia. He is also the chairman of the Board of Directors of JSC Kazchrome and the chairman of the Board of Directors of Eurasian Industrial Company, and a member of the Board of Directors of ENRC, Eurasian Financial Company.[784]

Originally, the trio started their business as the founders of Eurasian Bank Group (EBG) and later partnered with Trans World Group (TWG), a trading house of Rueben's brother to acquire the Pavlodar aluminum plant in 1994 through a management contract which later became JSC Aluminium of Kazakhstan.[785] With co-ownership of TWG, EBG also privatized Sokolov-Sarbai Mining and Enrichment Combine (SSGPO), the largest in Kazakhstan, Kazchrome, and Kazakhstanmarganets, Kazakhstan's manganese producer.[786] However, after the dispute over the management of TWG was expelled from the country with EBG taking the ownership of all the assets. Today, ENRC dominates many strategic sectors such as metallurgy, coal, mines, and some financial institutions grouped around the Eurasian Bank.[787] Kazchrome is third in the world market for ferrochrome production, while SSGPO is the world leader in the extraction of iron ore and Aluminum of Kazakhstan provides high-grade alumina from the mines in the Kostanay and Pavlodar regions. In 2006, ENRC was listed in London Stock Exchange with the value of $11 billion.[788] However, in 2013 ENRC faced a series of crises with regards to accusations of fraud and had to urgently delist shares from London Stock Exchange by buying back shares of USD$6 billion in partnership with the Kazakh regime to escape the

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[784] Journal Forbes, "Alijan Ibragimov — Forbes Kazakhstan," *Forbes Kazakhstan*, 2020, //forbes.kz/ranking/object/46.
[785] Peck, *Economic Development in Kazakhstan*, 133.
[786] Kalyuzhnova, *The Kazakstan Economy: Independence and Transition*, 43.
[787] Sebastien Peyrouse, "The Kazakh Neopatrimonial Regime: Balancing Uncertainties among the Family, Oligarchs and Technocrats," *Demokratizatsiya* 20, no. 4 (September 22, 2012): 353.
[788] Joanna Lillis, "Kazakhstan: Corporate Retreat from LSE Raises Governance Questions," *Eurasianet*, December 2013, https://eurasianet.org/kazakhstan-corporate-retreat-from-lse-raises-governance-questions.

criminal prosecution.[789] The Kazakh government was keen to make ENRC private because it feared that bad publicity about the company, which is the largest employer in the country, could damage Kazakh business in general.[790] The trio, which holds a combined 55.33% of shares, teamed up with the Kazakh government, which owns 11.65 percent, and Kazakhmys, a copper giant in the country, to form a consortium to buy ENRC back. After delisting, the ownership of ENRC came under the control of Luxembourg-based Eurasian Resources Group.

Another important player in competition with the ENRC is KazakhMys company, which was established and headed by Vladimir Kim and Vladimir Ni, ethnic Koreans from Kazakhstan, who were regarded as being among the premier oligarchs in the country with close ties to Nazarbayev. Kim was a former member of Nazarbayev's political council, while Ni was once president's chief of staff until his death in 2010.[791] Kazakhmys is the main copper producer and operates 15 open pit and underground mines that makes it the world's tenth-largest copper producer and fifth largest silver producer with earnings of USD$1.63 billion in 2009.[792] In 2005 Kazakhmys become the first company from the former Soviet Union to be listed on the London Stock Exchange, raising over USD$491 million in capital. While listed it generated annual revenues between USD$ 3 and 4 billion. As of 2010, three senior Kazakh managers of Kazakhmys, Vladmir Kim, Vladimir Ni, and Oleg Novachuk, collectively owned 47.6% of shares. Later in 2010, Kim sold an 11% share of the company to the government which made the government its largest shareholder.[793] After completing the asset restructure in 2014, the company changed its name to KAZ Minerals Plc, divesting its unprofitable assets to new Cuprum Holding, owned by former chairman Kim.[794] Currently, KAZ Minerals employs around 10,000 people, most of them in Kazakhstan.

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[789] Burgis, *Kleptopia: How Dirty Money Is Conquering the World*, 47.
[790] Simon Goodley, "Kazakh Mining Giant ENRC Takes Step Closer to Evading Market Scrutiny," *The Guardian*, June 24, 2013, sec. Business, https://www.theguardian.com/business/2013/jun/24/kazakh-enrc-evading-market-scrutiny.
[791] Bohnenberger-Rich, "China and Kazakhstan," 125.
[792] Witness Global, "Risky Business: Kazakhstan, Kazakhmys PLC and the London Stock Exchange," Report (London: Global Witness, 2010), 5.
[793] Bohnenberger-Rich, "China and Kazakhstan," 124.
[794] Firat Kayakiran, "Kazakhmys Completes Restructuring, Changes Name to KAZ Minerals," *Bloomberg.Com*, October 31, 2014, https://www.bloomberg.com/news/articles/2014-10-31/kazakhmys-completes-restructuring-changes-name-to-kaz-minerals.

How have the political oligarchs in the inner circle been able to operate in the second tier of the economy over the years? The functioning of ENRC and KazakhMys in the Kazakh economy provides a story of how big businesses build their existence on political, rather than economic rationale and thus can operate in industries next to the state sector. The basic rules that allowed the political oligarchic groups to operate and become rich are two-fold: a) they provide unconditional loyalty to the president, while sharing their wealth and investing in the stability of the regime and b) refrain from engaging in political activity. Relationships built on personal loyalty have enabled oligarchs to not only become rich, but to also have favorable tax arrangements and lax implementation of government regulations, as well as certain political guarantees that the government will not look into the company's suspect dealings. In exchange, the regime receives formal and informal rents, stock shares, and taxes from these corporations.

Both Mashkevich and Vladimir Kim are among the wealthiest businessmen in Kazakhstan, both with a net worth of over US$3 billion, according to *Forbes*. This kind of informal agreement made the oligarchs invest in maintaining Nazarbayev's grip on the regime. It is for this reason that Mashkevich and Kim have usually been commonly referred to as the "family cashier", whose "pocket companies" are sometimes required to pay for whatever top government officials require.[795] Monetary favor in the form of a *quid pro quo* sometimes also ended up as substantial contributions to Nazarbayev's electoral campaigns throughout his tenure. Also, the oligarchs' positions at Kazakhmys and ENRC as ethnic minorities make them less political – they are unable to exhibit political ambitions to challenge the regime because they lack Kazakh ethnic legitimacy. The Nazarbayev regime skillfully exploited their existence on both "international scene as an example of the success of interethnic cohabitation in the country, and on the domestic scene as a counterweight to the other oligarchs who might be tempted to convert their financial wealth into political tools."[796]

Figure 26.

[795] Tom Burgis, "Emails Raise Fresh Questions about Mining Group's Kazakh Ties," December 14, 2020, https://www.ft.com/content/781c5aeb-c154-40f8-b386-3e02f04ea13c.
[796] Sebastien Peyrouse, "The Kazakh Neopatrimonial Regime: Balancing Uncertainties among the Family, Oligarchs and Technocrats," *Demokratizatsiya* 20, no. 4 (September 22, 2012): 362.

Apart from the political rationale, the regime also has economic calculations in giving preferential treatment to these oligarchic companies. Regime-business relations do not always rely on a one-way street view where the government only give orders to corporations. Instead, Assel argues that Nazarbayev's regime understands the economic value of companies in mineral extraction, and it has thus provided the necessary legal framework and friendly environment to make them competitive. The regime also delegates control over certain markets to these companies through preferential treatment because "large corporations that enjoy monopolistic status or oligopolistic competition (those that hold unrestricted control over domestic market share, helping them to occupy leading economic positions globally) are capable of providing stronger political and economic support."[797] However, since the mid-2000s, relations between the regime and oligarchs started to tilt towards the former in which political leadership wanted to ensure strong control over the oligarchs. In 2012, Verny sold its controlling stake in metals company KazZinc to Swiss-based Glencore for $400 million. In February 2013, it sold its remaining stake in the mining company to Samruk-Kazyna for $1.65 billion.[798]

5.4.2 The economic oligarchs in the banking industry

Kazakhstan's financial industry is another shared sector that bred oligarchs of many sorts over the decades while being closely monitored by the political elite given its strategic importance. The oligarchs coming in the banking sector started after the transition as the finance and banking boom allowed them to form a financial industrial group. By 1994, the number of banks in the country reached almost 191, although such an increase did not result in financial intermediation and competition because of the high concentration of assets. In 1997, the five largest banks accounted for 60% of total banking assets.[799]

Later, strong economic growth from 2000 to 2007, due to mainly the growth of the oil sector, raised confidence in many sectors of the Kazakh economy. The rapid growth of the economy was then reflected in the increase in the capacity of the Kazakh banking system. For instance, the lending of commercial banks as a share of GDP rose from 7% in 1999 to 67% in

[797] Laruelle et al., *Kazakhstan in the Making*, 11.
[798] Staff Reuters, "UPDATE 1-Kazakh Wealth Fund Paid $1.65 Bln for Kazzinc Stake," *Reuters*, 2013, https://www.reuters.com/article/kazzinc-kazakhstan-stake-idUSL5N0BEBGQ20130214.
[799] David Hoelscher, "Banking System Restructuring in Kazakhstan," *IMF Working Paper* 1998, no. 096 (1998): 6, https://www.elibrary.imf.org/view/journals/001/1998/096/article-A001-en.xml.

2007 while the ratio of deposits to GDP increased from 8% to 48% over the same period.[800] The credit, financed through wholesale borrowing from abroad mostly went to the non-tradable sector, particularly construction which recorded unsustainably high growth rates. However, the boom in the domestic credit expansion in foreign currency amid weak institutional foundations made the sector susceptible to the 2008 financial when banks could not roll over their external debt. At that point the government had to intervene to support the liquidity of several banks through direct equities of Samruk Kazyna. Government intervention helped the elite to consolidate their financial assets, which culminated in the expropriation of BTA Bank, the second largest bank, and the integration of other major banks. As a result, public sector assets accounted for 60 percent of total banking assets.[801]

As of 2014, Kazakhstan's banking sector consisted of 38 commercial banks, accounting for 77 percent of total financial system assets and 44 percent of GDP.[802] Although information about the ultimate benefactors of the banks are concealed through obscure ownership, a closer look at the banking structure shows the consolidation of the banking sector *a)* owned directly by the political elite, *b)* controlled by their proxies in the government or *c)* run by oligarchs who are close to the top political elite or the president. Out of around 30 domestic banks, 10 are either directly owned by government officials or their family members.[803] The banks that have direct connections to Nazarbayev and his family include Halyk Bank, one of the largest banks that has long been controlled by president's daughter Dinara, and her husband, Kulibayev. The president's eldest daughter Dariga Nazarbayeva, and her son, Nurali Aliyev, owned the country's ninth largest bank, Nurbank, but in May 2010 sold it to Sarsenov, an oligarch who operates in the fringes of the oil industry.[804] Banks that are controlled by the proxies that serve the interests of the elite include Tsesnabank (currently Jýsan Bank) and Bank RBK. Tsesnabank,

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[800] John C. K. Daly, "Kazakhstan's Emerging Middle Class" (Silk Road Paper, Central Asia-Caucasus Institute & Silk Road Studies Program, 2008), 12.
[801] Joanna Lillis, "Kazakhstan: The Oligarch, the Bank, and the Battle with Astana," *Eurasianet*, 2013, https://eurasianet.org/kazakhstan-the-oligarch-the-bank-and-the-battle-with-astana.
[802] International Monetary Fund, "The Republic of Kazakhstan: Financial System Stability Assessment" (International Monetary Fund, 2014), 10, https://elibrary.imf.org/view/journals/002/2014/258/002.2014.issue-258-en.xml.
[803] Mesquita, "Kazakhstan's Presidential Transition and the Evolution of Elite Networks."
[804] Katherin Machalek, "Corruptistan: Meet the Oil Barons, Fashion Divas, and Ruling Families of Central Asia.," *Foreign Policy*, 2012, https://foreignpolicy.com/2012/09/04/corruptistan/.

the Central Asian nation's second biggest lender by assets, controlled by the family of Adilbek Zhaksybekov, who served as Nazarbayev's chief of staff until 2018.[805]

Table 15.

Apart from the family and political elites, there are several oligarchs who still control several banking institutions due to their close relations with the president. Such oligarchs in the banking sector include Nurzhan Subkhanberdin, Kenes Rakishev and Bulat Utemuratov. Among them, Subkhanberdin has been the longest-serving independent oligarch in the country with his control over Kazkommertsbank. Established in 1991 as Medeu Bank, Kazkommertsbank grew to become the leading bank not only in the country, but also among the former Soviet States.[806] Although Subkhanberdin joined the opposition party DCK that challenged the president, he was later granted to keep his assets in the banking after pledging to stay outside of politics. By 2009, Subkhanberdin owned 10% directly and 26% through Central Asian Investments of Kazkommertsbank.[807] For years, the success of the bank gave it considerable independent power and leverage vis-à-vis the government. Also, its importance in the economy meant that "country's economic well-being is dependent on Kazkomertsbank performing well – and this reduces the scope for the political elite to pressure the bank."[808]

However, in 2009, as a part of government's integration plan following the banking crisis, Samruk-Kazyna purchased a 24 percent stake in Kazkommertsbank, when it also incorporated BTA Bank. At the same time, the European Bank for Reconstruction and Development (EBRD), which bought a stake from the bank in 2004, increased its stake from 7 to 11%. Masquet argues that stake purchase by the EBRD was a purposeful action for Subkhanberdin; "given that the state's reputation could be tarnished if Kazkommertsbank were attacked for political purposes, the EBRD acted as a *de facto* "krysha" (roof) for the bank."[809]

[805] Staff Reuters, "UPDATE 3-Kazakhstan Plans to Buy $1.2 Bln of Tsesnabank Loans," *Reuters*, 2018, September edition, https://www.reuters.com/article/tsesnabank-loans/update-3-kazakhstan-plans-to-buy-1-2-bln-of-tsesnabank-loans-idUSL5N1W00KZ.
[806] Satpaev, "An Analysis of the Internal Structure of Kazakhstan's Political Elite and an Assessment of Political Risk Levels."
[807] Alibekov, "Nazarbayev Seeks to Close Kazakhstani Political Sphere by Opening Economy."
[808] Heidi Kjaernet, Dosym Satpaev, and Stina Torjesen, "Big Business and High-Level Politics in Kazakhstan: An Everlasting Symbiosis?" *China & Eurasia Forum Quarterly* 6, no. 1 (2008): 95–107.
[809] Mesquita, "Kazakhstan's Presidential Transition and the Evolution of Elite Networks," 380.

Although Subkhanberdin is said to be close to Timur Kulibaev, Subkhanberdin had long relied on sophisticated lobbying rather than a "roof" at the top to protect his business. However, after the EBRD sold its stake to Subkhanberdin in 2014, Subkhanberdin had to decrease his share from 20% to less than 6%. As Subkhanberdin's lobbying power waned, there emerged new oligarchs, in particular Kenes Rakishev, who, together with other owners, took control over the bank along with Samruk Kazyna, which controlled a 10% stake.

Kenes Rakishev, a son-in-law of Imangali Tasmagambetov, former defense minister and recently retired ambassador of Kazakhstan to Russia, represents the up-and-coming generation of young oligarchs in the banking sector.[810] Following the purchase of more shares from Subkhanberdin, Rakishev's total stake in the bank including indirect holdings reached to 71.23% in 2016.[811] It is rumored that Rakishev's rise to prominence is connected to and represents the interest of Kulibayev, the son-in-law of the president. Before becoming a pocket oligarch for managing the wealth of the regime, Rakishev worked in different state sectors, including KazTransGaz, Intergaz Central Asia, and KazMunayGaz. In 2004 he was appointed vice-president of KazTransGaz and CEO of Kazakhstan petrochemical industry. In 2014, Rakishev was appointed chairman of BTA Bank, allegedly to recover the hidden assets of the bank from the former owner Ablyazov.[812] According to Forbes, Rakishev is Kazakhstan's 6th richest man at the age of 40 with assets of USD$890 million. Rakishev also made connections with Hunter Biden who worked with him as a sort of go-between for his investment in the United States.[813] However, Rakishev's ambitious path to become new economic oligarch proved to be futile as he was proved to be only a shadow for the big players, including the

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[810] Tom Burgis, *Kleptopia: How Dirty Money Is Conquering the World* (UK: Harper Collins, 2020), 235.
[811] Staff Reuters, "Kazkommertsbank's Biggest Shareholder Raises Holding to over 70 Pct," 2016, April 20 edition, https://www.reuters.com/article/kazkommertsbank-shareholders-idUSL5N17N3YJ.
[812] Burgis, *Kleptopia: How Dirty Money Is Conquering the World*, 380–82.
[813] Adams Guy, "Prince Andrew, the Oligarchs and a New Bombshell for Joe Biden: America's Convulsed over Pictures of the Former Vice President's Son.," *The Daily Mail*, 2020, October 16 edition, https://www.dailymail.co.uk/news/article-8849097/As-GUY-ADAMS-uncovers-links-suspect-regime-just-damage-Hunter-Biden-cause.html.

presidential family. He disappeared from the public after he lost control over Kazkommertsbank in 2018 when Halyk Bank acquired 96.81% of ordinary shares in the bank.[814]

Another important figure in banking is a diplomat-turned banker Bulat Utemuratov, ex-chief of presidential administration.[815] Bulat Utemuratov became the richest businessman in 2016 with an estimated wealth of $2.4 billion. Utemuratov started his business career at the end of perestroika before joining the Ministry of Foreign Economic Relations, a strategic location for establishing networks with foreign investors. He was also appointed as presidential adviser on matters of foreign economic relations.[816] Utemuratov owned ATF Bank, the fifth largest bank in the country, before he sold the bank to Italian company Unicredit for more than $2 billion in 2007.[817] Utemuratov is also a major player in the financial industry, controlling 87.27% of shares in ForteBank JSC, ranked third in terms of assets and Bank Kassa Nova.[818] Apart from banking, Utemuratov controls Verny Investments Holding, an Astana-based asset management company that owns Ritz Carlton hotels in Vienna and Moscow, interests in Kazakhstan's oil and gas industry, as well as various media assets, including Channel 31 and Vremya.[819] When Samruk Kazyna unloaded several banking institutions, Utemuratov became one of the main benefactors: he acquired 79.88% of Temirbank and 16% of Alliance Bank. There is a corrupt relationship between Utemuratov and Kazakhstan's President Nazarbayev: he is usually described as "personal financial manager" to President Nazarbayev.[820]

The final strand of the oligarchic banks includes Eurasian Bank, Bank CenterCredit, and Kaspi Bank. Eurasian Bank, the ninth largest lender in Kazakhstan, belongs to the members of Trio that operates in the mining industry under the shadow of the regime. Bank CenterCredit, a

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[814] Staff Report in Business on 6 August 2018, "Merger of Kazkommertsbank, Halyk Bank Complete," *The Astana Times* (blog), August 6, 2018, https://astanatimes.com/2018/08/merger-of-kazkommertsbank-halyk-bank-complete/.

[815] Kenjali Esbergen, "Bulat Utemuratov may bypass Timur Kulibayev in terms of capital", Radio Free Europe/Radio Liberty, 2011, May 11, http://rus.azattyq.org/content/bolat_utemuratov_glencore_ipo_/24097854.html

[816] Sebastien Peyrouse, "The Kazakh Neopatrimonial Regime: Balancing Uncertainties among the Family, Oligarchs and Technocrats," *Demokratizatsiya* 20, no. 4 (September 22, 2012): 356.

[817] Matthew Patridge, "Why Bulat Utemuratov Sells His Assets in Kazakhstan?," *Finance Talk*, 2020, http://www.talk-finance.co.uk/international/why-bulat-utemuratov-sells-his-assets-in-kazakhstan/.

[818] Mesquita, "Kazakhstan's Presidential Transition and the Evolution of Elite Networks."

[819] Staff Forbes, "Bulat Utemuratov," *Forbes Kazakhstan*, 2021, https://forbes.kz/ranking/object/41.

[820] "Kazakhstan: The Ablyazov Factor," Wikileaks Public Library of US Diplomacy (Kazakhstan Astana, October 2, 2009), https://wikileaks.org/plusd/cables/09ASTANA1762_a.html.

top five lender in the country, belongs to a second-tier oligarch, Bakhytbek Baiseitov (48%) and Lee Vladislav (10%), a member of Korean faction.[821] Baiseitov is also president of the Association of Kazakhstan Banks. Having to sell the bank in the midst of the 2008 financial crisis, Baiseitov took back the reins on the bank in 2018 after buyingout bank's share from Tsesnabank. Baiseitov's acumen in navigating the political in-fights made him one of the richest people in Kazakhstan: his fortune, according to the 2009 estimate of Forbes, was about $ 1.0 billion.[822] Kaspi Bank, the third-largest bank which also owns the fin-tech start-up Kaspi.kz, belongs to Baring Vostok, Russian-based investment company, chairman Vyacheslav Kim, and Mikhail Lomtadze. Fin-tech Kaspi.kz that revolutionized the mobile banking in the country launched its IPO at London Stock Exchange in 2020 at a value of $6 billion. Kaspi had close relations with the regime too: Kairat Satybaldy, the politically powerful nephew of Nazarbayev, had shares in the bank until he allegedly sold his shares in 2018 to avoid bad publicity prior to the bank's IPO at LSE.[823] Still with ties to the regime, Kaspi emerged as an unofficial national online bank for paying taxes and fines, assuming a role that is usually played by the civil service or a government department.

How has the regime conducted the relations with the business in recent years? Unlike Russia, where the oligarchic businesses are seen as "junior partner" to the regime, in Kazakhstan the president remains as the ultimate king that decides the fate of the business. As Junisbai argues, the decisions regarding who can become a player in Kazakhstan's big business are ultimately the president's prerogative. The president's will can decide which group can gain or lose control over companies, firms, and even whole sectors of the economy.[824] This is the reason that the fortunes of economic oligarchs can increase dramatically or shift any time depending on their loyalties, as the cases of Ablyazov and Subkhanberdin demonstrate. Although many of those so-called oligarchs serve as trusted front men to hide the assets of the family and

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[821] Paolo Sorbello, "A Tough September for Kazakhstan's Banks," *The Diplomat*, 2018, https://thediplomat.com/2018/10/a-tough-september-for-kazakhstans-banks/.
[822] Irina Galkina, "Who Owns Kazakh Banks," *Zona Kazakhstan*, 2017, https://zonakz.net/2017/10/26/komu-prinadlezhat-kazaxstanskie-banki/.
[823] David Dawkins, "The Two Billion Dollar Mystery Behind The Ownership Of London-Listed Kazakh Fintech Kaspi," *Forbes*, 2020, https://www.forbes.com/sites/daviddawkins/2020/11/25/the-two-billion-dollar-mystery-behind-the-ownership-of-london-listed-kazakh-fintech-kaspi/?sh=2a12a2a74a39.
[824] Junisbai, "A Tale of Two Kazakhstans," 253.

political elites in the shadows, there are also seasoned oligarchs that run their business on the ground of loyalty and patronage.[825] Yet, at the same time, the health of independent oligarchic businesses is immensely dependent on state support. This can be seen in the rescue operation for ENRC from corruption scandals and domestic banks from liquidity problems. Since domestic banks are always in a mess with toxic loans, they make regular calls for state intervention for liquidity, especially in 2008, 2016, and 2018.[826] In this process, political proximity to the elite gives the oligarchs an edge in receiving these rescue fund.

5.5 The second-tier economy in Kazakhstan: the private businesses in market sectors and bazaar economy

Similar to Russia, various market sectors in Kazakhstan, including manufacturing, construction, service, and retail, host a large number of SMEs that operate in a different environment compared to the businesses state and oligarchic sectors. The law on entrepreneurship defines an SME as an enterprise that employs fewer than 250 workers. The difference for the size, small and medium, is based on the value of annual assets and number of employees: small businesses have annual assets less than 1 million tenge and employ fewer than 50 people[827], while medium size business has assets over 1 million tenge and employ fewer than 250 employees.[828]

Figure 27.

The small property-owning class emerged after the period of radical reforms and mass privatization which set off a sort of capitalist regime of property ownership and wealth accumulation.[829] As analyzed in previous sections, former party leaders remained at the

[825] Expert Kazakh, “On the Oligarchs and Their Frontmen,” Kazakhstan 2.0 Kz.expert, 2019, https://kz.expert/en/news/analitika/1724_onthe_oligarchs_and_their_frontmen.
[826] Sorbello, “A Tough September for Kazakhstan’s Banks.”
[827] The law changed in 2015, which adjusted the definition of small enterprises from 50 to 15-100. In addition, the new category, microenterprises (up to 15 employees), was added to the list.
[828] Kassymkhan Kapparov, “Leveraging SME Finance through Value Chains in Kazakhstan,” ADBI Working Paper (ADBI, 2019), https://www.adb.org/publications/leveraging-sme-finance-through-value-chains-kazakhstan.
[829] Gul Berna Ozcan, *Building States and Markets: Enterprise Development in Central Asia*, 1st ed. (London: Palgrave Macmillan, 2010), 14, https://books.google.co.jp/books?id=zqgYDAAAQBAJ&pg=PA279&lpg=PA279&dq=Ozcan+bazaar

forefront of the new capitalist regime, dominating the redistribution of strategic assets and governance of market control in minerals, oil and gas extraction, and mining to benefit family members and the cliques around them. However, in parallel to their dominance in the "first-tier" economy, the "upper class", through liberal market policies, granted small property owners the freedom and opportunities to become an affluent capitalist class through wealth accumulation in "second-tier" sectors. As in Russia, these private enterprises have enjoyed greater stability and freedom in running their businesses in "permitted" sectors that lie beyond the interest of ruling family and oligarchs. What determines the business owning middle class is their relative access to the opportunities and resources that are shaped by the ruling elite above them. The success of business by ordinary people then comes from their ability to take advantage these opportunities and resources.

Another important venue for second-tier private business initiatives is the so-called bazaar economy in Kazakhstan. Traditionally, bazaars have always played an important role in Central Asian countries as modern institutions with vital economic and political functions.[830] Yet, bazaars reemerged as a shuttle trade in the end of 1980s and beginning of 1990s during the loosening of the socialist system and border controls.[831] After the Soviet collapse which disrupted trade networks, the shuttle traders, or "perestroika entrepreneurs" occupied bazaars and with that a niche of supplying people with various goods.[832] The retail trade in the bazaars became a means of survival during the economic disruption that followed independence. Today, bazaars remain to be a unique marketplace with its formal and informal structures in the economy of Kazakhstan, accounting for nearly half of all of Kazakhstan's retail trade.[833]

The private businesses that occupy the "second-tier" and bazaar economies had both economic and political roles to play in the emerging capitalist regime of Kazakhstan. The

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+economy&source=bl&ots=KCIhYNrcEs&sig=ACfU3U0AQGnIcZFzXEG1obScQas7oELF-Q&hl=en&sa=X&ved=2ahUKEwinzvTu-vvzAhUkGKYKHXJbCboQ6AF6BAgSEAM#v=onepage&q=Ozcan%20bazaar%20economy&f=false.

[830] Regine A. Spector, *Order at the Bazaar: Power and Trade in Central Asia*, Illustrated edition (Ithaca, NY: Cornell University Press, 2017).

[831] Irina Mukhina, "New Losses, New Opportunities: (Soviet) Women in the Shuttle Trade, 1987-1998," *Journal of Social History* 43, no. 2 (2009): 1987–98.

[832] Sholk Dena, "Kazakhstan's Bazaar Economy: A Second-Best Institution," in *Central Asia in the Era of Sovereignty: The Return of Tamerlane?* ed. Daniel Burghart and Theresa Sabonis-Helf, 1st ed. (London: Lexington Books, 2018).

[833] Dena.

entrepreneur class manufactured new goods and delivered new services and created new market opportunities to satisfy the growing demand of the population and deepen market relations.[834] The new business ventures established by this new class came to form the fabric of local communities and economies. Through this economic role, the new business class replaced the Soviet economic system of planning. Apart from their role as building blocks of the market, the new entrepreneur class played a political role in new capitalist regime that furthers the interests of the ruling elite, importantly taking "a central position between the growing poor and disfranchised population and the increasingly unaccountable bureaucratic regime entangled with oligarchic business groups."[835] In other words, businesspeople became a social and political guarantor of stability between the ruling elite and dispossessed masses.

5.5.1 Small business development in Kazakhstan

Historically, private business initiatives grew as a non-state sector in Soviet Kazakhstan on a large scale even before the Soviet collapse. Scholars provide multiple reasons for such activism.[836] For one, for years Central Asian countries, including Kazakhstan, had a surplus workforce thanks to high birth rate and low level of migration to countries in the Soviet Union. Yet, the abundance of manpower lingered in the country in the form of unemployment that reached as high as 15%. People without jobs were often involved in the non-state sector of the economy, including an illegal shadow market, to have a stream of income. Another reason for the growth of private businesses is linked to the centralized structure of Soviet planning economy that emphasized the state sector in industry and agriculture until the reforms in the mid-1980s. The remaining sectors in the economy, such as transport, trade, and service infrastructure, were monopolized with the purpose of serving the centralized command economy. Yet the clumsy state sector could not meet the demands for consumer goods and services as proved by massive shortages. The result was the development of a non-state sector in the economy that functioned, usually in the form of a black market, next to the state sector, filling consumer demand in such sectors as agriculture, services, and small-scale construction.

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[834] Rafis Abazov, "Formation of the Non-state Sector and Privatisation in Kazakhstan and Uzbekistan," *Communist Economies and Economic Transformation* 9, no. 4 (December 1997): 431–48, https://doi.org/10.1080/14631379708427896.

[835] Gul Berna Ozcan, *Building States and Markets: Enterprise Development in Central Asia*, 1st ed. (London: Palgrave Macmillan, 2010), 23

[836] Abazov, "Formation of the Non-state Sector and Privatisation in Kazakhstan and Uzbekistan," 433.

Later, the collapse of the Soviet economy that unleashed a wave of radical market reforms generated market-based small enterprises in the non-state sector of the Kazakh economy. Entrepreneurs became residual beneficiaries of the dissolution of the command economy that legalized private property and entrepreneurship, liberalized prices, and generated programs for mass-scale privatization which denationalized state enterprises with up to 200 workers.[837] The small and medium-sized state enterprises in the services sector, including food, shops, and restaurants were privatized mostly by their own workers. The long tradition of private entrepreneurship and underdeveloped service infrastructure in Kazakhstan provided impetus to indigenous businesses in the services sector, especially in retail trade, which absorbed many unemployed people. In only six years after the independence in 1991, the self-employed population increased from 4.3 % to 24 %, which is more than double the number of entrepreneurs in Russia.[838] However, the process of economic reform was hardly supported by the financial infrastructure and market institutions which were lacking in an economically distressed country. At the same time, private businesses could not escape from Soviet market structures and social norms. When the problems of institutional deficiencies and a lack of government support were coupled with weak demand in local markets, many enterprises were forced to abandon production and moved to trade and services instead.[839] Still, unlike mafia-capitalism in Russia, the radical nature of economic reforms created a relatively business-friendly and less criminal business environment in Kazakhstan. Although forging connections was important for success of business, providing necessary documents, complying with the regulations, and paying taxes became the way to run businesses in Kazakhstan.[840]

Later in the 2000s, the rise in oil revenues generated huge earnings to the country that boosted the domestic economy. The rapid growth rates from 2000 to 2006 averaging around 9% replaced economic shocks of 1990s.[841] The growing need for energy security among powerful countries, including China and the EU, put Kazakhstan in an important position in Central Asia.

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[837] Aslund, *How Capitalism Was Built*, 100–124.
[838] Paul J. Davis and Fatima Abdiyeva, "En Route to a Typology of the Female Entrepreneur? Similarities and Differences Among Self-Employed Women," *Journal of Management Policy and Practice* 13, no. 4 (September 1, 2012): 121–37.
[839] Abazov, "Formation of the Non-state Sector and Privatisation in Kazakhstan and Uzbekistan."
[840] Ken Roberts et al., "Post-Soviet Management: Evidence from Kazakhstan," *Journal of East European Management Studies* 8, no. 3 (2003): 319–31.
[841] Spector, *Order at the Bazaar*, 14.

After the consolidation of power in the mid-2000s, President Nazarbayev increased the state's role in economic governance and development through industrial policies and changes in the corporate structure of state companies. Due to the importance of the hydrocarbon and mining sectors, the political and economic elite largely left the small businesses alone. This is one reason that unlike Russia, the private sector in Kazakhstan have been relatively free from tax and regulatory burdens.[842] According to the Global Entrepreneurship Monitor, 80% of people in Kazakhstan regard becoming an entrepreneur as a high-status career option.[843]

At the same time, oil rents provided financial resources for the political elite who directed the resource-dependent country towards economic diversity through market reforms. The reforms and consequent boom in turn widened opportunities for entrepreneurs whose entrepreneurial ingenuity helped them to join the middle class, along with young technocrats and former apparatchiks.[844] One of the important results of market reform in Kazakhstan that aided private businesses was the flexible business environment in which entrepreneurs started to form independent business organizations and lobbying consultancies with the purpose of providing solidarity, avoiding bureaucratic hassles and supporting their business interests. Content with oil riches, the Kazakh authoritarian regime became permissive in allowing this kind of business interest representation, "as long as these business groupings remain politically neutral and peripheral to and/or not in competition against the major interests in sectors such as banking, rich mineral resources and oil exploration."[845] Prominent business organizations included business incubators and innovation centers (BIIC) and the Almaty Association of Entrepreneurs (AAE), both of which were founded to protect the rights of entrepreneurs in the face of day-to-day administrative problems.

Over the years Kazakhstan has cultivated a supporting environment to generate a relatively healthy level of small business enterprises in the economy. The government established a new organization, DAMU Entrepreneurship Fund in 2007 to provide a range of

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[842] Gul Berna Ozcan, "Overcoming Barriers: Business Consulting and Lobbying in Kazakhstan," in *Innovation and Entrepreneurship: Successful Start-Ups and Businesses in Emerging Economies*, ed. Ruta Aidis and Friederike Welter (London: Edward Elgar Publishing, 2008), 53.
[843] OECD, *OECD Development Pathways Multi-Dimensional Review of Kazakhstan Volume 1. Initial Assessment: Volume 1. Initial Assessment* (OECD Publishing, 2016).
[844] Daly, "Kazakhstan's Emerging Middle Class," 6.
[845] Ozcan, "Overcoming Barriers: Business Consulting and Lobbying in Kazakhstan," 60.

services to small businesses, including funding and training.[846] Since the financial crisis, the government initiated several policies to address such issues faced by businesses such as a lack of financing and administrative burdens. Viewing small business as an important factor for creating jobs and boosting production, the government adopted the *Accelerated Industrial-Innovative Development of Kazakhstan 2010–2015* and the *Roadmap for Business – 2020* which aimed to improve the business climate and remove barriers.[847] According to the World Bank's Ease of Doing Business report, Kazakhstan moved from the 74th ranking in 2010 to the 36th ranking in 2018 to become the most business-friendly country out of 183 nations.[848] In comparison, neighboring Russia ranked on 51st in 2018.

Despite these government efforts, entrepreneurs in Kazakhstan face operational challenges, which prevented them from becoming the building block of private sector development and growth.[849] According to Luthans and Ibrayeva, the fundamental problem lies in the resistance of political and economic elites to change that would otherwise empower entrepreneurs.[850] In addition, for years small business owners have suffered from poor infrastructure, the underdeveloped legal institutions, lack of finance, corruption, and bureaucratic obstacles. Although the government has attempted to improve conditions, reports indicate that corruption, bureaucratic interference, and excessive control over business activities have persisted.[851] These existing structural and day-to-day hindrances have prevented the growth of entrepreneurial activity in the country to certain extent. By the end of 2016, SMEs operating in Kazakhstan accounted for 1.1 million units. The share of these businesses in national GDP was only 23.1% in the same year, far behind the global average.[852] Unlike the diversified nature of small businesses in Russia, SMEs in Kazakhstan tend to be highly concentrated in certain sectors. More than 80% of small businesses in Kazakhstan are engaged

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846 "DAMU Annual Report" (Astana: Baiterek DAMU, 2016), https://www.damu.kz/upload/iblock/add/Damu_GO_ENG_inet%20(1).pdf.
847 Kapparov, "Leveraging SME Finance through Value Chains in Kazakhstan."
848 OECD, *OECD Development Pathways Multi-Dimensional Review of Kazakhstan Volume 1. Initial Assessment*, 69.
849 Davis and Abdiyeva, "En Route to a Typology of the Female Entrepreneur?"
850 Fred Luthans and Elina Ibrayeva, "Entrepreneurial Self-Efficacy in Central Asian Transition Economies: Quantitative and Qualitative Analyses," *Journal of International Business Studies* 37 (2006): 92–110.
851 Kapparov, "Leveraging SME Finance through Value Chains in Kazakhstan," 12.
852 "DAMU Annual Report."

in wholesale, retail, construction, and the service sector since these sectors are relatively low risk and require small capital. Only 17% and 3% of small businesses operate in agriculture and industry, thus limiting their opportunity to diversify the economy.[853]

Table 16.

5.5.2 The bazaar economy and small business

Bazaars, or open marketplaces, are another important venue for smalls-scale entrepreneurs who are engaged in the retail trade business, usually in informal fashion. They represent a less developed form of economic exchange that is characterized by personalized transactions with little information.[854] Bazaars have a long history in Central Asia but found a new life after the Soviet collapse disrupted supply chains and left many people unemployed during early 1990s.[855] Self-employment in a bazaar became a means of economic refuge during the disruption following independence. Put simply, bazaars became an informal economy that run outside of formal frameworks based on the personal networks.[856] Using informal ties, people throughout the Soviet Union, including Eastern Europe, Russia, and Central Asia started to engage in petty trading in informal and open-air spaces. Yet with the successful transition by the early-2000s, informal bazaar trading mostly vanished in Easters Europe.

In Central Asia, the informal bazaar-to-market transition, which is an important package of market capitalism in developed economies, remains incomplete. During the mid-1990s, the trade activities across borders became an important source of income for thousands of self-employed vendors in Kazakhstan. Privately-owned open-air and container bazaars became a facilitator for growing entrepreneurship outside the realm of the state.[857] During the transition years, the bazaar economy had an important economic function of capitalizing on cross border informal trade. The new regimes supported an informal exchange of goods and people across

[853] Ozcan, *Building States and Markets: Enterprise Development in Central Asia*, 49.
[854] Clifford Geertz, "The Bazaar Economy: Information and Search in Peasant Marketing," *The American Economic Review* 68, no. 2 (1978): 28–32.
[855] Volkov, *Violent Entrepreneurs*.
[856] Meiirzhan Baitas, "The Traders of Central Bazaar, Astana: Motivation and Networks," *Central Asian Survey* 39, no. 1 (January 2, 2020): 34, https://doi.org/10.1080/02634937.2019.1697642.
[857] Dena, "Kazakhstan's Bazaar Economy: A Second Best Institution."

borders as it provided a new economic strategy and political stability.[858] As of 2004, there were over 900 bazaars in Kazakhstan, ranging from construction materials, cars, clothing, and livestock. According to government statistics, since 2000 over 55 % of retail trade occurs in bazaars annually. Also, between 12-18% of the labor force in Kazakhstan has been involved in bazaar-related jobs, including retail, security, and administration.

In terms of structure, bazaars in Central Asia (including Kazakhstan) share certain peculiarities. Although they are made of formal structures, informal practices dictate economic outcomes. Since independence, bazaars in Kazakhstan have become an informal and chaotic trading infrastructure that was occupied by a new set of actors who developed an interest in maintaining the emerging bazaar system: traders, bazaar owners, and government officials.[859] Originated as "suitcase" or "shuttle" traders, these entrepreneurs became important actors in an emerging "second-tier" economy. Bazaars in many cities localized the informal economy that functioned in parallel to the formal one for years. As Baitas puts it, the informal economy, in its day-to-day operations, is "removed from the macro-economy and the world of politics at the state level."[860] However from 2014-onwards, all individual traders in bazaars are required to register either as individual enterprises or license holders to operate their small businesses. The second important actor is the owners of the land in which a bazaar is located. Traders normally rent out the space or a container in a bazaar which is privately owned and managed by politically connected wealthy individuals. The owners benefit from the rampant informality which allows them to hide property ownership and rent extraction. While the traders *use* the space to sell goods, the bazaar owners *control* the space using their political ties with the government officials and political elites. For instance, the largest bazaar in Central Asia, *Baraholka* (flea market) located in Almaty, Kazakhstan, employed 20,000 individuals in over 11,000 trading spots that generated $170 million in rents in 2012.[861] Although *Baraholka* bazaar itself

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[858] Hasan H. Karrar, "Between Border and Bazaar: Central Asia's Informal Economy," *Journal of Contemporary Asia* 49, no. 2 (March 15, 2019): 272–93

[859] Regine A. Spector, "Bazaar Politics: The Fate of Marketplaces in Kazakhstan," *Problems of Post-Communism* 55, no. 6 (November 2008): 43

[860] Meiirzhan Baitas, "The Traders of Central Bazaar, Astana: Motivation and Networks," *Central Asian Survey* 39, no. 1 (January 2, 2020): 42

[861] Hasan H. Karrar, "The Bazaar in Ruins: Rent and Fire in Barakholka, Almaty," *Central Asian Survey* 39, no. 1 (2020): 8–94.

accounted for almost 70% of the economy of the city, the retail sector only contributes 5% in taxes collected by the government, an indication of bazaars' informality.

Bazaars represent an important part of the "second-tier" economy in Kazakhstan for several reasons. First, the informal nature of the bazaar economy renders them as an appealing space for employment for disfranchised people who utilize the space as a survival mechanism until today. As an informal economic venue, bazaars fill in the gaps in the formal system and provide social security to vulnerable layers of society. It is not the state but the people who drive economic activity in bazaar.[862] In that sense, bazaars represent "a localized form of pure, free-market capitalism—where individuals, principles of scarcity, price and quality determine economic outcomes."[863] For years, the bazaar economy remained beyond rent extraction system in the state sector that is controlled political elite and big businesses. However, much of the wealth generated in bazaars is still channeled upward to the elite who control the bazaar space. The elite's attempt to control these bazaars as a new source of rent have recently intensified with rhetoric of modernizing bazaars' infrastructure.[864] Newly emerging figures, including high-level officials, regional governors, and the members of family have begun to establish control over bazaars.

5.5.3 The threshold of success at the "second-tier" economy: the case of retail trade

As in Russia, "second-tier" sectors in Kazakhstan can provide opportunities for many small-scale businesses to become successful game changers. Unlike the power relations that define property allocation in the state sector, success in the market sector is primarily driven by the interplay of free market rules, competition, and entrepreneurial ingenuity. The retail sector has been one of the main venues for business success in Kazakhstan that does not require much beyond good relations with officials. This is because for years business in the smaller-scale wholesale and retail sector have featured a relative absence of high-profile political elites. However, with changes in consumer behavior, retail business in modern supermarkets in big cities have become an important source of wealth for members of the political elite. In other

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[862] Ozcan, "Overcoming Barriers: Business Consulting and Lobbying in Kazakhstan."
[863] Dena, "Kazakhstan's Bazaar Economy: A Second Best Institution," 293.
[864] Hasan H. Karrar, "The Bazaar in Ruins: Rent and Fire in Barakholka, Almaty," *Central Asian Survey* 39, no. 1 (2020): 8–94.

words, like the cronies of Putin, members of the Nazarbayev family have made inroads into the lucrative retail sector by expropriating successfully expanding supermarket chains.[865]

The retail sector accounted for 16% of GDP in Kazakhstan in 2018.[866] The sector also absorbed almost 15% of total employment in the country.[867] As described above, for years open air bazaars and kiosks where small entrepreneurs sell groceries, electronics, cars, and dairy products have become important shopping locations for consumers. Sales by these small entrepreneurs in bazaars constituted around 20–25% of the total retail market in Kazakhstan. However, following the credit boom, consumers have increasingly become amenable to the higher quality and reasonably priced products that are often provided by supermarkets. Since early 2000, such trends became highly observable in electronic appliances and grocery retailers.[868] Modern grocery stores increased from 17% in 2013 to 31% in 2018.[869] Making good use of changes in consumer behavior, pioneering chains, such as Technodom (electronics), Magnus (grocery), and Bipek Auto (car retail) gained prominence in the retail sector. Some of these businesses in retail that transformed from small business to become influential market players without the political interference will be described below.

Technodom is a chain of stores that specialize in selling electrical and computer equipment. The company was established by Eduard Kim, an engineer of ethnic Korean origin, in Almaty, as a tomato shop in 2002. Operating over 80 stores in more than 27 cities of Kazakhstan and neighboring Kyrgyzstan, Technodom employs over 8000 people and generates revenue of $ 22.47 million in 2019.[870] Starting out as a small retail business, over the years Technodom expanded to become one of the largest electronics providers with 37% of market share in the electronic distribution market. According to Kim, the motivation behind the business expansion was to break free from dependence on government agencies and officials.

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[865] Expert Kazakh, "A Forecast for Bolat Nazarbayev's Future," Kazakhstan 2.0 Kz.expert, accessed November 3, 2021, https://kz.expert/en/news/analitika/1985_a_forecast_for_bolat_nazarbayevs_future_.
[866] Bakertilly, "Modern Trends in Kazakhstan Retail Business," Market Analysis (London: Bakertilly, 2019).
[867] Lalita A. Manrai et al., "Retail Developments in Poland, Kazakhstan, and Ukraine: A Comparative Analysis," *International Journal of Business and Economics* 14, no. 1 (2015): 68–69.
[868] Euromonitor, "E-Commerce in Kazakhstan," Market Research Report (London: Euromonitor International, 2021), https://www.euromonitor.com/e-commerce-in-kazakhstan/report.
[869] Bakertilly, "Modern Trends in Kazakhstan Retail Business."
[870] Staff Forbes, "Technodom.Kz — Forbes Kazakhstan," *Forbes Kazakhstan*, 2020, https://forbes.kz/ranking/object/939

Apparently, small-scale business suffered from the nightmare of bureaucratic interference since they tend to remain in the informal sector. Kim's success story indicates the important rule in the "second-tier "sector: when growing businesses follow all the laws and regulations, it is possible to develop a transparent and competitive business in the country. Indeed, the success of Technodom is not merely due to the compliance of laws, but another crucial rule for the non-state sector: "the sweat and tears of a leader who refused to rest and felt overwhelming joy on moving minds to find contemporary solutions".[871] Representing a rags-to-riches success story, Kim was 17th among the most influential businessmen in Kazakhstan and 28th among the 50 richest people in the country, according to Forbes.

Another important player in retailer sector is Magnus Cash & Carry company, the largest department store chain in Kazakhstan. Magnus was founded in 2007 by Alexander Graber as small retail business with a single shopping center in Almaty.[872] Over 13 years it has grown to have 75 stores and shopping centers in 9 cities across the country. In 2016, Magnum was listed in the Kazakh Stock Exchange. In 2019, Magnus was ranked as 10th largest among the 50 largest companies in the country with a revenue of $430 million and a net profit of $5.1 million.[873] Trained as an economist, Garber began his career in the Ministry of Internal Affairs of Soviet Kazakhstan and became a broker after 1991. Since the mid-1990s, Garber opened several businesses in distribution and logistics and had stakes in a Kazakh Indian tea company. Having built a successful retail business in Magnum over the years, Garber became a newly minted multi-millionaire businessman in the country. In 2019, he is ranked the 32nd richest businessman among the top 50 candidates with the wealth of $180 million.[874] With its impressive size and astounding growth rates, Magnus already exceeded the threshold of being a small company in the "second-tier" sector and became a quick target for members of presidential family. Kenes Rakishev, a son of a former Foreign Ministry official and representative of the new generation

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[871] Hoon KIM Sung, "Being Young Means There Are More Chances," *Daily Tomorrow*, 2018, http://www.dailytw.kr/news/articleView.html?idxno=17840.
[872] Cash Magnum, "Magnum | Company Magnum," accessed November 3, 2021, https://magnum.kz/page/aboutmagnum.
[873] Staff Kursiv, "The Largest Kazakhstani Retailer Is Expanding into New Market," *Kursiv Kazakhstan*, 2020, https://kursiv.kz/en/news/kompanii/2020-09/largest-kazakhstani-retailer-expanding-new-market.
[874] Staff Forbes, "Aleksander Gaber," *Forbes Kazakhstan*, 2021, https://forbes.kz/ranking/object/104.

of oligarchs, came to the party of dividing the shares first when he bought 30% of Magnum.[875] After the exchange of shares between the oligarchs, in 2020 the subsidiary of the Caspian Trading Company mysteriously became the sole owner of the company, replacing Garber's rein after 14 years. According to insiders, Garber was briefly arrested, after which he had to give up ownership to members of the family, Kayrat Satybaldy and Bolat Nazarbayev, who became the new owners of Magnum.[876]

[875] Staff Banker.kz, "Vyacheslav Kim Bought out a Stake in Magnum from Kenes Rakishev," Banker Kazakhstan, 2017, https://www.banker.kz/news/vyacheslav-kim-bought-from-kenges-rakishev-share-o/.
[876] Kazakh, "A Forecast for Bolat Nazarbayev's Future."

Chapter 6. Conclusion

The primary goal of this dissertation was the need to address the underlying factors behind the problems of authoritarian governance, with its high level of state interference in the economy and the corrupt nature of state-business interactions in the former Soviet states. Among these lingering issues, this dissertation is particularly motivated by one puzzling phenomenon: following a brief period of marketization and privatization that began in the late 1990s, the economies of Russia and Kazakhstan rolled back their commitment to free markets and espoused increased state control in important sectors of economy. This resulted in state-led capitalist economies in these countries in which the state carved out a large portion of important sectors, leaving the less important ones to the market sector. From an economic perspective, a state-led economic model which relies on significant state ownership and control is generally less efficient than one that gives priority to private actors. The question then is why did political elites have the incentive to reestablish state control over important economic sectors, instead of reformulating privatization programs and pursuing economic efficiency? This dissertation argues that an answer to this question lies in a deep understanding of power consolidation and political survival in the personalist authoritarian regimes of these countries.

6.1 Summary of findings: how theoretical framework applies to the case studies

This dissertation investigated the linkages between the political context of personalist authoritarian regimes and the rise of economic models that allow a greater role for state control and ownership, with a primary focus on Russia and Kazakhstan. Through meticulous analysis, the dissertation found that presidents Vladimir Putin's and Nursultan Nazarbayev's decisions to reestablish state control over key sectors of economy in Russia and Kazakhstan goes beyond their autocratic whims or programs of economic modernization. These autocrats' decision to install state-led economic systems is inherently linked to certain *structural* factors specific to their personalist authoritarian regimes: the nature of political insecurity and power consolidation in the early stage, the necessity of political survival in later stages, and the nature of dominant economic system in the country. This dissertation has argued that these factors produced *political order* in Russia and Kazakhstan which incentivized these autocratic presidents to pursue interventionist economic policies that favor heavy state control.

The analysis linking early political consolidation and rise of state expropriation and economic nationalism key sectors in Russia and Kazakhstan clearly demonstrated this argument. The dissertation found that due to the irreconcilable tension between social forces brought about by early liberal economic reforms and the necessity of consolidating power and extending survival, both presidents turned toward state activism in terms of ownership of strategic assets. As analyzed throughout the dissertation, this process worked in quite similar fashion in both countries. Neoliberal reform of privatization and liberalization that both Russia and Kazakhstan unleashed following the breakup of Soviet Union resulted in the concentration of important economic assets in the hands of a new and exclusive economic class, oligarchs, and multinational companies in Russia and Kazakhstan. Putin and Nazarbayev saw this precarious system as the ground in which political opposition by diverse power centers can emerge and political instability can ensue, as demonstrated in several cases. Thus, these presidents began to consolidate power and stabilize the regime through centralization and targeted repression. The logic of power consolidation and subsequent regime survival required both presidents to conduct asset expropriations and establish state control over certain strategic sectors, while allowing limited market freedom for regime loyalists, foreign companies, and small businesses. The personalization of power under Putin and Nazarbayev over the years further increased presidential discretion in economic governance and perpetuated the pattern of arbitrary state intervention and control over strategic sectors.

This dissertation also found that the emergence of political order in Russia and Kazakhstan bred a distinctive *economic order* which is subject to the logic of political survival. Through its detailed analysis, this dissertation demonstrated how the logic of acquiring and exercising political power and extending survival in personalist authoritarian regimes led to an emergence of state-led capitalism in both Russia and Kazakhstan. Following power consolidation, Putin and Nazarbayev effectively personalized their respective political systems, further increasing their autocratic discretion over the political and economic policymaking. Such personalized political systems brought structural changes to the existing economic arrangements in Russia and Kazakhstan that had previously involved the interplay between fair market forces and benign state regulation. The new political economy that emerged under the personalist regimes of Putin and Nazarbayev featured *dualistic state capitalism*. This dissertation conceptualized this economic order as the one in which the state asserts special

rights to govern strategic *state sectors* of economy through its prerogative of interference and ownership, while allowing the bulk of private businesses to operate in the *market sector*. In this new economic order, the state emerged as an active manager and owner of strategic economic assets through targeted expropriations for supposedly "economic modernization" purposes, while the rest of the economic sectors, deemed not strategic, became open to market forces.

This dissertation found that the state sector in Russia and Kazakhstan is composed of important industries such as oil, gas, heavy industries, and banking. Lying at the core of the economy, these strategic sectors have been important for autocrats to consolidate power and facilitate survival thanks to the revenue, export earnings, and employment that they provide. The important players in these state sectors are the national champion state-owned enterprises (SOEs) or wealth funds whose rents allowed both presidents to enrich themselves, provide patronage to the loyal supporters and general populace, and gain leverage in domestic politics. Through these state companies, both presidents concentrated massive economic and political power in their hands. The only political exception was given to oligarchs who stayed in between having foot in both sectors. In addition to the findings in the state sector, the dissertation provided a thorough analysis of the market sector, or periphery economy, which consists of private businesses in second-tier sectors of the economy such as manufacturing, construction, or retail that has no barrier for entry to almost anyone. A few cases of small businesses in Russia and Kazakhstan showed that these entrepreneurs are petty capitalists who find themselves being regulated by local market forces, although the proximity to the governing elite gives some privilege to their businesses.

Finally, this dissertation found that due to the nature of the regime coalitions and inner circles around the presidents, state-led capitalism in Russia and Kazakhstan features two versions: *crony-style* and *family-dominated* state capitalism. Crony-style state capitalism in Russia features an economic system in which powerful friends and cronies of the president Putin dominate the major sectors of economy through a uniquely designed state-private partnership. Taking advantage of the positions at the state companies and living off government contracts, these political elites and crony oligarchs been able to generate massive personal wealth and transferred Russia into a kleptocratic country. In contrast, the dissertation found that *family-dominated* state capitalism in Kazakhstan is dominated by the extended family members of the president Nazarbayev. The strategic sectors of the economy such as the oil and gas industry

were concentrated under a single sovereign wealth fund, Samruk Kazyna, which has been governed as the family business over the years.

The scope of the theoretical framework presented here provides explanations to the conditions and mechanisms in which the logic of political survival and rent seeking breeds autocratic state capitalism following economic liberalization. The theory can in fact offer several implications about cases where economic and political reforms do not backslide into economic nationalism in the post-Soviet states. An interesting puzzle is the question of why such post-Soviet countries as Georgia or Ukraine that conducted modest liberal economic reforms did not themselves backtrack toward the temptations of economic nationalism. The theory of this dissertation suggests that differences in the development of political institutions, linkages to the global economy, and availability of natural resources seem hold the answer to the puzzle. The consolidation of power under a single autocrat against weak democratic forces and the availability of massive resource rents facilitated the emergence of state capitalism in Russia and Kazakhstan. In contrast, the strength of social control, diversity of political forces, and relative absence of resource rents seem to have strengthened democratic and market institutions in such countries as Poland, Ukraine, and Georgia in among the post-Soviet states. Such forces seemed to balance liberal market forces against leaders' political temptations to slide into rent-seeking and economic nationalism.

What kind of value-added this analysis offers to the extant literature? Through empirical analysis, this dissertation offered a nuanced discussion of state capitalism in the post-Soviet area by combining two related but distinct fields, political economy, and regimes analysis. The value of this dissertation comes from its break from the existinging literature that offers non-systematic analysis of state capitalism in different parts of the world. By bringing structural analysis of the political systems in Russia and Kazakhstan into the equation, this dissertation offered a novel explanation of the conditions and mechanisms of how distinct types of dictatorial state capitalism may emerge. Also, by combining big and small private businesses along with state dominant sectors into a holistic view, the dissertation produced a more complete theorization of the *dualistic* nature of state capitalism, adding a new dimension to the discussion. Such dualistic analysis will enable a better understanding of the puzzling coexistence of liberal economic principles with non-democratic state capitalist systems, including a freer business

environment conducive to private ownership and foreign investment, along with their political rationale.

6.2 The varieties of state capitalism in comparative perspective: the party-style state capitalism in China

The primary case studies of this dissertation are Russia and Kazakhstan. Although the political and economic context of these post-Soviet states prove to be unique in various dimensions, the theoretical discussions and findings of this dissertation can be applied to broader contexts, including the state capitalist economies of developing world. The argument of this dissertation is that the rise and functioning of state capitalism as an economic system in which the state directs economic ordering is closely linked to the logic of regime survival in the authoritarian context. Self-enrichment, the provision of patronage, and mitigation of exogenous shocks are several pathways through which state capitalism assists the regime elites with political survival. Although specific functions of state capitalism may differ depending on conditions, at the end, through a state-controlled economy, the political elite consolidates and maintains power in authoritarian regimes. This logic can be observed in several types of authoritarian regimes that practice *national varieties* of state-led capitalism in Asia and Middle East.[877] Among the ardent practitioners of state capitalism, China can indeed be an exemplar with its *modus operandi*.

Chinese state capitalism stems from its unique blend of political and economic systems[878] . In politics, China is a single-party authoritarian regime that does not allow open political competition from other political parties. In the economy, China morphed from a Soviet-style centrally planned state socialism into a hybrid economic system in which state companies and private businesses coexist but compete in an uneven playing field. As Wu puts it, "while the Party-state holds vast control levers, it allows market forces to play out in huge swaths of

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[877] Ilias Alami and Adam D. Dixon, "State Capitalism(s) Redux? Theories, Tensions, Controversies," *Competition & Change* 24, no. 1 (2020): 43, https://journals.sagepub.com/doi/full/10.1177/1024529419881949?fbclid=IwAR0XQXORIvBjM_vskF3Du71ETeqv24ZnVWJg8hVizxM33x0Zlk4fPPklg3M&.

[878] Barry Naughton and Kellee S. Tsai, *State Capitalism, Institutional Adaptation, and the Chinese Miracle* (New York: London: Cambridge University Press, 2015), 2, https://www.cambridge.org/core/books/state-capitalism-institutional-adaptation-and-the-chinese-miracle/B22E95BADECE68CF04EC39682D8953C8.

the economy."[879] Chinese state capitalism as a whole can be branded as contemporary state capitalism: its approach to the control and competition in the hybrid economy shares both similarities and differences with the crony- and family-dominated versions of Russian and Kazakhstan.

A close similarity that Chinese state capitalism shares with the cases under study lies in the fundamental logic behind the economic systems: China has successfully integrated political control and economic efficiency in line with its objective of maintaining regime power.[880] However, unlike the highly *personalist* versions of state capitalism in Russia and Kazakhstan, *party-led* state capitalism in China created a relatively liberal and productive economy that enabled high economic growth for years with a degree of political legitimacy and stability.[881] In essence, Chinese party-state capitalism is built around collective party leadership which maintains a balanced interaction among such objectives as top-down political control over strategic sectors, a bottom-up competitive market economy, and integration into global economy. As in the case of Russia and Kazakhstan, the state capitalist system in China that merges political control with market freedom created a "tiered economy": the top tier is composed of large state-owned companies in strategic sectors, while the bottom tier is dominated by small-scale businesses in non-strategic sectors, including manufacturing and services.[882]

The first important pillar of the Chinese state capitalism is the party's direct control over the most critical sectors, including energy, telecommunication, finance, and other natural monopolies. Although for the most part this highly competitive economy is driven by the initiatives of private sector, the Communist Party holds the prerogative to control the strategic sectors, support priority industries, and use regulatory and financial incentives to drive development towards political objectives.[883] As in the case of Russia and Kazakhstan, the

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[879] Mark Wu, "The 'China, Inc.' Challenge to Global Trade Governance," *Harvard International Law Journal* 57 (2016): 282.
[880] Margaret Pearson, Meg Rithmire, and Kellee S. Tsai, "Party-State Capitalism in China," *Current History* 120, no. 827 (September 1, 2021): 207–13, https://doi.org/10.1525/curh.2021.120.827.207.
[881] Joshua Kurlantzick, *State Capitalism: How the Return of Statism Is Transforming the World* (Oxford, New York: Oxford University Press, 2016), 96.
[882] Naughton and Tsai, *State Capitalism, Institutional Adaptation, and the Chinese Miracle*, 32–37.
[883] Nis Grunberg, "Party-State Capitalism under Xi: Integrating Political Control and Economic Efficiency," *Mercator Institute for China Studies*, 2021, https://merics.org/en/party-state-capitalism-under-xi-integrating-political-control-and-economic-efficiency.

Communist Party attaches high importance to state-owned enterprises (SOEs) as an economic foundation.[884] China's largest SOEs maintain dominant market positions in many of these sectors, ensuring the Party's ability to govern the Chinese economy.[885] In the mid-1990s, China's SOEs contributed only 10% of GDP, but since the early 2010s they have grown to account for 25% of GDP.[886] According to estimates, the assets of the top 100 SOEs account for more than $63 trillion, which is nearly 80% of global GDP.

Unlike the highly inefficient SOEs of post-Soviet countries, China's SOEs rose to become productive competitors in the global economy thanks to a series of institutional and corporate governance reforms in the late 1990s that eliminated unproductive SOEs.[887] Once they were restructured, China's SOEs in selective sectors were subjected to market competition with a few other state enterprises in a controlled manner. The strategic value of sectors, determined by political considerations, influenced the government's decision to either decentralize or centralize state control of SOEs in industrial sectors. According to Lin and Milhaupt, more than two-thirds of Chinese companies in the Global Fortune 500 consist of SOEs.[888] From economic and political perspectives, the Party values SOEs not only as macro-economic levers during exogenous shocks, but also the provider of critical economic resources that help maintain the regime power.[889]

Since the reign of Xi Jinping began in 2012, the Party redesigned the "muscular form" of state capitalism, increasing the importance of the state sector in the economy. As *The Economist* puts it, such state capitalism requires that "state-owned companies get more market

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[884] Li Xing and Timothy Shaw, "The Political Economy of Chinese State Capitalism," *Journal of China and International Relations* 1, no. 1 (2013): 94, https://www.semanticscholar.org/paper/The-Political-Economy-of-Chinese-State-Capitalism-Xing-Shaw/b15e2d2488e8cdb628c38591aab8132446d906af.

[885] Jude Blanchette, "Confronting the Challenge of Chinese State Capitalism" (Washington, D.C: Center for Strategic and International Studies, 2021), https://www.csis.org/analysis/confronting-challenge-chinese-state-capitalism.

[886] Kurlantzick, *State Capitalism*, 100.

[887] Barry Naughton and Kellee S. Tsai, *State Capitalism, Institutional Adaptation, and the Chinese Miracle* (New York: London: Cambridge University Press, 2015), 35–45

[888] Li-Wen Lin and Curtis J. Milhaupt, "We Are the (National) Champions: Understanding the Mechanisms of State Capitalism in China," *Stanford Law Review* 65, no. 4 (2013): 697–759.

[889] Dong Zhang, "State Capitalism and the Logic of Political Survival" (PhD dissertation, Illinois, Northwestern University, 2016), https://www.proquest.com/openview/45d8bff99adcc3f1c9ad7f48e52574f7/1?pq-origsite=gscholar&cbl=18750.

discipline, while private enterprises get more party discipline."[890] In this new version of state capitalism, SOEs should become more efficient, stronger, better, and bigger, and team up with private companies, if necessary. Although the government seems to be profit-driven industrial policy and commercialization through the SOEs, the political rationale is the highest priority for the leaders. SOEs are politically important for Party leaders as the holders of state assets. Serving in the boards of directors, Party leaders have political utility in promoting the SOEs.[891]

Figure 28.

Another important feature of state capitalism in China is that heavy state control coexists with a highly competitive and dynamic market economy, the missing variable in Russia and Kazakhstan. The free market economy in China is not overwhelmed by the planned economy. Large parts of China's economy operate on the basis of market principles which allow a prominent role for private companies.[892] To the extent that the Communist Party provided a safe place for private capital, it gave a preference to the direct investment by foreign corporations. Following economic reforms, the Chinese government adopted several policies to allow private companies to open businesses, including the security of property rights, an easing of ideological stigma, and political legitimacy.[893] Over the years, the role of the private sector in China rose to an unprecedented level thanks to state policies, greater efficiency of private companies, and commercialization of bank lending. Being literally non-existent years ago, the private companies came to contribute around 60% of China's GDP and produced around 40% of exports by 2013.[894] The dynamism of private sector development in China produced highly valuable corporations with a global scope of operations, including Alibaba, Tencent, and Huawei.

[890] Staff, "Xi Jinping Is Trying to Remake the Chinese Economy," *The Economist*, 2020, https://www.economist.com/briefing/2020/08/15/xi-jinping-is-trying-to-remake-the-chinese-economy.
[891] Grunberg, "Party-State Capitalism under Xi: Integrating Political Control and Economic Efficiency."
[892] Nicholas R. Lardy, *Markets Over Mao: The Rise of Private Business in China* (Peterson Institute for International Economics, 2014).
[893] Stephan Haggard and Yasheng Huang, "The Political Economy of Private Sector Development in China," in *China's Great Economic Transformation*, ed. Loren Brandt and Thomas G. Rawski (Cambridge: Cambridge University Press, 2008), 337–74, https://doi.org/10.1017/CBO9780511754234.011.
[894] Lardy, *Markets Over Mao*, 86–88.

Despite the growing wealth and influence of private sector actors, Communist Party elites managed to thwart the political challenges that the oligarchs once tried to exert on the liberalizing regimes of Russia and Kazakhstan. The Communist Party was highly successful integrating Chinese capitalists into the political system, thus co-opting them to become an important base of support. In earlier times, leadership controlled the private sector economy through the instrument of personnel control over local government officials who themselves have various tools at their disposal to shape the local economy. In this state-led capitalist system, both political elites and capitalists became dependent on each other to promote growth. However, since the rise of Xi Jinping, the cozy relationship between the Party and business started to deteriorate due to the growing influence of the latter. Market-driven economic growth began to be replaced by the resurgent role of the state.[895] The fundamental tenet of the Party under Xi became to reestablish domination over both political and economic aspects of society.[896] The government re-installed control over private business through placing Party members on the board of companies, depriving them of credit or absorbing them into state companies. The Party adopted new guidelines to "continuously enhance the political consensus of private businesspeople under the leadership of the party."[897]

Finally, China's state-led capitalism is characterized by the elite's focus on positioning the country in the global economy. In contrast to the relative global isolation of resource-abundant state capitalism in Russia and Kazakhstan, China's state capitalism is heavily reliant on the global economy. From the 1990s, China started to orient its development strategy towards integration into the global economy through export promotion. China's new growth strategy was further facilitated by low investment rates and over-accumulated capital in the West.[898] Party leadership made strategic use of incoming foreign investment and industrial policy and

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[895] Nicholas R. Lardy, *The State Strikes Back: The End of Economic Reform in China?* (Washington, D.C: Peterson Institute for International Economics, 2019), https://www.piie.com/bookstore/state-strikes-back-end-economic-reform-china.
[896] Richard McGregor, "How the State Runs Business in China," *The Guardian*, 2019, July 25 edition.
[897] Lingling Wei, "China's Xi Ramps Up Control of Private Sector. 'We Have No Choice but to Follow the Party.,'" *Wall Street Journal*, 2020, December 10 edition.
[898] Ho-fung Hung, "Rise of China and the Global Overaccumulation Crisis," *Review of International Political Economy* 15, no. 2 (April 16, 2008): 149–79, https://doi.org/10.1080/09692290701869654.

promoting the country's deep, yet selective, immersion into global supply chain networks.[899] As a result, China emerged as the world's second largest economy, biggest trading nation, and largest exporter. Such development then started a "recentering of the global economy and a restructuring of competitive relations in international markets has taken place."[900]

Figure 29.

In short, the Chinese example shows that despite differences in approach, the primary goal of state-controlled economies in authoritarian regimes is its ability to allow political elites to consolidate their hold on power and ensure continuous survival. In the context of China, political considerations of sustaining the economic and political stability of the single party regime led Communist Party elites to establish a state capitalist system where the party controlled key sectors while allowing a certain degree of a competitive market economy and economic internationalization. However, under Xi Jinping, China has entered in a new version of state capitalism in which the party has entrenched the state control at the expense of a liberal economy where the Party has sought to integrate the Party organizations with private enterprises.

6.3 The policy implications: the political economy of development and market reform in authoritarian regimes

This dissertation has attempted to explain state control of the economy through the framework of political survival in an authoritarian context. The findings of this dissertation provide insightful reflections and implications, both theoretical and policy, for comprehending the political economy of development and market reforms in authoritarian regimes. The application of the analytic framework developed in this dissertation is of great importance as the existing analyses of political economy of authoritarian rule in contemporary Russia and Kazakhstan limit their investigation to the catchall concepts of crony or patrimonial capitalism and overemphasize their explanatory value. In that sense, this dissertation constitutes one of the few attempts in that it scrutinizes the political basis of state control over the economy in Russia and Kazakhstan and contributes to the scholarly literature on the subject. Finally, the

[899] Andreas Nölke, "Second Image Revisited: The Domestic Sources of China's Foreign Economic Policies," *International Politics* 52, no. 6 (November 1, 2015): 657–65, https://doi.org/10.1057/ip.2015.13.
[900] Tobias ten Brink, "The Challenges of China's Non-Liberal Capitalism for the Liberal Global Economic Order," *Harvard Asia Quarterly* 16 (November 28, 2014): 36–44.

implications of this dissertation hold important substance for future research on comparative state capitalism in different authoritarian regimes. It is right to state that without reference in the functioning of state-led economies in different authoritarian regimes in countries that share certain similarities with the case studies, it would hardly be possible to determine possible ways of building genuinely functioning capitalist democracies.

There are few policy implications that the argument of this dissertation holds. The most important is related to the general topic that deals with the political logic behind state control over the economy. In fact, studies on the state control over the economy were mostly neglected by scholars of political economy in authoritarian regimes. For long the area was dominated by two strands of studies, either the neoliberal approach or the statist approach to development theory. The neoliberal approach towards development focuses on efficiently allocating the resources via free markets and limiting state intervention to only property protection and contract enforcement. In contrast to the neoliberal approach, the statist approach puts faith to a more active state in regulating imperfect markets and directing economic development through industrial policy, market coordination and investment.[901]

As this dissertation briefly discussed in the literature review, the extant studies on the statist approach give a lot of attention to the role of "altruistic" political leaders in developing countries, including post-Soviet states, to genuinely advance socio-economic goals by facilitating the policies of state engagement in the economy. However, the existing literature provides little understanding into why and how certain states exert direct control over companies through state ownership and promote state-led investment for political motives. If it is the failure of markets, political leaders could mitigate such failures through active state regulation, not ownership. The major implication of my dissertation is that behind such state control over economic resources through ownership lies the goal of political consolidation and regime survival. My dissertation argues that political leaders maintain state control over the economy in the hope of first consolidating their reign and then prolonging the longevity and stability of the regime. According to my analytical framework, it is not out of the benevolence of political leadership to promote state activism through ownership and control for the sake of

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[901] Atul Kohli, *State-Directed Development: Political Power and Industrialization in the Global Periphery* (Cambridge: Cambridge University Press, 2004), https://doi.org/10.1017/CBO9780511754371.

economic modernization, but that state-controlled entities such as state corporations and SOEs are economic means of the regime whose control first enables the leader to consolidate power and further his survival through the patronage rents they provide to the elite and public. Such an argument explains how economic resources an important source for autocrats can be to consolidate and maintain regime stability. This provides a better explanation than existing works in authoritarian regime analysis which has long argued of the importance of institutions as political parties and legislatures in regime stability but overlooked economic resources and interests that populated these institutions.[902]

The arguments of this dissertation have profound implications for the question of how power relations in personalist authoritarian regimes interact with market reforms and what that means for the overall market-building process. Since scholarly attention to transition studies has faded, scholars have long sidelined such issues from their analysis.[903] In general, issues related to the relationship between authoritarianism and markets is connected to two general debates in political economy. The first is the role of the state in economic development, as briefly discussed above, and the second is the relationship between capitalism and democracy. However, neither of these debates directly explain the links between authoritarianism and market, although both provides indirect insights about potential linkages.

In developmental state literature, several features of developmental states such political repression and strong bureaucracy led scholars to associate such states to authoritarian regimes. Woo-Cumings writes that there is a relationship between 'the developmental state' and authoritarianism.[904] Johnson argues that authoritarian regimes of late 1960s selectively used markets forces to solve political issues of economic development, "namely, how to mobilize the overwhelming majority of the population to work and sacrifice for developmental projects."[905] However, such analyses are one-dimensional and old enough to have lost its applicability due to the ongoing diffusion of democratization and globalization. Reanimating this decades-long

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[902] Jennifer Gandhi, *Political Institutions under Dictatorship* (Cambridge University Press Cambridge, 2008).

[903] Andrew Barnes, "From the Politics of Economic Reform to the Functioning of Political Economies," *Demokratizatsiya the Journal of Post-Soviet Democratization*, Special Issue, "Twenty Years since the Collapse of the USSR: What Have We Learned?" 20, no. 2 (2012): 79–86.

[904] Meredith Woo-Cumings, *The Developmental State* (Cornell University Press, 1999), 69.

[905] Johnson Chalmers, "The Developmental State: Odyssey of a Concept," in *The Developmental State*, ed. Meredith Woo-Cumings, 1st ed. (Ithaca, N.Y: Cornell University Press, 1999), 52–53.

debate, this dissertation shifts the focus from the politics of economic development back to the political use of economic resources for regime survival. In doing so, this dissertation has presented empirical analysis through case studies to demonstrate that political leaders use state-owned assets not to promote economic modernization, but to distribute rents and patronage for their political survival. This insight implies that political calculations might come ahead of economic benefits in developing countries in which state has "neo-developmental" inclinations in rearranging their economies.

This dissertation's discussion of the relationship between politics of authoritarianism and market reforms can also provide insights into this relationship's connection to the nexus of capitalism and political regimes. Scholars of modernization theory have long argued that there is abnormal link between authoritarianism and capitalism.[906] This is especially true for transition economies, including post-Soviet states, where the development of market and democracy was asynchronous: economic transformations did not follow the end of old rules and political accountability. Manzetti argues that without such changes, political leaders can manipulate market reforms "in a way that creates opportunity for corruption, crony capitalism, and political patronage", creating conditions for unstable economies and rent seeking.[907]

However, scholars of the modernization paradigm do not address why authoritarian regimes advocate markets in the first place since the scholars tend to see state-led market authoritarianism as a short-term distortion in the modernization process. This dissertation provides the implication that state-led market authoritarianism is not a distortion of capitalist democracy but rather a distinct politico-economic order in authoritarian regimes that emerges as a byproduct of power consolidation and political survival. This implication arrives from the argument of the dissertation: as markets create a new set of threats to the stability of authoritarian rule, autocrats introduce selective market reforms in specific sectors so that such reforms satisfy specific needs of the regime. This dissertation provides empirical analysis of how the regimes in Russia and Kazakhstan allow competitive market mechanisms in market

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[906] Adam Przeworski et al., *Democracy and Development: Political Institutions and Well-Being in the World, 1950-1990* (Cambridge University Press, 2000), 1950–90.
[907] Luigi Manzetti, *Neoliberalism, Accountability, and Reform Failures in Emerging Markets: Eastern Europe, Russia, Argentina, and Chile in Comparative Perspective* (Pennsylvania: Penn State University Press, 2009), 6

sectors such as manufacturing, trade, and services to co-opt the public that engage in small businesses and generate economic diversity in the economy.

In conclusion, this analysis of how authoritarian regimes utilize a mixture of state control and market mechanisms is crucial for our understanding of the contemporary ways in which authoritarian regimes have survived waves of democratization and turbulence in the global economy. At the same time, it is important to challenge existing practices of public policy that spread around different parts of the world. Many authoritarian regimes, including those of Russia and Kazakhstan, utilize the discourse of market logic in certain public sectors to legitimize its politico-economic arrangement, without committing themselves to the market economy in other sectors. Like the adoption of elections and party systems to ease the pressure of democratization, authoritarian regimes have learnt to espouse selective market reforms in the process of “marketization” to ensure such reforms fulfill the needs of their regimes.

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