

**Colour Revolution or Soft Authoritarianism?  
Different Ways to Cope with Similar Challenges in the Globalised World**

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## **Colour Revolution or Soft Authoritarianism? Different Ways to Cope with Similar Challenges in the Globalised World**

### *Abstract*

Why have colour revolutions, launching a regime change from authoritarianism towards democracy, erupted in some countries of the FSU while in other FSU countries, the regimes remain authoritarian?

The paper explains the different trajectories followed by countries that launched colour revolutions and those that remain authoritarian, contrasting revolutionary Ukraine with non-revolutionary Russia. It argues that both types of regime change came about for similar reasons, but had different natures, namely, that while the Orange Revolution is a discontinuous regime change, soft authoritarianism is a continuous one. Both implement the preferences of the influential elite, i.e. business groups. The nature of change depends upon the differences in characteristics within business groups, the availability of the oligarchic rents and the degree of implementation by which these preferences enter into Ukraine's and Russia's state politics.

### *Introduction*

In the transition from Soviet socialism, post-Soviet republics had to juggle the multiple tasks of building a national state, implementing democracy, moving towards a market economy and establishing a new legitimacy for state authority in society. Consequently, before the recent upheavals, i.e. colour revolutions erupting in Georgia, Ukraine, and the Kyrgyz Republic, the delayed transition in the economic sphere resulted uniformly in 'clan capitalism' and in political terms these countries landed somewhere within the 'grey zone' between democracy and authoritarianism.

The labels for the new regimes, i.e. 'defected democracy' (Merkel 1999, 2003, 2006; Croissant 2004), 'imitated democracy' (Furman 2006), 'illegal democracy' (Karatnucky 1999), 'competitive' or 'soft authoritarianism' (Levitsky and Way 2002; Ottoway 2003), reflected the idea of a continual transition, although whether this was a movement in the direction of democracy was disputable (Levitsky and Way 2002; Diamond 2002; McFaul 2002a). Those who considered 'authoritarian' and 'patriarchal' regimes to be the final outcome of this transition, as well as those who still hoped for a further democratisation of the former Soviet Union (FSU), were surprised at the colour revolutions. A lack in understanding of the ongoing transition was the reason why speculations ran wild regarding further radical democratic reforms in Georgia, Ukraine, and the Kyrgyz Republic and over the potential for the colour revolutions to spread within the FSU. After such speculations proved groundless, the limitations of attempting to explain the transition within the FSU through an ideological lens became evident.

The purpose of this article is to provide an analysis of why colour revolutions, launching a regime change from authoritarianism towards democracy, have occurred in some countries of the FSU, whilst the political regimes of other FSU republics have remained authoritarian in nature.

In contrast to previous research, which often only emphasises the similarities between those countries where colour revolutions have occurred, this paper applies most similar cases with different outcomes design and addresses these upheavals by contrasting revolutionary Ukraine with non-revolutionary Russia. These two countries had been following a similar transitional trajectory in their political and economic development, prior to the Orange Revolution taking place in Ukraine. These were the states with strong presidential power and

weak parliamentary oversight, where business groups—often called oligarchic clans—captured state authorities and where civil society was absent.<sup>†</sup> The economies of both these countries suffered from their Soviet legacies, e.g. inefficient over-industrialisation, energy intensive technologies, market distortions and rent-seeking opportunities. Partial economic reforms ran parallel and had similar outcomes in both Ukraine and Russia. In good times and bad, these countries, almost contemporaneously experienced the financial crises, whilst benefiting from similar driving forces in economic recovery. Nevertheless, since 2004, both Ukraine and Russia have been moving on divergent paths. In applying the research question to these countries, the aim of this paper is to analyse why the Orange Revolution occurred in Ukraine, while the political regime in Russia remained authoritarian.

This paper assumes that the divergent course of institutional change in both Ukraine and Russia depends upon the differences in the characteristics of the Ukrainian and Russian business groups, the availability or disappearance of their oligarchic rents and the degree of implementation by which these dynamic business preferences enter into both Ukraine's and Russia's state politics.

This paper is organised as follows. In the first part, the article outlines a theoretical framework based upon the neo-institutional approach for the analysis of colour revolutions and non-revolutionary changes. Having identified business groups as the main domestic drivers of institutional change in post-Soviet rent-seeking societies, the second part summarises the similarities and differences in the make up of these Ukrainian and Russian business groups. The third part takes a closer look at the dynamics of the oligarchic preferences and argues that these preferences depend upon the sources of the rents. This part also concentrates on the sources of the oligarchic rents and on the way that both global and domestic forces supply and constrain opportunities for these rents. Finally, this paper analyses the links between the business groups and state rulers, whilst addressing the issue of whether the state policies of both Ukraine and Russia correspond to the dynamic preferences of the business groups.

### *Unravelling the mystery of colour revolutions*

The question of whether the title 'revolution' is deemed appropriate, in the events that this article will be addressing, depends upon the definition that one uses. Theories of revolution do not provide a clear-cut definition of revolution. Understanding of revolutions, their causes, processes and consequences are revised after every wave of change in the world's political structure. As a result, by the end of the 20<sup>th</sup> century, there are now four generations of revolutionary theory.

Each generation has its own interpretation of what defines a revolution. The comparative school on the 'natural history of revolutions' referred to as the first generation of revolutionary theory. This school has a radical definition of revolution as being a point that 'marks a new era or ends forever the abuses of the old regime or digs a gulf between the old X and the new Y' (Brinton 1938, reprinted 1965, p.237). Similar to the school on 'natural history', the second generation considers modernisation and structural functionalism as part of their definition of revolution. However, representatives of the second generation describe revolution more moderately as 'a rapid, fundamental, and violent domestic change in the dominant values and myths of a society, in its political institutions, social structure, leadership, and government activity and policies' (Huntington 1968, reprinted 1977, p.264). The third generation examines social revolutions using a structural approach and combines

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<sup>†</sup> This paper uses the terms "oligarchic" or "business" and "clans" or "groups" to describe those business entities with a wide influence over national politics, which exist in the post-Soviet era. The reader should take into account that these terms describe the same objects, but are differently employed for the populist purposes of those, who use this terminology to reflect their own negative or positive attitudes to these business entities.

the revolutionary features adumbrated by previous generations. Thus, Skocpol (1979, p.4) defines social revolution as ‘rapid basic transformations of a society’s state and class structures...accompanied and in part carried through by class-based revolts from below...set apart from other sorts of conflicts and transformative processes above all by the combination of two coincidences; the coincidence of societal structural change with class upheaval and the coincidence of political, with social, transformation’. The ideas of the third generation were taken as standard through the 1970s and 1980s. However, in the last decade of the 20<sup>th</sup> century, the structural approach was challenged as new events around the world occurred which no longer fitted in neatly with structural definitions of what a revolution meant. The appearance of failed states in Africa, transition in the post-Soviet era, guerrilla warfare in Latin America and the dissemination of Islamic fundamentalism over the world created an intense impulse for the fourth generation. This last generation of revolutionary theory incorporates into its interpretation, issues like revolutionary ideologies, ethnic and religious bases for revolutionary mobilisation, intra-elite conflicts and the possibility of multi class coalitions (Goldstone 2001, p. 140). It describes revolution as ‘the forcible overthrow of a government followed by the reconsideration of authority by new groups, ruling through new political (and sometimes social) institutions...although the fall of a government may be sudden, the causal trends leading up to that fall, the ensuing struggle for power among contenders and the reconstruction of a stable state often span decades’ (Goldstone 1991, p.37).

Each generation not only becomes less radical in its understanding of the sort of upheaval that could constitute a ‘revolution’, but also emphasises the different causes, processes and consequences of revolutions. Nonetheless, the different definitions still have common features: (a) change of regime without reverse possibilities; (b) change of economic and social structures; (c) change of state political institutions by means of non-institutionalised and anti-constitutional actions; (d) change, driven by some class or elite group, to replace the incumbent ruling group; (e) change legitimised by some ideology or doctrine; (f) change enforced through mass mobilisation and (g) change occurring through violence or the threat of violence, despite repression instigated by the existing authority.

The attempt to identify the common features of the events of 2004 in Ukraine brings mixed results. The presidential election was a contest between two main candidates: Viktor Yanukovich, the current prime minister, leader of the ‘Party of Regions’ (*Partiya Rehioniv*) and favourite of the outgoing president Leonid Kuchma, and Viktor Yushchenko, the opposition leader of the ‘Our Ukraine’ (*Nasha Ukrayina*) fraction in the Ukrainian parliament and a former prime minister. After the run-off vote of the presidential election, a series of protests took place in the capital of Ukraine. Electoral fraud was the catalyst for these protests. The incumbent state authorities rigged the results of the election in favour of Yanukovich. The reports of a few domestic and foreign election monitors, combined with opposition media broadcasting, promoted the dissemination of these protests nationwide. The local councils in a few pro-Yushchenko Ukrainian regions refused to accept the official election results. At the same time, local officials in Eastern and Southern Ukraine, which supported Yanukovich, proclaimed their intentions regarding the federalisation of the country, if the victory of Yanukovich was not recognised. Finally, the decision of Ukraine’s Supreme Court ended the political crisis by annulling the original results of the run-off and ordering a re-vote.<sup>‡</sup> Shortly after the resolution made by the Supreme Court, the Ukrainian parliament passed the ‘package deal’; namely, it approved revised laws on elections and put the changes to the Constitution, in order to reduce presidential power and turn Ukraine into a

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<sup>‡</sup> The strong dependence of the judiciary on the executive in Ukraine lets the author assume that the resolution of the Supreme Court is a part of the ‘package deal’.

parliamentary-presidential republic.<sup>§</sup> The results of the re-vote on December 26, 2004 gave victory to Yushchenko and peacefully led to the successful conclusion of those events, now famous as the Orange Revolution.

On the one hand, many features of a classical revolution are present in these events (Fairbanks 2007). Firstly, a new political parliamentary order replaced the old political regime, the distribution of power between white-blue and orange elite groups changed and possibilities for the monopolisation of state authority by any one political force diminished.\*\* Second, political institutions were changed and Ukraine was transformed into a parliamentary-presidential republic. Third, these events found widespread support from all over Ukraine. During the two-week revolution, thousands went out on to the streets and protested against the electoral fraud. At the peak of this protest, 1.5 million supporters of the Orange Revolution demonstrated in and around Maidan in Kyiv (Kudelia 2007).

On the other hand, some events that occurred during and after the Orange Revolution in Ukraine hardly confirm the idea of a revolutionary regime overthrow. First, the achievements of the Orange Revolution were minimally radical. The decision for a second run-off presidential election was a negotiated compromise between white-and-blue and orange political forces. The agreement on a new run-off, combined with constitutional reform, from one perspective, reduced the achievements of the protests for the opposition orange forces, but still enabled a re-vote; whilst from another viewpoint, this agreement softened the defeat experienced by the white-and-blue forces, as constitutional reform meant that the new president had lost his power, thereby diminishing the value of the presidential position, as a result. Second, it only appeared that a new ruling group had replaced the old ruling group. The activists of the Orange forces had actually started their careers within the apparatus of the old regime. Moreover, in the following election of 2006, the 'Party of Regions' returned to their previous position as the main holders of political power by winning the parliamentary election and obtaining a large majority within parliament, along with the Communist and Socialist Parties. Viktor Yanukovich, with the support of the 'Our Ukraine' bloc, once again became prime minister. Third, the return of the white and blue coalition proved inconsistent with the main feature of a revolution involving change in society and state authorities, without reverse possibilities. Fourth, the mass protest was not supported by any ideology or doctrine; instead these were protests against election fraud. Fifth, the Orange Revolution was not class-based and did not lead to any changes in social structures. Finally, the protests were peaceful. Moreover, the incumbent ruling group did not attempt to take power by means of repression or military force.

Overall, comparisons of colour revolutions with classical revolutions do not provide any clarity because colour revolutions can be explained in a variety of different ways. One could define them as revolutions and hence revise the definition of revolution once more, thereby establishing a fifth generation of revolutionary theory (Tucker 2007; Beissinger 2007; McFaul 2005). Alternatively, one could address them as new and largely non-violent sub-species of revolution and engage in an exercise in adjectives (Fairbanks 2007). Finally, one can reject the term revolution due to the impact of outside interference in the upheavals (Herd 2005; Popescu 2006). The dispute regarding whether colour revolutions are true revolutions contributes little to their understanding. Revolution theory has only a limited capacity to create a general definition, and reliable explanation, of what a revolution is. Revolutions occur due to different causes and evolve in different ways, are carried out by different actors

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<sup>§</sup> The 'package deal' is a label for the agreement made on the re-vote, the amendments of election law and the changes in the Constitution that the orange and white-and-blue forces debated during Round-table negotiations (Koliushko and Tymoshyk 2004).

\*\* Orange is the colour of Yushchenko's "Our Ukraine" bloc. White-and-blue is a symbol of Yanukovich's "Party of Regions".

and lead to different outcomes. Jack Goldstone (2001) summarises that the study of revolution is overwhelmed by the variety of cases and concepts it seeks to encompass. Each revolutionary wave broke out in different regions and in different time periods and had its own causes, processes and outcomes. Therefore, a much broader, generalised and contemporary definition of revolution, as discontinuous regime change in a specific part of the world at a definite period of time, is more useful. However, the creation of a new generation of revolutionary theory is not the aim of this paper.

Most studies on colour revolutions have utilised the method of agreement (Mill 1974), selecting cases on the dependent variable. Thus, they have concentrated on those countries where revolutions have taken place and where revolutions have been successful. Michael McFaul (2005) identifies the similarities of the upheavals and their differences to other democratic revolutions. Charles Fairbanks (2007) compares these upheavals, in a historical perspective, with the French and English Revolutions.

The application of the method of agreement on the dependent variable has its weaknesses. First, the only things that can actually be explained using a sample selected on the dependent variable are differences and similarities among selected cases (Geddes 2006). Regarding the issue of colour revolutions, the method of agreement makes apparent a catalogue of characteristics shared by all countries with experience of colour revolutions and concludes that, in the researched countries, these commonalities are the circumstances prerequisite for a successful revolution. Additionally, it infers that the causality relationship, within the researched group of cases, reflects the same causality relationships in the entire population of countries with experience of revolutions. However, there is no evidence to suggest that the revolutionary causes identified with the method of agreement are present or not in countries where no revolutions have occurred. The causes of revolutions and the favourable conditions required for revolutions to occur do not become clear until their absence is proved in non-revolutionary cases. Thus, countries, which have not undergone a colour revolution, should be included in the analysis. Therefore, to answer the research question, this paper contrasts revolutionary Ukraine and non-revolutionary Russia.

Second, revolutions are discontinuous change. However, similar changes of a continuous nature can occur in countries that have not experienced a colour revolution. According to Douglass North (1990, p.90), a discontinuous institutional change—different groups building a coalition to resolve a reform gridlock—takes place, if informal and formal institutions do not provide a ‘framework for actors to settle disputes and realise the potential gains’. If a state ruler ‘makes new bargains and compromises between players possible’, then institutional change can be continuous and go unnoticed. Referring to the neo-institutional approach, this paper considers colour revolutions to be cases of discontinuous institutional change, towards a more democratic regime, and non-revolutionary cases of being continuous institutional change, resulting in ‘re-launched’ authoritarianism.

Third, the method of agreement reveals the circumstances necessary for a successful revolution. These circumstances are mostly conditions, which favour the choice of a confrontation strategy and have a considerable effect on the outcome of the upheavals. The deeper reasons behind why some state and non-state actors—opposition or allies—decided to use or create these circumstances and confront the incumbent regime are still to be discovered, although the answer to this question is the key to understanding the colour revolutions. The neo-institutional approach links the nature of institutional change with the interactions between the most powerful non-state actors and a state ruler. Namely, if a state ruler implements the preferences of the most powerful non-state actors, the institutional change will be continuous. However, if a state ruler neglects their preferences, the most powerful non-state actors could calculate the costs and benefits of a confrontation strategy and thereby create a coalition in order to overthrow the political ruler. In addition, preferences and strategies of powerful non-state actors are in constant flux. Therefore, a state ruler is

consistently challenged to implement the dynamic preferences of powerful non-state actors in state policies, and to revise the 'rules of the political game' (Higley and Burton 2006), thereby providing a new institutional framework. This assumption directs attention to both the state and non-state actors who are powerful enough to instigate changes within the society.

Different actors and groups took part in the Orange Revolution and confronted the incumbent regime. The central question is: who were the driving actors in these events?

The usage of the term 'revolution' points towards the importance of the role civil society played (Opp 1994; Goldstone 1994). Indeed, reporters and politicians highlighted the important role of popular protests within the Orange Revolution and in so doing put into doubt the conventional presumption that civil society in Ukraine was weak. Moreover, some studies (McFaul 2005; D'Anieri 2005; Karatnycky 2005; Wilson 2005; Beissinger 2007; Tucker 2007) define civil society as the central driving force behind upheavals. Is it true that the activities of civil society led to the breakdown of Kuchma's regime? Are these popular protests the signs of Ukraine's established civil society able to articulate its interests? Or are these protests similar to the popular demonstrations of the early 90s in Eastern Europe and therefore overestimated?

Due to the low level of organisational membership within social organisations, the post-Soviet civil society (this is true for Ukraine, as well as for Russia) had the least participatory civil society in the world (Howard 2002; World Values Survey 2004) and was regarded as weak and passive.<sup>††</sup> Therefore, public choice was neither a driving nor constraining force during the previous transition years (Aslund 1999; O'Loughlin and Bell 1999; Howard 2000, 2002; Domrin 2003; McFaul 2002b).<sup>‡‡</sup> This weakness had many explanations. First, after the suppressive experience of mandatory membership in the communist organisation, the population generally distrusted new mass organisations and so opted against joining them (Howard 2002). Second, the population was still involved in the Soviet 'clientelist' and patrimonial networks, incorporated into the transition societies and therefore felt no need to participate in civil society (Vojtenko et al. 2002; Howard 2002; Pidluska et al. 2003). Among other barriers to greater citizen participation in non-governmental organisation (NGO) activities in Ukraine and Russia was the widespread disappointment associated with the political and economic results of transition. The World Bank study (2003) gives an insufficient public awareness of the importance of citizen participation in the governance process (67 percent) and the poverty of the majority of the public, whose main focus was upon their day-to-day survival (66 percent), as reasons for the weakness of civil society in Ukraine. The negative development of civil society in post-Soviet countries was accelerated by unfavourable demographic trends like depopulation and emigration causing the shortage of the social capital,<sup>§§</sup> i.e. a large proportion of young people, without experience of life under communism, and well educated people, who together had the potential of becoming the foundation stones of civil societies in their respective states, instead left their countries to live and work abroad.

Common features of the weakness within post-Soviet civil societies were the lack of trust in politicians and both governmental and non-governmental political institutions, the absence of a strategy or program relating to social society actions, and a distinct apathy and pessimism concerning both an individual, as well as their country's future (Stepanenko 2002; Golosov 2002-2003; Hritsenko 2002). In these countries, the NGOs and political parties as the main producers of participatory values were without mass support and virtually 'rootless'

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<sup>††</sup> World Values Survey, available at: <http://www.worldvaluessurvey.org/>, accessed 18 January 2008.

<sup>‡‡</sup> Even though unperfected, the common measurements of a civil society are the number of registered organisations and associations, and the percentage of citizens who are members of voluntary organisations and associations.

<sup>§§</sup> The majority of Ukrainian forced migrants (about 7 million) are either young or middle-aged, and therefore the most socially active.

(Golosov 2002-2003) and developed either under state auspice or through foreign finance. The state authorities continued to exert immense influence on the development of civil society through institutional regulations, while foreign foundations carried weight through financial means.<sup>\*\*\*</sup> The widespread traditions of political manipulations on and financial patronage of civil society in Ukraine (Lytvyn 2002) undermined the autonomy of the public protests during the Orange Revolution.

The absence of a strong civil society in Ukraine is also confirmed by statistical information. The national representative survey, 'Monitoring Ukrainian society' (*Monitorung Ukrainiskogo Suspil'stva*), reveals dramatically low levels of citizen participation in civic organizations and NGOs.<sup>†††</sup> Remarkably, civil society was weak a few months prior to the Orange Revolution and continues to remain weak well after 2004. After the revolution, the political disinterest and social apathy of most of the population, due to the change for the worse, i.e. lower individual income and a drop in living standards, can hardly confirm the institutionalisation of the norms and values of civil society in the country.

The puzzling phenomenon of mass demonstrations occurring during the Orange Revolution, despite the weakness of civil society, could be explained by arguing that the Orange Revolution was not the response of a developed and established civil society, but instead an emotional and psychologically charged popular protest based upon social dissatisfaction with the incumbent political regime. In line with the World Bank's study (2003), some experts outlined the dissatisfaction of the economical and political situation as the grounds for potential mass mobilisation at the time of the Revolution (Stepanenko 2006). According to this empirical and statistical evidence, the article defined the Orange Revolution in terms of 'the birthday' of a civil society that underwent an elementary stage in its development, but is still nascent in nature. Although the contribution made by the mass demonstrations towards the outcome of the colour revolutions was meaningful, such a nascent civil society could not so much as be described as the driving force behind the Orange Revolution, but rather more as its result.

Another possible driving actor could relate to leadership. Following a *first-level analysis*, institutional change, often called 'reform', is devoted to a new country's ruler coming to power either by means of uprising or through election. A few studies applied *first-level analysis* to explain the colour revolution and non-revolutionary cases, thereby highlighting the differences in personality and leadership style (Motyl 2006).<sup>‡‡‡</sup> However, Yushchenko and Vladimir Putin were not the type of charismatic leader that is usually seen in such situations. Moreover, in the FSU, state authority, which had already lost legitimacy during the Soviet era, became even weaker during transition as powerful rent seekers have controlled the governments of the post-Soviet states, since their respective independencies.

The rent-seeking business groups, often organized in oligarchic clans, were the only powerful actors, 'capturing state authorities' and controlling the enforcement and implementation of reforms during the early stage of transition (Hellman 1998; Karklins 2002). Referring to the ratings of the most influential people in Ukraine and Russia both before, and after 2004, business groups kept their immense influence in the politics and economy of both countries.<sup>§§§</sup>

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<sup>\*\*\*</sup> 'Concord' (*Zlagoda*), the Union of Ukrainian Businessmen and Managers and the League of Ukrainian Lawyers are counted as government operated, non-governmental organisations (GONGOs) in Ukraine. Walking Together and 'Ours' (*Nashi*) are examples of GONGOs in Russia.

<sup>†††</sup> Since 1992, the Institute of Sociology and National Academy of Sciences has annually conducted the survey, Monitoring Ukrainian Society.

<sup>‡‡‡</sup> Motyl, A. 'Ukraine and Russia: divergent political paths' 16 August 2006, available at: [http://opendemocracy.net/democracy-ukraine/russia\\_ukraine\\_3830.jsp](http://opendemocracy.net/democracy-ukraine/russia_ukraine_3830.jsp), accessed 18 January 2008.

<sup>§§§</sup> The ratings of the most influential persons in politics and the economy of Ukraine and Russia are periodically published by a few national journals and newspapers. For Ukraine, *Ranking of The Most Influential People of the Country*. *Hvardiya*, *Halyski Kontrakty*, 2002-2005; Rating of the 200 Most Influential Ukrainians 2007, in:

Business clans, with their hidden social networks, are not a new phenomenon within the political systems of the FSU. They have their origins in the Soviet past (Wedel 2003). In the early period of transition, the representatives of clans, possessing administrative resources in the Soviet system, had opportunities to turn reforms to their own advantage and accumulate large amounts of wealth. Furthermore, being the intermediate winners of transition, the clans put into place obstacles, to prevent future political and economic reforms in Ukraine and Russia damaging their interests. They also constructed political and economic institutions, which provided benefits for their financial empires. As these clans were interested in a reform gridlock, they are blamed for an incomplete market economy and distorted political system in the early 1990s (Hellman 1998, p.204).

According to the logic of a captured state, the successful implementation of Putin's reforms and full-fledged authoritarianism in Russia and the regime change via the Orange Revolution in Ukraine could only work with the support of Russian and Ukrainian business clans. In fact, Putin's policies were steeped in the preferences and requirements of this business elite (Steen 2003). Similarly, the dissatisfaction with the reform gridlock under Kuchma revealed a shift in the preferences of the Ukrainian elite, who, as their preferences were no longer being implemented in state policies, took action that ultimately led to the displacement of the president and the discontinuous change of a political regime.

In contrast to the previous transition years, most oligarchic clans directly or indirectly supported Putin's reforms in Russia, the Orange Revolution in Ukraine and the ensuing institutional changes, in the political and economic systems of both countries (Malynkovych 2006).<sup>\*\*\*\*</sup> Therefore, it is evident that the preferences of the elites in these countries changed.

By arguing that the colour revolution and 'soft authoritarianism' both involved institutional change, but with different natures, i.e. continuous in Russia and discontinuous in Ukraine, this paper addresses the driving forces behind these changes. As oligarchic clans play an important role in politics and the economy of Russia and Ukraine, this paper defines the similarities and peculiarities of the Ukrainian and Russian business groups.<sup>†††</sup>

### *Oligarchic clans: driving forces in a rent-seeking society*

#### a) Organisational structure

Although clan capitalism is widespread in the post-Soviet era, the Ukrainian and Russian clans differ from the classical understanding of clans. They are not groups of relatives or systems of kinship, as analysis on European and Asian clans has demonstrated (Collins 2004), but business entities.<sup>††††</sup> They are mainly interested in the accumulation of assets, profitable activities and new markets. Ukrainian and Russian clans are constructed into hierarchical levels. The top position is bestowed to a chieftain, who is surrounded by the core, the most trustworthy group of business partners, relatives and friends, while professionals and ordinary members, working in enterprises under clan control, hold the lowest positions in a clan's hierarchy. Agents of influence or patrons in politics take special place. Officially, they are not members of the clan, but their mutual support and co-operation are vital for the clan's

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Focus 51(64), 21 December 2007. For Russia, 100 Leading Politicians in 2007, *Nezavisimaja gazeta*, 17 January 2008, available at: [http://www.ng.ru/ideas/2008-01-17/11\\_politiks.html](http://www.ng.ru/ideas/2008-01-17/11_politiks.html), accessed 18 January 2008.

<sup>\*\*\*\*</sup> In Ukraine, the members of the oligarchic clans supporting the "orange camp" took part in the public protest personally, or indirectly through financial and media resources.

<sup>††††</sup> Although oligarchic clans in Ukraine and Russia are heterogeneous, this paper treats them as a single group in the political system of each country.

<sup>††††</sup> Relatives could be included in a clan, but actual relative relationships played a secondary role.

prosperity.<sup>§§§§</sup> However, the symbiosis between politics and economy does not involve a mere connection by patronage. The assimilation of clan members into politics and *vice versa* is a common phenomenon. In the Ukrainian and Russian transition, a special hybrid of political and economic actor, often called oligarch, appeared. In this sense, an oligarch is a political entrepreneur, who uses the strategy of ‘power-money-power’ for the accumulation and circulation of wealth. Thus, access to state power enables an oligarch to secure his economic interests and make profits, which he uses to broaden his political power. The personal representation of the clan’s interests in politics by a chieftain, or members of the core, is common in Russia and Ukraine, but with different frequency.

The systems of patronage in Russia and Ukraine are divergent. While the Russian governmental structures could be described as corrupt, in Ukraine they were more oligarchic (Aslund 2005). During Kuchma’s era in Ukraine several businessmen from different oligarchic clans became prime minister or chiefs of the presidential administration, whilst in Russia, the short-term appointments of businessmen, such as Vladimir Potanin and Boris Berezovsky, to senior government posts were exceptions, rather than the rule. The Russian clans preferred to buy services from an appropriate bureaucrat *via* means of corruption and fraud.

#### b) Scope of influence

The establishment of the financial empires of both the Ukrainian and Russian clans followed a similar historical path. During the early years of transition and under the presidencies of Leonid Kravchuk and Yel’tsin, the clans started to accumulate wealth. With gains from illegal trade or financial speculation, oligarchs bought profitable enterprises during privatisation. State officials had supplied them with information about the financial situations and the productive capacities of certain enterprises and ensured the oligarchs of an advantageous and privileged position during the privatisation auction. Consequently, the oligarch’s capital was concentrated on the most profitable sectors, i.e. gas and oil, metallurgy, machinery and food. Due to the dissemination of the clans’ properties across different sectors, the separation between them is not just upon industrial lines, as clans tended to cover all economic activities in a particular region.

The increasing number of clans, especially in Russia, complicates the classification of clans on a regional dimension, as the same regional origin does not stop competitiveness between newly created clans. Wars between clans have become commonplace. In addition, further diffusion diminished the power of a single clan’s influence in the political game, at the national level. In comparing the elite constellation in both Ukraine and Russia, Vladimir Gel’man (2008) admits that the extreme localism of the Russian clans, where only a few clans are able to exert decisive influence in national state power and any potential for building coalitions amongst regional clans is damaged by problems of ‘collective action’. At the same time, due to Ukraine’s smaller dimensions, the regional clans are in power as ‘veto players’ in the national decision-making process, but remain extremely fragmented.

#### c) Channels into politics

In the political framework of a ‘defective’ democracy, oligarchic clans can, in principle, capture the state through the executive, the legislative or juridical branches.<sup>\*\*\*\*\*</sup> In

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<sup>§§§§</sup> The patronage relationship between Pavlo Lazarenko, the former prime minister of Ukraine, and Yulia Tymoshenko, the former president of the United Energy Systems of Ukraine, ensured that this company had the monopoly of Ukraine’s gas market.

<sup>\*\*\*\*\*</sup> The juridical could not be regarded as an independent branch of state power, so long as it was strongly influenced by the executive.

the early years of transition, the Russian and Ukrainian clans concentrated their attention on building up connections with the executive. They secured their enterprises by contacts with the president, the presidential administration and the government, as a direct connection to the president was of the highest value. Leonid Kuchma, Boris Yel'tsin and Putin all tried to keep up the appearance of legitimacy in order to be elected. The oligarchic clans, therefore, had the task of supporting election campaigns with financial resources and media propaganda. In return for such services, the presidents appointed the representatives of regional clans to the national state authorities, where these representatives could favour their enterprises. The position of a presidential adviser was especially valuable to the symbiotic relationship between the president and the oligarchs.<sup>†††††</sup> In the early 1990s, the Ukrainian and Russian clans had devoted little attention to government posts, as they preferred to buy services from the relevant officials.

In the late 1990s, the connections with parliamentary representatives or, preferably, a personal representative in parliament, became increasingly important. Some oligarchs founded or captured political parties, became their members, or simply bought slots on party lists. Others used one-man constituencies of a mixed majoritarian and proportional representation system. The oligarchs became independent from national politics and transformed themselves into state actors, translating their interests into public policy and passing 'made-for-oligarch' laws. In addition, they received full personal immunity throughout their term in office, thus helping them to avoid criminal liability. Therefore, oligarchs could secure their illegally obtained properties with the legal privileges afforded them and avoid persecution or punishment by the tax administration. As a result, the oligarchic clans expanded their political and economic influence. The Ukrainian oligarchs, in particular, appreciated parliamentary seats, because the Ukrainian legislature (*Verchovna Rada*) was the influential player in Ukraine's politics (Whitmore 2004). Although the Ukrainian presidents possessed more resources than lawmakers, they preferred to bargain with parliamentary representatives in 'cartel-like deals' (Gel'man 2008, p. 11). Hence, Kravchuk and Kuchma escaped direct confrontation with the parliament, as their own performances, as well as popularity and support with the population, were low. In contrast to the Ukrainian clans, their Russian counterparts were interested in networking with the Supreme Soviet (*Duma*), the Russian legislature, whilst at the same time attaching less importance to it. This depreciation in the value of these connections was rooted in the earlier experience of 1993, when the parliament was shot at by tanks and suffered defeat in the conflict with Yel'tsin.

Paralleling this increase in power, in the political and economic sphere, was a marked increase in the utilisation of the courts, the judiciary branch of power, as laws evolved. The courts were corrupt and, as a result, costly as they demanded bribes (Kaufmann and Siegelbaum 1996; Hendley et al. 1997). However, as the judiciary, in both countries, was under the control of the executive authorities, the oligarchic clans ceased to view it as a separate state entity, instead they intended to gain influence within the courts either through their connections in the executive, or by means of bribes.

While Russian oligarchic clans implement their interest in national politics, thereby co-operating with the executive, the Ukrainian oligarchic clans are not limited by having to co-operate with the executive. As members of the still influential Ukrainian parliament they are national state players and therefore formally independent from the executive.

#### d) Levels of internal and inter-clan trust

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<sup>†††††</sup> In Ukraine, the position of a presidential adviser was held for a long time by oligarchs, i.e. Vadym Volkov and Oleksandr Rabynovich. The career of businessman Andriy Derkach also demonstrates an appropriate example as, in 1996, he was appointed to the position of presidential advisor on foreign trade, then two years later he became the chief of Kuchma's election team.

The interactions within and among oligarchic clans are regulated by informal rules and norms, originally coming from *blat*, practices in the centrally planned ‘economies of favours’, where friends and acquaintances were bound together in an intricate weave of favours and counter-favours, thereby facilitating access to commodities or services in short supply (Ledeneva 1998, 2003). In conditions of shortages and by a system of state privileges, *blat* secured access to public resources through private channels and catered to the needs of personal consumption.<sup>††††</sup> During transition, *blat* essentially replaced the authority of law, by providing the basis for both corruption and regulated informal networks, within politics and the economy. The presence of these rules does not exclude the rivalry that exists amongst oligarchic clans. As their business interests are concentrated upon the most profitable spheres of the Ukrainian and Russian economies, clans are often in competition with each other.

The degree of inter-clan trust was different, in that there was an expectation amongst rule adhering clans, that others clan could potentially take opportunistic action, thus breaking ‘rules of the game’ when it suited them. Unlike the Russian clans, the Ukrainian ones are characterised not only by inter-clan competition, but also by high internal rivalry (Kosals 2006). In Ukraine’s case, clan members do not act in a particularly close and supportive way towards each other. Instead, internal rivalry has caused further divisions between new business groups, where wealthy core members have created their own clans. In Russia, even through inter-clan competition, the trust between the same-clan members was strong. The labelling of the Russian clans as a ‘brotherhood’ and single members as ‘brothers’ reveals this high degree of inter-clan trust. The level of trust, both inside and among clans, determines the ability of clans to carry out joint actions, like the choosing of a candidate to play the arbitrary role of the state ruler.

Even to date, the political systems of both countries remain influenced by oligarchic clans. Ukraine is dominated by a multi-clan system, which results in the fragmentation of power. Regional clans possess veto rights up to the national level. However, no single clan is able to monopolise the state and force other clans to co-operate or compromise, both amongst themselves, or with the state ruler. The characteristics of the Ukrainian clans provide a plausible explanation for the negotiated transformation of Ukraine into a parliamentary-presidential republic. The high level of distrust inside and amongst business groups was the reason for their inability to agree on a single presidential successor. The strengthening of the legislature, where the regional oligarchic groups with a national scope of influence were represented, put limits on any monopolisation of state power, by any one business group, and was therefore the best way to solve the ‘successor issue’.

In Russia, it is more relevant to speak about a system where a single player, namely the state, dominates and is in the position to implement institutional change without having to negotiate with the clans. The strong state ruler’s position in power emanates from a widely supported compromise between the Russian business groups. Even if the state ruler is associated with maintaining public distance in their political governance, the business groups would still prefer to have a strong independent arbiter in the position of the state ruler, both in order to avoid continual fights with one another and also to avoid the risk of suffering defeat in the political game. The dominating ruler, as a wise leader and arbiter, maintains the current equilibrium of power and resource distribution, while looking after the interests of those clans that support ‘him’ and punishing those that seek to weaken ‘his’ rule.

### *From national to global player*

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<sup>††††</sup> *Blat* is translated as ‘acquaintances and connections’. Despite the fact that it was provided at the public expense, *blat* was seen, in Soviet society, as a positive phenomenon.

Oligarchic preferences have changed over time. At the beginning of transition, policy recommendations, regarding the transition towards democracy and a market economy, were alien concepts to the Ukrainian and Russian oligarchic clans as they were only interested in the implementation of those reforms, which could provide them with personal benefits. As a result, only partial reforms were implemented (Hellman 1998). In the late 1990s, the situation changed. As a reaction to the financial crisis of 1998, the comprehensive macroeconomic reforms on fiscal stabilisation, price liberalisation and privatisation were successfully implemented in both countries. Furthermore, due to favourable conditions within the national and international markets, i.e. high oil, gas and steel prices, both Ukraine and Russia experienced rapid economic growth. In contrast, changes in the political sphere moved in a different direction. While Kuchma was still following the strategy of 'divide and rule', i.e. recruiting members of rival clans to governmental posts of similar authority and maintaining the rivalry between state bodies, his counterpart in Russia had reasserted the power of central government, strengthened the 'vertical of state power' and created a 'dictatorship of law'. Furthermore, the reactions of the oligarchic clans to such policies were different. While the reforms of Putin found wide spread support among the Russian oligarchic clans, as well as the Russian population, the activities of Kuchma in Ukraine encountered rising resistance within all levels of society. Also, dissatisfaction can be shown in the fact that the Ukrainian oligarchic clans had directly or indirectly supported the Orange Revolution.<sup>§§§§§</sup>

The enigmatic interests of the oligarchic clans in reforms could be explained by theories of a rent-seeking society. With reference to Mancur Olson's approach (2000), the aspiration for reforms could be explained by arguing that the oligarchic clans, in both Ukraine and Russia, are transforming themselves from 'roving' to 'stationary bandits'. 'Roving bandits' are rulers that have short-term horizons, are interested in quick personal gain and stealing as much as they can. The availability of short-term rents, like non-renewable resources, provides the basis for the rent-seeking strategy of 'roving bandits'. 'Stationary bandits' are already rich enough and therefore begin to care about the prosperity of their citizens. They have long-term horizons and concentrate on profit-seeking. 'Roving bandits' can transform into 'stationary ones', if they reach the limits of their capacities to accumulate and control wealth. The absence of short-term rents accelerates this transformation. Other researchers also confirm the possibility of 'pro-democratic' reforms in a rent-seeking society. Aaron Tornell (1998) considers a 'reform from within' as a consequence of the anticipation of the crisis, when rent-seekers themselves restrain rent-seeking. Dixit, Grossman and Helpman (1997) show how a 'captured government' still retains the ability to undertake reform and act as a 'common agent', of the numerous rent-seeking groups, in the situation where rent-seekers try to solve a 'prisoners' dilemma'. However, what is not shown is the momentum of such a 'change from within' a rent-seeking society.

According to these theories, this paper presumes that the Ukrainian and Russian business groups broadened their respective short-term horizons by switching from a strategy of wealth accumulation, to one of wealth protection. A longer-term horizon effectively replaced the short-term one that was involved with rent-seeking, accumulation of new profitable assets, lobbying state bodies and the elimination of rivals. In the long-term perspective, clans began to strive, not only for rent and wealth accumulation, but also in terms of profit making, securing their capital, and sustaining the growth of their companies and society in general.

The current trends of both economic and political development in Ukraine and Russia are in line with these theories. Due to rapid economic growth, since the end of the 1990s, most oligarchs have at least doubled their wealth. The *Wprost Rating of the Richest Europeans* of 2006 includes 48 Russians and 15 Ukrainians, with respective fortunes as great

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<sup>§§§§§</sup> '5 channel' (*5 kanal*) and the broadcasting company *Era* were both loyal to the Orange forces media and were owned by the Ukrainian oligarchs.

as \$19,500 million and \$7,200 million. By comparison, in 2002, only 10 Russians and 3 Ukrainians were listed among the richest Europeans, with respective fortunes of up to \$3,700 million and \$1,700 million. However, these developments may not only be the result of economic growth. They may also be due to the transfer of capital from the shadow economy into the official economy. By 2000, several of the major oligarchs had become completely legal and legitimate, paying taxes, declaring their assets and spending substantial amounts on charity.

**Table 1. The Wealth of Russian and Ukrainian Oligarchs, 2002-2007**  
Source: *Lista 100 Najbogatszych Europy, Wprost*; own calculations.

Whether the oligarchs have reached the limits of wealth accumulation and have now crossed over to its protection is difficult to identify, as the amount of wealth necessary to ignite such a switch of strategy is not quantitatively defined. However, it is possible to identify the changes in the sources and terms of capital accumulation. Thus, a deeper look at the driving forces behind current economic growth and sources of economic rents in both countries is necessary. In the context of this paper, it is important to state that the explanatory power of rents depends upon the type of rents. Even in the case of resource rents, the availability of rents from the exploitation of oil, gas and mining creates different incentives, compared to the exploitation of renewable resources like forests and agriculture, or low value-added goods like steel and iron.

As both Ukraine and Russia have achieved strong economic growth towards the end of the 1990s, the issue of how sustainable this growth has become is now crucial. Figure 1 (below) reveals the drivers of growth from the demand side, showing the contributions of final use components to GDP growth. Figure 2 (below) analyses the value added by economic sectors. \*\*\*\*\* As is clear from Figure 1, the drivers of growth have changed from year to year. However, three different phases of growth can be distinguished.

Some evidence of output recovery appeared in late 1997 in Ukraine and in early 1998 in Russia, but this fell away quickly during the financial crisis of 1998. After the crisis, economic performance was mainly driven by the increased competitiveness of Ukrainian and Russian goods, due to the devaluation of the *hryvnia* and the *rubel*. An ensuing reduction of real wages and a huge cut in real social spending led to a significant drop in real household incomes. Rising poverty forced consumers to buy cheaper domestic goods, as the prices of imported goods rapidly increased. However, these negative tendencies had a positive effect on the domestic private sector, which, due to huge domestic demand, started to recover and make profits. According to Figure 2, industry played the driving role in the recent recovery, since 1999, followed by the services sector. Industrial production began to recover, especially in those non-resource sectors that supplied goods to domestic markets. The fall in real wages and cheap domestic resources decreased input costs and made Russian and Ukrainian industries competitive on the world market, too. Additionally, liberalisation and privatisation reforms allowed private enterprises to use the opportunities provided by the currency devaluation. Therefore, in that initial period from 1999 to 2001, the economic recovery in both countries was not solely resource-dependent.

Between 2000-2004, the inflation rates in both countries gradually declined. Russia experienced an oil extraction boom and Ukraine benefited from the strong international demand on metal products. Additionally, the export prices for energy resources and metal products were extremely high. Thus, while the positive effects of the devaluation gradually

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\*\*\*\*\* The output data in Russia and Ukraine presents a distorted picture of the economy. Due to transfer pricing, a large scale of GDP generated by natural resources and metallurgy sectors, is not reflected in the accounts of the extraction and producing companies, but in the trading ones. As a result, export-oriented industries are underestimated, while trade is over-estimated in the Ukrainian and Russian national accounts.

faded, oil and gas in Russia, and the metallurgy sector in Ukraine, became the main drivers of growth in that period.

In 2004, the growth of GDP, driven by energy and metal production began to decline in both Ukraine and Russia, while domestic consumption booms were rapidly driving their respective economies. At the same time, the role of domestic production in satisfying domestic demand largely decreased, thus creating room for imported goods. Although rapid import growth gives the impression that exports had decreased, economic growth in 2002-2004 would have been minimal without the strong exports of natural resources in Russia and metallurgy in Ukraine. The other positive effects were brought about by the simplified tax schemes (flat tax) for small firms, which pushed them from the shadow economy into the official one.

Figure 1. GDP growth by demand components in Ukraine and Russia, 1990-2004  
Source: World Development Indicators, World Bank; own calculations.

Figure 2. GDP growth by sectors in Ukraine and Russia, 1998-2004  
Source: World Development Indicators, World Bank; own calculations.

Similar to the sources of economic recovery, the sources of rents changed over time. Figure 3 shows the dynamic availability of national and international sources of rents, as well as the dynamic rent opportunities and barriers in Ukraine and Russia. In the early 1990s, fuel and metal product exports were the most attractive sources of rents. Hyperinflation, along with higher positions in the informal political networks, brought in huge monopolistic and arbitrage revenues (Pritzel 2002). In resource-poor Ukraine, though on short-term basis, the oligarchs stood to benefit from the imported and then immediately exported, gas and oil from Russia. In the mid 1990s, the rents stemming from hyperinflation disappeared, but the clans in both countries continued to benefit from the political patronage that supplied them with indirect subsidies, special treatment and tax incentives (van Zon 2002). During that time, the international community was more concerned with the political stability of those FSU countries possessing nuclear weapons, then with their progress on reform. Overall, during the initial transition years, the impact of the domestic dimension on rent revenues and rent opportunities was more important than international one. The international dimension did not begin to play a crucial role in the extraction of rents, until after the financial crisis of 1998. For the period after that crisis, this paper gives a detailed illustration of rent opportunities (see overleaf).

Figure 3. Changes in Domestic and International Sources of Rents and Rent-Seeking Opportunities, or Barriers in Ukraine and Russia

Notes: 'bold' script reveals the new sources of rent, 'grey' script depicts the disappearance of some sources of rents and 'normal' script shows the persistence of the source.

Source: Aslund (2002); Prizel (2002); Zimmer (2006); own illustration.

Despite rapid economic growth since 1998-1999 and large revenues from exports, the oligarchic clans have met with obstacles to their businesses that need to be overcome, if they are to drive on the sustainability of economic recovery. Oligarchic capital is mostly concentrated in export-oriented branches. Typically, the Russian oligarchs are preoccupied with gas, oil and metals, while the larger Ukrainian oligarchic groups tend to concentrate on steel and iron. Until 2000, the oligarchs made their money mostly from the commodity trade,

predominantly trading with gas, oil and metal products.<sup>†††††</sup> Other sources of revenue were subsidised state credits, coal subsidies and agricultural and chemical exports (Aslund 2000).

The current growth is extensive with exports of intermediary, semi-finished and low-quality goods. The efficiency of the basic exporting industries is low, while the energy wastage is high. At the same time, Russia's oil and gas fields and transport systems, as well as Ukraine's metallurgy industry, are becoming old and out of date. The use of new technologies and the modernisation of production capacities are important, in terms of competitiveness within the world markets. As the state is not able to provide financial aid to local corporations, private investment, either local or foreign, is required. However, investment will not happen, until the possibility of reaping rewards from the investment is secured.

The necessity for investment is an even greater challenge for Ukraine, as metal products are more vulnerable than oil and gas. In 2004, Ukraine's steel industry reached one of its highest levels of capacity utilisation, 95,4%, up from 52,1% in 1998. The replacement of outdated production equipment and machinery and the increase of their efficiency are the current goals of the Ukrainian oligarchic clans, whose assets are concentrated mostly in metallurgy. This challenge is exacerbated by a forecasted fall in prices for metal products after 2008, rising prices of imported Russian energy and higher transport costs. Not surprisingly, the investment rates in the steel sector grew in 2004 by 43% and in 2005 by 56%.<sup>†††††</sup> Nevertheless, Ukrainian metallurgy attracts less investment than the Russian steel, oil and gas industries, as Ukraine's metallurgical exports are permanently under antidumping investigations.<sup>§§§§§</sup> To escape high antidumping fines and discriminatory attitudes, the Ukrainian metal companies strive for market status in their individual enterprises, as well as generally for the market economy status of Ukraine. They are also expanding globally. In this way, they are trying to improve their access to international capital markets and increase the capitalisation of their assets, which would additionally lead to more financial openness, the disappearance of transfer pricing and the showing of taxable profits.<sup>\*\*\*\*\*</sup>

The other disappearing source of economic rent for the Ukrainian clans stemmed from imports of oil and gas from Russia and other energy rich FSU countries. Although the gas and oil revenues made the Ukrainian business groups rich, this source of rent gradually disappeared. In Soviet times, Russia subsidised Ukraine by supplying around 50 million tons of oil and substantial amounts of gas each year, at approximately 35-40% of the world price. After the collapse of the Soviet Union, Russia and other energy rich CIS countries did not intend to continue subsidising the Ukrainian industry. As a result, the prices for imported energy to Ukraine increased continuously, but were still below world price levels.<sup>†††††</sup> Due to the state's inability to pay, and the Ukrainian business groups' unwilling to pay, the Ukrainian government ran up considerable debts. Russia, however, continued exporting, often through bartered or delayed payments. On the one hand, Russia was forced to continue supplying energy because of the necessity of securing access for its pipelines to Western Europe.<sup>†††††</sup> On the other hand, it blackmailed the Ukrainian government, using energy

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<sup>†††††</sup> One of the gas oligarchs, Ihor Bakai, famously stated in an interview in 1998, "All really rich people in Ukraine have made their money on gas" (Tymoshenko, V. (1998) 'Vse bogatye lyudi Ukrainy zarabotali svoi kapitaly na rossiiskom gaze' ('All Rich People in Ukraine Made Their Money on Russian Gas'), *Nezavisimaya gazeta*, 16 October.

<sup>†††††</sup> Ukraine's Cabinet Resolution, 'On the State Programme for Developing and Reforming mining and metalworking, for the period to 2011', Kyiv, 2004, July 28.

<sup>§§§§§</sup> From 1993 to 2001, there were 43 anti-dumping cases (Eremenko and Lisenkova 2004).

<sup>\*\*\*\*\*</sup> Ukraine's metal companies own metal works, wholesalers and retail metal traders in Europe.

<sup>†††††</sup> The end prices were also lower than the world prices due to the inclusion of compensation for transit charges in the payment for energy resources.

<sup>†††††</sup> Russia inherited an inflexible infrastructure for energy transportation from the Soviet period. The *Druzhba* oil and *Soyuz* gas pipelines, passing through Ukraine on their way to Central and Western Europe, were

supplies as a form of political pressure, so that it could base the Russian Black Sea fleet in Sevastopol and attempt to get shares in the Ukrainian oil and gas infrastructure through a debt-for-equity scheme. §§§§§§§§

In such a disastrous situation of energy dependency and growing debts, the Ukrainian oligarchic clans amassed gigantic profits, by illegally tapping the pipelines and re-exporting the energy to European countries under the world market price. \*\*\*\*\* The gains from energy re-export and trade with energy-intensive commodities in the 1990s helped their recipients to strengthen their influence over the state authorities and the reform process in Ukraine. In the early 1990s, the Ukrainian government was liable for the payment of the oil and gas debts for the energy imports. Only in 1995 did the government reject continued responsibility for the debts, incurred by private companies, although it still regulated imports and the distribution of energy on the national market. The government allocated import quotes, as well as consumers on the national market, among private companies. In these circumstances, the opaque and corrupt state regulations of the energy industry were of benefit to the oligarchic clans. Despite the huge debts of Ukrainian energy consumers, the oligarchic companies also earned their money on the national market. They could influence the division of national consumers and so supplied the only reliable clients who were able to pay. Having captured the state authorities, a few of the oligarchic companies were able to influence the allocation of consumers and monopolise the market on energy imports. †††††††† Moreover, the oligarchic clans then increased their profits, as they paid their suppliers from Russia and Turkmenistan even less than they received from their Ukrainian consumers.

However, the limits of such economic rents in Ukraine became more and more evident. Even before the Orange Revolution, the relationship between Ukraine and Russia was marked by energy conflicts. Russia insisted on the re-payment of debts and stolen gas, as well as an increase of energy prices up to world price level. Russia had many reasons to change its previous subsidising policy. First, despite huge profits from supplying energy to the international market, it sustained losses trading with its 'near neighbours'. In the face of insufficient investment capital for improving and expanding the Russian oil and gas production and pipeline system, the eradication of such losses was of paramount importance for the Russian government and oligarchic clans. Second, Russia was demanding a price increase, in line with the free market economic policies of government, due to its desire to join the World Trade Organisation (WTO), which made an increase in gas prices to the world market level a condition of membership and regarded any special prices as a violation of the principles of competitiveness.

The turnaround of possibilities for economic rents is obvious in the latest developments within the gas market. According to the agreements, signed in early 2004, Ukraine covered its energy debts to *Gazprom* by way of Eurobonds and transit charges for Russian gas, up to 2009. For the Ukrainian oligarchic companies, this meant that since 2005, no gas has been supplied to cover the transit fee. †††††††† At the same time, *Gazprom* revealed

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the only pipelines enabling Russian gas exports. These pipelines deliver more than 80% of Russian gas imports to Europe (Balmaceda, 1998).

§§§§§§§§ Rosaria Puglisi (2003, p.839) estimates that within the short span of six months in 2000, Russian concerns took over 50% of the Ukrainian petroleum market and Russian oil traders now control the supply of oil to Ukrainian refineries.

\*\*\*\*\* In early 2000, quantities of gas, valued at \$1 billion, were illegally siphoned by Ukraine. The Ukrainian government confessed to this accusation, but never defined the exact amount. *NIS Observed*, 23 August 2000.

†††††††† Four Ukrainian company 'monopolists' were Intergas, Itera-Ukraina, the United Energy Systems of Ukraine and Naftogas.

†††††††† A copy of the agreement was published in *Ukrainskaya Pravda*, January 5, 2006, available at: <http://www2.pravda.com.ua/ru/news/2006/1/5/36448.htm>, accessed 18 January 2008.

its intention to set gas prices to world levels.<sup>§§§§§§§§</sup> Therefore, the possibility of obtaining rents from cheap Russian energy imports disappeared. Additionally, the importance of two pipelines going through Ukraine, a 'high-value card' in the bargaining position of Ukraine *vis-à-vis* Russia, diminished; since 1999 the Yamal-pipeline began to transport Russian gas across Belarus and Poland. The loss of geopolitical advantage for Ukraine, in relation to energy transit, will be intensified by the pipeline running through the Baltic Sea, which will connect Russia directly to Germany and is due to be completed by 2010.

An additional source of rent in both countries was financial aid from international lending organisations like the International Monetary Fund and the World Bank.<sup>\*\*\*\*\*</sup> In the early 90s, Ukraine and Russia received financial aid under 'soft' conditions. As the creditors lost their trust, after the crisis, the financing of the budget deficits through external borrowing became more difficult. The IMF revised its 'soft' crediting policy. To be able to borrow, Ukraine and Russia had to commit to market reforms. In such a way, the external shock, following the crisis of 1998, translated into successful economic and political reforms in these rent-seeking countries. At the request of the IMF and trying to avoid a full-fledged financial default, the Ukrainian and Russian governments undertook some market reforms and cancelled soft budget constraints. Thus, the most conservative part of the Ukrainian and Russian elite, the 'red directors', lost their rents through subsidies and donations, and left the stage of the political theatre behind them.

These changes happened not just at the national level, but at the company/corporate level too. After the economic crisis of 1998, requirements for good corporate governance and transparency became essential in conducting business. The case studies on the Russian and Ukrainian oil and gas sectors confirm the ongoing implementation of corporate governance norms, as the business and ownership structure became more transparent, international bookkeeping norms were launched, and companies and corporations began to develop long-term strategies (Heinrich 2004, 2005; Zheka 2006). Transparency and international norms in doing business also meant that illegal 'shadow' resources, which helped to ensure financial capital and market benefits by means of state capture or corruption, were scaled back.

Overall, globalisation can be treated as an exogenous force, limiting the sources of rents and challenging the major oligarchic clans in Ukraine and Russia to modernise. In both countries, the oligarchic clans, whose businesses became more internationalised, were required to implement the international standards of transparency and corporate governance. It appears that Ukrainian clans experienced the impact of these requirements more deeply. As the sources of their economic rents diminished, or were limited to a greater extent, than those in Russia, the need to implement these standards became paramount if they were to conduct business within the international markets.

Because of the exposure to competitiveness from international markets, they are modernising their energy-intensive companies, especially in the energy, metallurgical and chemical sectors. The modernisation, however, requires large financial investments, which in turn depends upon political stability.

### *Striving for Sustainability and an Arbiter*

In the late 1990s, a decline in the sources of rents, combined with the existing high costs of informal networks and the changes to the trading rules in doing business in the international markets, led to the favouring of stable formal institutions and the enforcement of property rights. Informal networks cannot secure the oligarchs' accumulated wealth, as they are unstable and costly. Formal institutions can secure property rights and encourage a

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<sup>§§§§§§§§</sup> After the 2006 crisis, *Gazprom* sold gas to Ukraine, via its jointly owned company RosUkrEnergo, at a price of \$230/mcm. (*Russia Morning Comment (UFG)* 11 August 2004; Stern (2006).

<sup>\*\*\*\*\*</sup> The IMF provided the conditioned loan within the Systemic Transformation Facility.

sustainable growth in the best way. Moreover, sound corporate governance requires sound political governance (Oman et al. 2003). The rating of a single company on the financial markets could not be higher than the rating of the whole country. Hence, transparency of a single business, in a country with a 'patronage regime' (Hall 2005) makes this business vulnerable to rival attacks. Therefore, the Ukrainian and Russian oligarchic clans began to demand good formal institutions that could secure their wealth, despite rotating people within state authorities. The state ruler, who is formally in the position to change and implement formal institutions, thereby acting as an independent arbiter, accordingly began to play the central role.

A good government that enforces order and guarantees reliable institutions, in the form of political stability, protection of property rights and business contracts, has become the essential requirement for private business empires and countries in general. The quality of its institutions affects both a country, as well as an individual company's ability to achieve sustainable growth and be successful in its long-term development. Figure 4 shows the positive development of institutions, in both Russia and Ukraine, since 2000. Separate analysis of three institutional dimensions, reveals different rates of progress in the political, economic-administrative and legal institutions of Ukraine and Russia. The development of political institutions in Ukraine and Russia was more advanced during early transition. Taking into account the fast transition from socialism to democracy, with the consequent change of formal rules and laws (although their actual implementation lagged behind the constitutional changes), such differences in institutional dimensions seem to be quite plausible. The influence of informal rules impedes the implementation of newly established formal rules, a fact that becomes evident in the estimation of economic-administrative and legal institutions. The improvements in institution building, in the ensuing years, were done, in the first instance, in the economic-administrative and legal dimensions. This trend was even stronger in Russia than in Ukraine.<sup>+++++</sup> However, Ukraine radically improved the quality of its institutions, as a result of its structural changes, following the Orange Revolution. These developments indicate that FSU-style institution building may be different to what might be expected, in relation to the western concept of good governance.

**Figure 4. Progress in institution building in Ukraine and Russia, 1996-2004**  
**Source: World Bank Governance Indicators; own calculations.**

A central role is usually assigned to the institution of property rights when analysing rates of progress in FSU countries.<sup>+++++</sup> In the early stages of transition, the security of property rights and the rule of law had little appeal to the Ukrainian and Russian oligarchic clans. On the contrary, weak property rights gave them the opportunities to define those enterprises that were to be privatised and to buy new assets in the privatisation auctions. Even after privatisation, the oligarchs neglected the rule of law and refused to make dividend payments to small shareholders and workers. This disappointing state of affairs led to small shareholders selling madly and at low prices, thus enabling oligarchic clans to become major shareholders in enterprises at prices far below what these shares were actually worth.

In the era of the presidents' Kuchma and Yel'tsin, property rights were secured with informal rules, negotiated within the informal networks that existed between the political sphere and the private sector. These informal rules abided by the following idea: that the

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<sup>+++++</sup> In Russia, economic-administrative institutions are better developed than political institutions. However, political indicators take democratic institutions as an instance of good governance. Thus, the quality of political institutions is rated to be poor in countries with authoritarian regimes.

<sup>+++++</sup> Economic historians assume that differences in the enforcement of property rights explain inequalities in economic performance across the country (North 1981; Wintrobe 1998; Braguinsky and Yavlinsky 2000; Svenjar 2002).

‘security of a financial empire depended upon the position of your patron within state bodies’. In Russia and Ukraine, the protection of property rights became a rare privilege; indeed one could almost term them as a commodity, utilised by political leaders as a reward for their most active supporters.

Such a strategy, based upon patronage protection, was extremely short sighted. If a political patron loses power, the financial empire of the oligarchic clan runs the risk of ‘going under’. As oligarchs accumulated their wealth illegally, they could not claim the protection of formal laws, which were often both dubious and contradictory. The oligarchs were vulnerable to state prosecution, whereby legislation could be selectively enforced in order to act in the interests of a rival business group.<sup>§§§§§§§§</sup> Even the same clan’s origins could not guarantee further prosperity, or the security of property rights, with regards to the oligarchic accumulated capital.<sup>\*\*\*\*\*</sup> Additionally, maintaining patronage networks was very costly.<sup>†††††††††</sup> The economic prosperity of the oligarchic clans depended upon their ability to insure themselves against political risk. The customary way of ensuring capital was to deposit it in foreign bank accounts.<sup>†††††††††</sup> However, due to the huge demand for investment, these options became inappropriate.

With the enlargement of their business empires, the necessity for protected property rights became the central concern. Anatoly Chubais (Steen 2003, p.93) complains that Russian businessmen ‘steal absolutely everything during raw capitalism’. However, he remains optimistic about this situation, arguing that, ‘they become owners and decent administrators of this property’.

The Global Competitiveness Report shows a similar tension to the one evident from the World Bank Governance Indicators. From 2003 to 2005, Russia leads the way in the security of property rights (Figure 5). As argued by Braguinsky and Myerson (2007), promises to exchange protection for political support are credible only among individuals who have reputations for honouring such agreements. For example, Putin’s reputation for honouring political support pacts reduces the negative view of political risk, whilst Kuchma’s strategy, on permanent policy changes and people rotation, increases the perception of risk.

**Figure 5. Security of Property Rights in Ukraine and Russia, 2000-2007**  
**Source: The Global Competitiveness Report**

The political systems of both Russia and Ukraine still belong to so called ‘hybrid’ regimes, stuck in the ‘grey zone’ between democracy and authoritarianism. The diversity of terms used to describe these ‘hybrid’ regimes in the FSU, i.e. ‘imitated’, ‘façade’ and ‘pseudo’, reveal the limitations of categorising these political regimes according to their democratic and authoritarian features. Rather, what distinguishes these countries is the presence of an arbiter, a dominating state ‘actor’, who is able to monopolise state power without having to negotiate with others and has the authority to close ‘structural holes’ (Burt 1998) within authorities and establish balance and stability, in the distribution of power and

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<sup>§§§§§§§§</sup> Kuchma, as well as Putin, used state tax administration as a separate government agency in order to exercise their personal powers, while punishing opponents and benefiting supporters.

<sup>\*\*\*\*\*</sup> Preliminary results of the case study on Russian oligarchs (Braguinsky and Myerson 2007) indicate that out of the 302 oligarchs in the 1990s original sample, by 2005, at least 111 had lost ownership of all their assets.

<sup>†††††††††</sup> Pavlo Lazarenko, the Premier Minister of Ukraine, received in 1996-1997, around \$72 million in bribe money for special benefits in the Ukrainian gas market, from the United Energy System of Ukraine, the company headed by Yulia Tymoshenko (*Financial Times*, 6 June 2000).

<sup>†††††††††</sup> The Central Bank of Russia estimates the capital flight in Russia in 1994-1999 as \$136,3 billion. In 2002, this number decreased to \$10,4 billion. *Obzor rkonomiceskikh pokazatelej*, 15.01.2002, available at: <http://www.eeg.ru>, accessed 18 January 2008); *Russian Economic Trends Monthly Update (RECEP)*, October 2002, Table 10.

resources, between oligarchic clans. The presence of such a state arbitrator is also fundamental for sustainable economic growth. Paul Hare (2007) regards the state, which has a monopoly over the means of enforcing order, as being more able to protect property rights and business contracts, carry out the levy of taxation and manage the public budget. Thomas Carothers (2002), on the other hand, describes a political system without a dominating actor, which he refers to as 'feckless pluralism'. Here, a significant amount of political freedom is combined with free-floating power that is dispersed between different political groups. In such circumstances, the state remains a weak actor. Ronald Burt (1998) argues that political systems of 'feckless pluralism' are characterised by 'structural holes' within state bodies, which can be used by other actors to secure their own benefits. Carothers' ideas correspond with the situation in Ukraine. The syndrome of 'feckless pluralism' was visible during the Kuchma era. Hare's description, of a state that has a monopoly on enforcing order, is demonstrated by the situation in Russia, during the era of Putin. Although, in the early years of transition, both countries suffered from 'structural holes', Putin's state authority succeeded in closing them.

This article will now examine in depth Ukraine's own 'feckless pluralism'. Kuchma's policies in Ukraine were seen as highly corrupt, clan-dominated and non-beneficial to society. Kuchma's 'divide and rule' strategy involved a permanent rotation of handpicked individuals in state authorities. Additionally, he appointed representatives of rival oligarchic clans to similar powerful positions within office.<sup>§§§§§§§§§§</sup> In this way, he prevented the growth of any potential internal opposition to his authority. However, the regular rotation of individuals, able to protect or damage one's oligarchic preferences, also meant high instability and insecurity in accumulated properties, thereby creating fewer incentives for investors. Kuchma's designated successor, Yanukovych, had to admit that his inability to unite all the clans was evident. Being the prime minister, in the years before the election in 2004, he benefited from his association with the *Donezk* clan. Observers do not believe (Portnikov 2004) that Yanukovych would have become an independent arbiter, ruling in the interests of all clans.<sup>\*\*\*\*\*</sup> Because of the low level of trust, both within the same clan and amongst clans, the transformation of Ukraine from a presidential to a parliamentary republic, where no force was able to monopolise state power, was the 'second best choice' for all oligarchic clans. Thus, the legislative package of the new run-off presidential election, as well as the constitutional changes, got huge support among the Ukrainian elite.

In Russia, the political system developed in a different way. The struggle for a dominating role started in the time of Yel'tsin. Then Putin successfully closed the 'structural holes' between the legislative, executive and judiciary branches, and established a political system of 'dominating power' in Russia (Gelman et al. 2000). Despite having an affiliation with only one clan, often called *siloviki*, Putin played the role of an independent arbiter, and secured the current distribution of power between oligarchic clans (Renz 2006). His all-embracing image helps to eradicate any commitment to a particular oligarchic clan. However,

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<sup>§§§§§§§§§§</sup> The Presidential Administration, established in 1991, had initially no influence on political decision-making, until President Kuchma bestowed it with governmental capabilities. The Presidential Administration, called the "shadow government", had under its control all the executive authorities. Consequently, the value of this position for the oligarchic clans increased radically. The chieftains of clans often became the heads of the Presidential Administration (for instance, Jevhenij Kusnarjov, from the *Kharkov* clan and Viktor Medvedchuk from the *Kyiv* clan). This position gave opportunities to obtain information about privatisation plans, to bargain subventions for enterprises and to benefit from credit placing and license awards. During the presidency of Kuchma, representatives of both the *Dnipropetrovsk* and *Donezk* clans held these government positions. The offices of the head of the Presidential Administration and premier minister were objects of exchange between the *Kyiv*, *Donezk* and *Dnipropetrovsk* clans.

<sup>\*\*\*\*\*</sup> Portnikov V., Vortrag im Moscow Carnegie Center, 22 December 2003, available at: <http://www.carnegie.ru/ru/pubs/media/71858.htm>, accessed 5 February 2008.

the success of Putin's reforms cannot be attributed to his personality alone. It is also due to the congruence in his reforms and the preferences of the Russian clans, who preferring not to confront each other, allowed an equidistant actor to rule in the political game.

The decision to initiate or support protests, or uprisings against a state ruler, 'a confrontation strategy', emanates from the presence of revolution-promoting conditions within a country. Here are some brief descriptions of a few of these revolution-promoting conditions.

First, a population should be dissatisfied with an incumbent ruler. The economic recovery of the previous years led to rapid growth in per capita GDP. However, it is perceived individual economic wealth that is important and not the reality. Although the standard of living was improving in both Russia and Ukraine, many Ukrainians were dissatisfied with their poor living standards. This contributed to wide dissatisfaction with Kuchma's political regime.<sup>††††††††††</sup> Additionally, from the very beginning of his presidency, Kuchma did not have the full support of the Ukrainian population. He was elected as 'the lesser of two evils', i.e. his rival was the Communist Party candidate. The trust in President Kuchma dropped abruptly after the *Gongadze* affair and the 'tape recording scandal'. In contrast, Putin was widely supported in Russia throughout his presidency (White and McAllistar 2003).

Second, a free media is required to inform citizens about election fraud and to mobilise the masses for countrywide demonstrations. In Russia, during the presidency of Yel'tsin, the oligarch's Boris Berezovsky and Vladimir Gusinsky controlled the media. President Putin has slowly expanded government ownership of and control over the media, however, so far the media remains in the hands of a few pro-Putin oligarchs. In contrast to Russia, by 2004, the opposition media still existed in Ukraine. The central government independent '5 channel' and the broadcasting company 'Era' were loyal to the Orange forces media that had broadcasted, countrywide, the news about the election fraud.

Third, the decision to confront, or co-operate with a state ruler is a rational one because the assessment of the benefits and costs dictate the strategy. The experience of previous 'defections' in the 'principal-agent' relationship probably created the perception that punishment could be avoided.<sup>††††††††††</sup> President Putin severely punished his opponents. If one of the Russian oligarchs began criticising governmental policy, his days became numbered. The Yukos-affair was the pre-eminent example of what the consequences of political opposition could result in.<sup>§§§§§§§§§§</sup> The high probability of punishment made the cost of 'defection' very high. In Ukraine, president Kuchma undertook a moderate policy and so his political opponents went unpunished. The leading forces of the Orange Revolution were based within the opposition parties of the Ukrainian parliament and were founded by oligarchic clans opposed to Kuchma. In this situation, the cost of 'defection' was minimal.

Fourth, the revolving elite require an ad-hoc event to create the spark that could ignite protests and an ensuing confrontation with the incumbent regime. Election is a point in time, when authoritarian regimes become vulnerable (Hale 2005). The threat of overthrow arises, if a ruling party is weak (Way 2005; Geddes 2006). Presidential or parliamentary elections, which were often manipulated and fraudulent in the FSU, provided just such an event. In Ukraine, the protests of 2004 were aimed at the pending election of the president and were directed primarily against election fraud. In addition, there was little support for Yanukovich, Kuchma's successor, either amongst the population, or in the parliament.

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<sup>††††††††††</sup> Survey on trust in social institutions, Central European opinion research group, Brussels, October. 2004, available at: <http://www.ceorg-europe.org/research/2004-09.pdf>, accessed 8 January 2008.

<sup>††††††††††</sup> Defection describes the attempt of the agent, oligarchic clan, to undermine the power of the principal, a state president, and go outside of the principal's control.

<sup>§§§§§§§§§§</sup> Yukos, Russia's most successful oil company, was officially accused of tax fraud. In the case of the Yukos trial, observers suspected that the Kremlin had punished Khodorkovsky, the owner of Yukos, because he might have supported several political parties, but not the established pro-Putin United Russia party. Yukos was auctioned off to pay \$27 billion in back taxes and Khodorkovsky was sent to prison.

Overall, while Putin consolidated state authority and created a system with a 'dominating power' base, thereby fulfilling new requirements for the stability of political power and the security of property rights, Kuchma pursued the 'divide and rule' strategy in a situation of 'feckless pluralism' (occasionally benefiting one clan or another) and therefore, accelerated uncertainty and instability. Unsatisfied with this policy, the Ukrainian clans used the revolution-promoting circumstances to overthrow the incumbent political ruler.

### *Conclusions*

The colour revolutions, or re-launched soft authoritarianism are the types of regime change that have a similar logic, but a different nature. They are continuous and discontinuous regime changes that implement the new preferences of the influential elite, i.e. business groups. While the Orange Revolution in Ukraine is a discontinuous regime change, 'soft' authoritarianism in Russia is a continuous one. The ways in which the new preferences are implemented depends on the differences in the characteristics of business groups, the availability or disappearance of their oligarchic rents and the degree of implementation of the dynamic business preferences into Ukraine's and Russia's state politics.

Despite similarities in the organisational structure, Ukraine and Russia had divergent systems of political patronage. While the Russian governmental structures could be described as corrupt, in Ukraine, they were more oligarchic. The Russian business groups preferred making corruption payments to state bureaucrats, more than personal representation in politics. Additionally, they devoted less importance to the legislature in Russia's political system. The neglect of these interactions in politics, *via* the legislature, reduced the business groups to the roles of non-state actors, thus accelerating their dependence to the executive. In contrast, the Ukrainian business groups were directly incorporated into the political system of Ukraine, making it oligarchic. The Ukrainian oligarchic clans were not limited to just co-operating with the executive. As members of the still influential Ukrainian parliament, they were national state players, formally independent from the executive. The differences were also in the scope of the influence. The Russian business groups have predominantly a local area of influence. In comparison, due to the smaller size of Ukraine, even local business groups were able to influence politics at the national level. The increasing number of veto-players at the national level made decision making difficult. Additionally, the huge level of internal distrust within Ukrainian business groups, as opposed to their Russian counterparts, impeded the mutual co-operation of clans, thus making an amicable agreement on Kuchma's successor, impossible to reach.

The Ukrainian and Russian business groups possess divergent sources of rents, especially, since the financial crisis of 1998. The sources of rents, in both countries, stem from international and domestic dimensions. The impact of each dimension and the sources of the rents changed over time. During the initial transition years, the impact of the domestic dimension on rent revenues and rent opportunities was more important than international one. The international dimension began to play the crucial role in the extraction of rents, only after the financial crisis of 1998. Globalisation limited the sources of rents and challenged Russia's and Ukraine's major oligarchic clans to modernise. In both countries, the oligarchic clans, whose businesses are becoming more internationalised, are required to implement international standards of transparency and corporate governance. It appears that Ukrainian clans experienced the impact of these requirements more deeply. As the sources of their economic rents diminished, or were limited to a greater extent, than those in Russia, the need to implement these standards became paramount if they were to conduct business within the international markets.

The business elite in Ukraine and Russia are striving for responsible and secure state governance, as globalisation constrains their rent-seeking possibilities and unstable informal networks fail to provide protected property rights. In the circumstances of a global economy,

the state should play the role of an arbiter, which is able to protect property rights and guarantee stability. While Putin consolidated state authority and created a system with a 'dominating power' base, thereby fulfilling new requirements relating to the stability of political power and the security of property rights, Kuchma pursued the 'divide and rule' strategy in a situation of 'feckless pluralism' and in-so-doing, accelerated uncertainty and instability, while occasionally benefiting one clan, or another. Unsatisfied with such a policy, the Ukrainian clans used the available revolution-promoting circumstances to overthrow the incumbent political ruler and transform Ukraine into a parliamentary-presidential republic with limited possibilities for the monopolisation of state power, by any one political or economic force.

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*Figures*

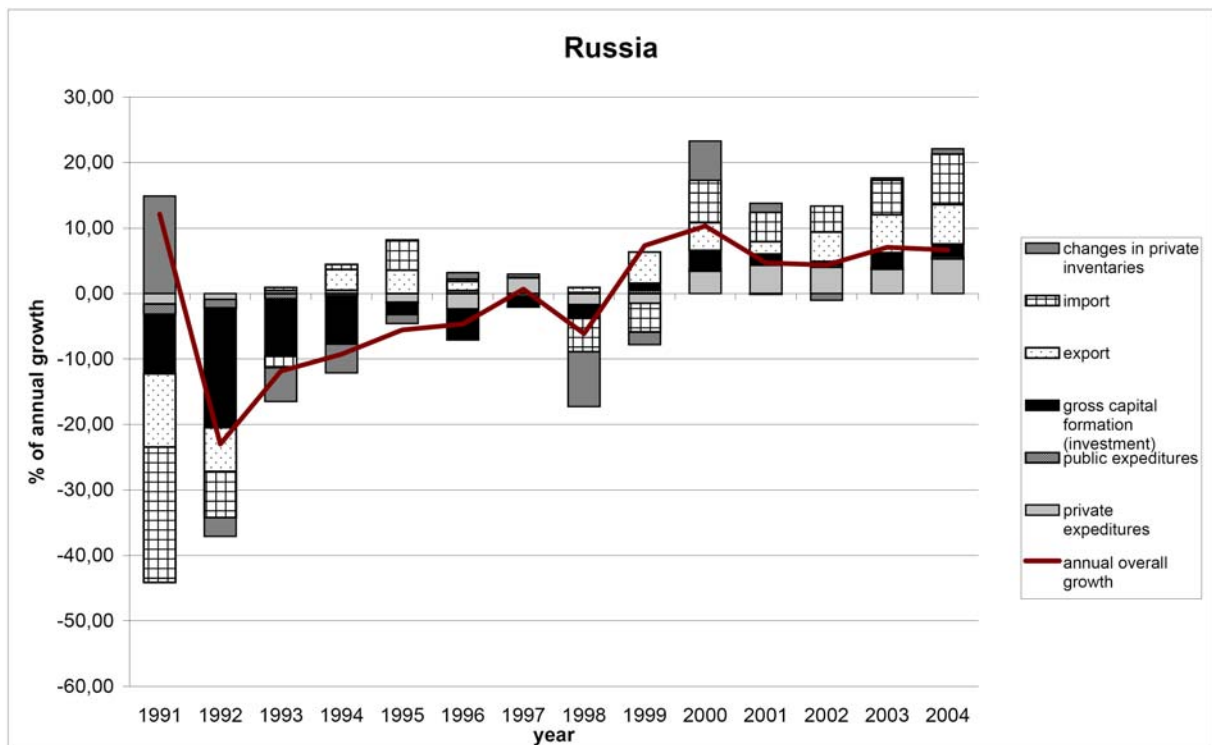
**TABLE 1**  
**THE WEALTH OF RUSSIAN AND UKRAINIAN OLIGARCHS, 2002-2007**

<i>Wprost</i>		<i>Russia</i>			<i>Ukraine</i>		
<i>Total number</i>	<i>Total number</i>	<i>Wealth, in million \$US</i>		<i>Total number</i>	<i>Wealth, in million \$US</i>		
		<i>Max</i>	<i>Min</i>		<i>Max</i>	<i>Min</i>	
2002	25	10	3 700	500	3	1 700	800
2003	50	31	8 300	550	6	1 900	400
2004	50	29	11 500	550	5	3 500	850
2005	100	55	15 000	300	7	2 800	350
2006	100	48	19 500	370	15	7 200	450
2007	100	43	30 000	550	24	18 700	650

*Source: Lista 100 Najbogatszych Europy, Wprost; own calculations.*

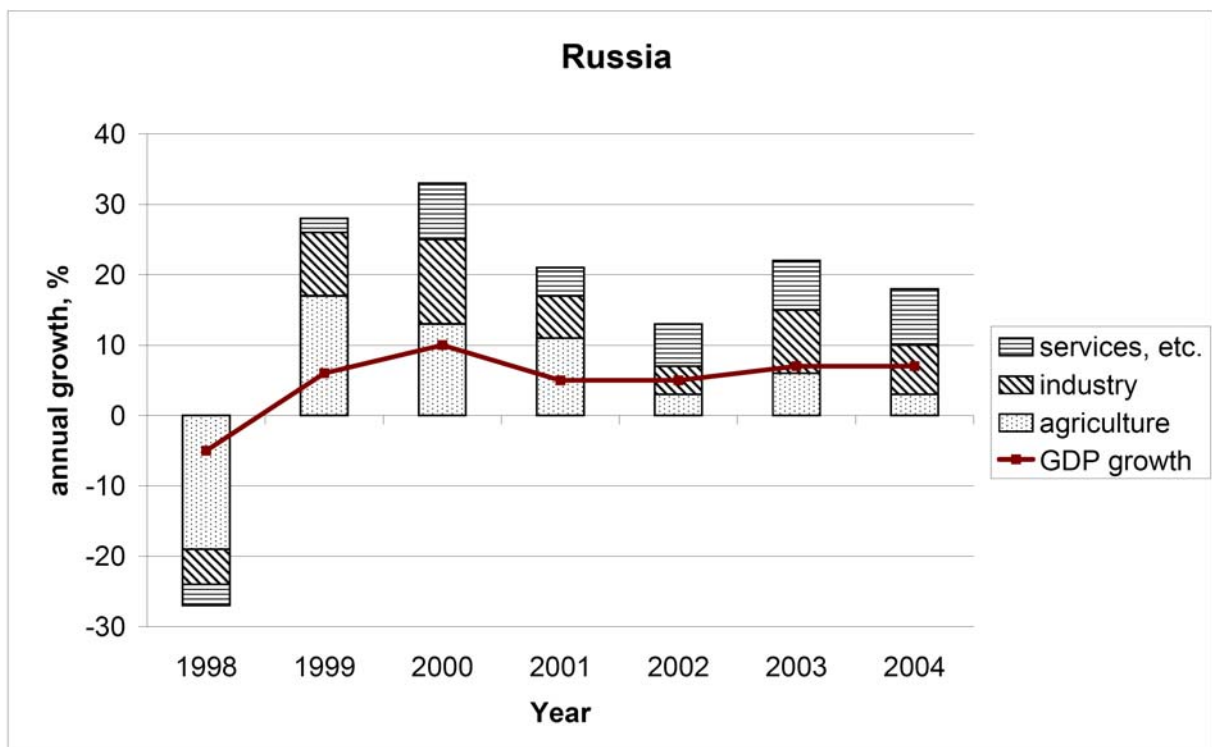
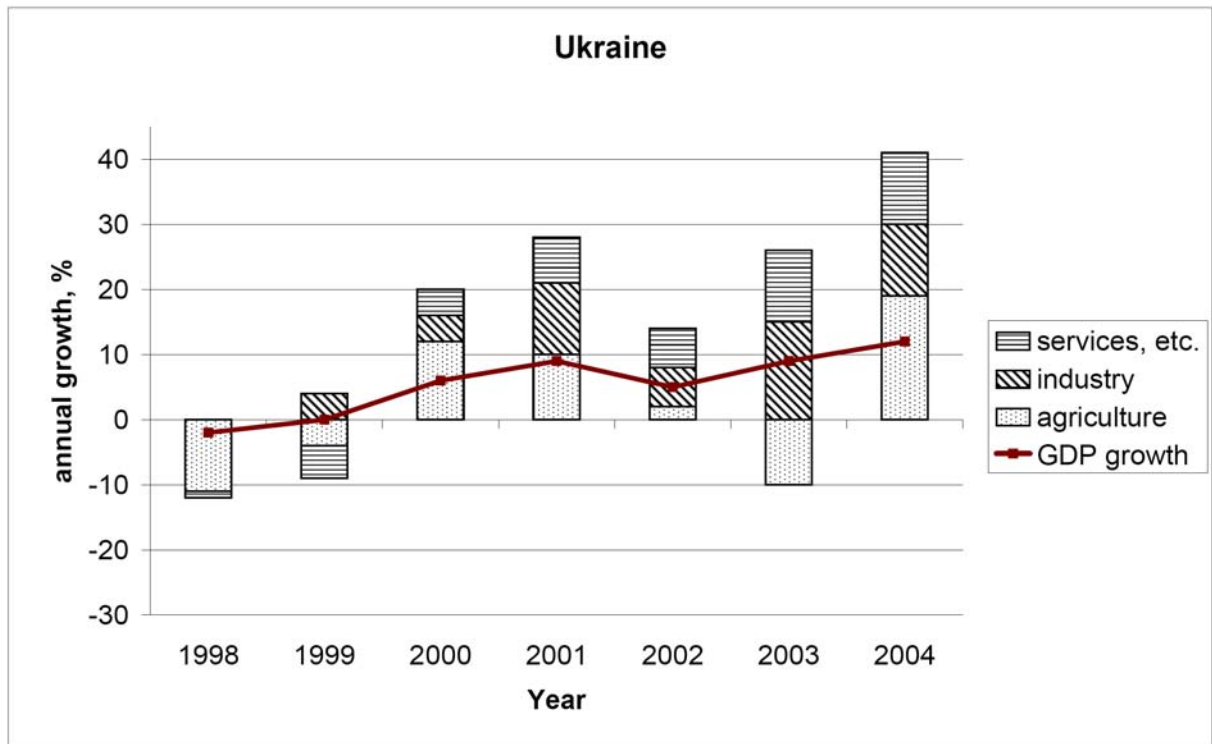
**FIGURE 1**

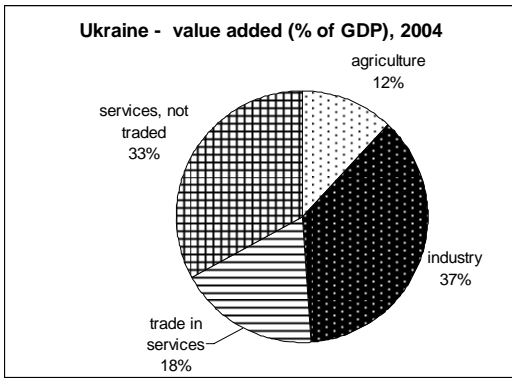
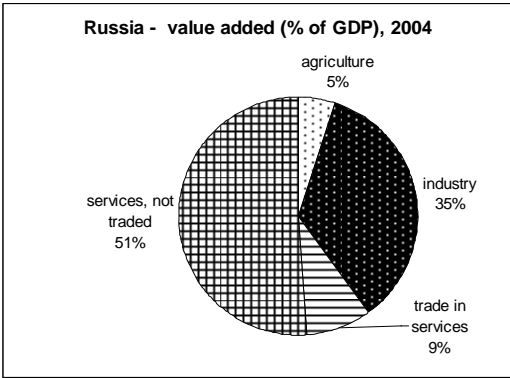
**GDP GROWTH BY DEMAND COMPONENTS IN UKRAINE AND RUSSIA, 1990-2004**



Source: World Development Indicators, World Bank; own calculations.

**FIGURE 2**  
**GDP GROWTH BY SECTORS IN UKRAINE AND RUSSIA, 1998-2004**





Source: World Development Indicators, World Bank; own calculations.

FIGURE 3

CHANGES IN DOMESTIC AND INTERNATIONAL SOURCES OF RENTS AND RENT-SEEKING OPPORTUNITIES, OR BARRIERS IN UKRAINE AND RUSSIA

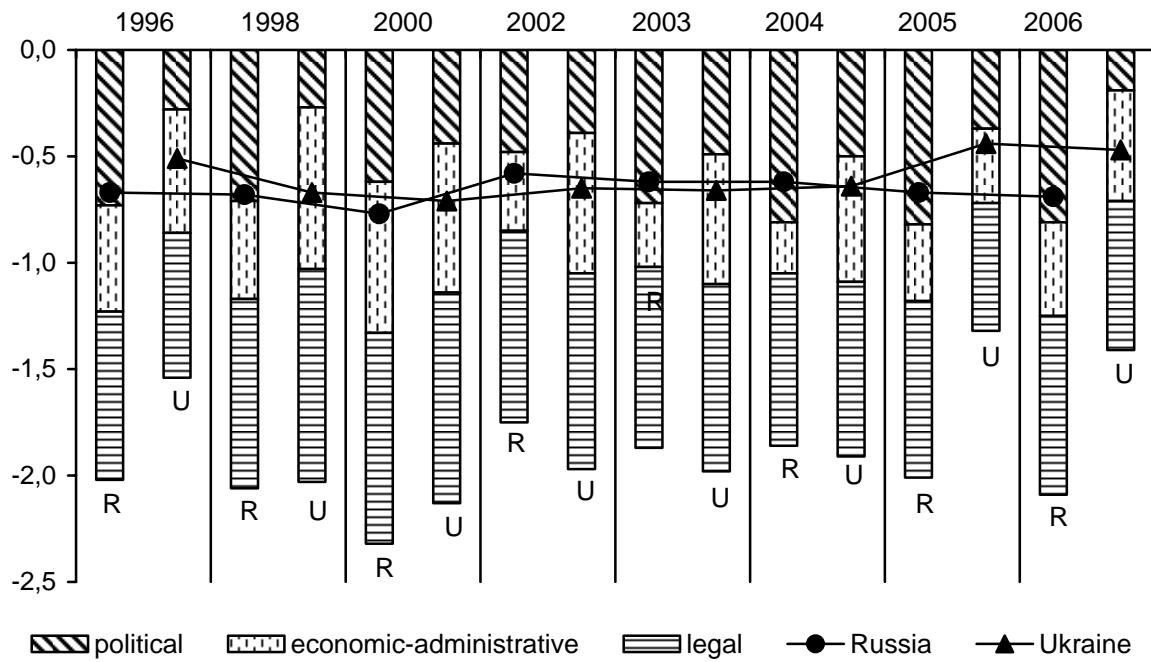
	early 1990s	middle 1990s	late 1990s	early 2000s
D O M E S T I C	<u>Russia:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies	<u>Russia:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies <b>* indirect subsidies</b> <b>* tax incentives</b> <b>* separate treatments</b> <b>* shadow/share-for-loans privatization</b>	<u>Russia:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies <b>* indirect subsidies</b> <b>* tax incentives</b> <b>* separate treatments</b> * shadow/share-for-loans privatization	<u>Russia:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies <b>* indirect subsidies</b> <b>* tax incentives</b> <b>* separate treatments</b> * shadow/share-for-loans privatization
	<u>Ukraine:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies	<u>Ukraine:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies <b>* indirect subsidies</b> <b>* tax incentives</b> <b>* separate treatments</b> <b>* shadow privatization</b>	<u>Ukraine:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies * indirect subsidies * tax incentives * separate treatments * shadow privatization	<u>Ukraine:</u> * credits of state's bank with negative real interest rates due to inflation *arbitrage opportunities * market monopolies * indirect subsidies * tax incentives * separate treatments * shadow privatization
I N T E R N A T I O N A L	<u>Ukraine:</u> * cheap fuel resources from Russia * external demand for Ukrainian metal and chemical products * weak international request for reforms * international focus on political stability * soft financial aid	<u>Ukraine:</u> * cheap fuel resources from Russia * external demand for Ukrainian metal and chemical products * weak international request for reforms * international focus on political stability * soft financial aid <b>* Russia's toleration of Ukrainian debts and illegal siphoning</b>	<u>Ukraine:</u> * cheap fuel resources from Russia * external demand for Ukrainian metal and chemical products * weak international request for reforms * international focus on political stability * soft financial aid * Russia's toleration of Ukrainian debts and illegal siphoning <b>* strong international pressure for reforms</b>	<u>Ukraine:</u> * cheap fuel resources from Russia * external demand for Ukrainian metal and chemical products * weak international request for reforms * international focus on political stability * soft financial aid * Russia's toleration of Ukrainian debts and illegal siphoning <b>* strong international pressure for reforms</b> <b>* focus on corporate governance</b>
	<u>Russia:</u> * resource endowments * weak international request for reforms * international focus on political stability * soft financial aid	<u>Russia:</u> * resource endowments * weak international request for reforms * international focus on political stability * soft financial aid	<u>Russia:</u> * resource endowments * weak international request for reforms * international focus on political stability * soft financial aid <b>* moderate international pressure for reforms</b>	<u>Russia:</u> * resource endowments * weak international request for reforms * international focus on political stability * soft financial aid <b>* moderate international pressure for reforms</b> <b>* focus on corporate governance</b>

Notes: "bold" script reveals the new sources of rents, "grey" script depicts the disappearance of some sources of rents and "normal" script shows the persistence of the source.

Source: Aslund (2002); Prizel (2002); Zimmer (2006); own illustration.

**FIGURE 4**

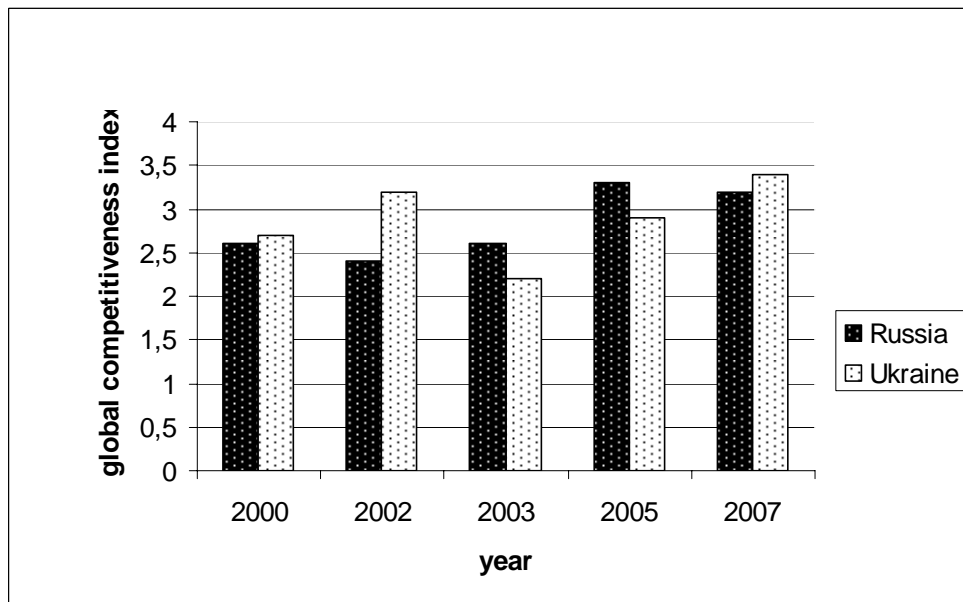
**PORGRESS IN INSTITUTION BUILDING IN UKRAINE AND RUSSIA, 1996-2004**



Source: World Bank Governance Indicators; own calculations.

**FIGURE 5**

**SECURITY OF PROPERTY RIGHTS IN UKRAINE AND RUSSIA, 2000-2007**



Source: The Global Competitiveness Report