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## Russia: An Abnormal Country

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### Abstract

Andrei Shleifer and Daniel Treisman recently rendered a summary verdict on the post Soviet Russian transition experience finding that the Federation had become a normal country with the west's assistance, and predicting that it would liberalize and develop further like other successful nations of its type. This essay demonstrates that they are mistaken on the first count, and are likely to be wrong on the second too. It shows factually, and on the norms elaborated by Pareto, Arrow and Bergson that Russia is an abnormal political economy unlikely to democratize, westernize or embrace free enterprise any time soon.

JEL Classification: P30, P40, P51, P52

Keywords: Russian economy, transition economics, comparative economic systems

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Master Pangloss taught the metaphysico theologo cosmologicology. He could prove to admiration that there is no effect without a cause, and that in this best of all possible worlds, the Baron's castle was the most magnificent of all castles, and my lady the best of all baronesses. It is demonstrable, said he, things cannot be otherwise than as they are, for as all things have been created for some end. They who assert that everything is right, do not express themselves correctly, they should say that everything is best (Voltaire, *Candide*, Chapter 1 How Candide Was Brought Up in a Magnificent Castle and How He Was Driven Thence, 1759. (Google, Online Literature Library).

### 1. Introduction

Andrei Shleifer and Daniel Treisman (Shleifer and Treisman, 2004; Shleifer, 2005) contend that Russia has become a "normal country,"<sup>2</sup> because thanks to the G-7's advice, Boris Yeltsin and Vladimir Putin have done most things right (Cf. Fischer and Sahay, 2004, Kuboniwa and Gavrilentov, 1997; Cf. Ellman, 2004).<sup>3</sup> They define "normalcy" interchangeably as 1) a nation which has crossed the threshold from a cold war, centrally planned, authoritarian martial police state to virtuous democratic free enterprise, and 2) a middle income developing country with mixed characteristics that might mature into the western ideal. There is no reason to doubt that Russia can be classified as normal in the later sense, without implying a common destiny, even though much of the evidence Shleifer and Treisman adduce is misleading, because the criterion is elastic, requiring little more than Russia's partial abandonment of authoritarian rhetoric, planning and state ownership. But the contention that consumer demand governs household supply under the rule of law, and people's preferences determine

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<sup>1</sup> The Bank of Finland Institute for Economics and Transition's support is gratefully acknowledged.

<sup>2</sup> Vladimir Shlapentokh also connects Shleifer's and Treisman's analysis with Pangloss. See Vladimir Shlapentokh, "Shleifer and Treisman's Economic Comparisons are Wrong," *Johnson's Russia List*, No.8091, Article 16, February 28, 2004. Shlapentokh contends that he was the first to use the term "normal country" citing his "'Normal' Russia," *Current History*, No.212, October 1997. However, Anders Aslund employed it a few months earlier. See Aslund, "Russia Gets on Track to be a Normal Country," *International Herald Tribune*, March 19, 1997, p.8. Cf. Matthew Maly (2002, 2004).

<sup>3</sup> John Olding-Smee, former Director of the IMF's European II Department 1992-2003 shares the same outlook.

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public choice is wrong, as are the assertions that the Kremlin eschews authoritarianism at home and domination in the “near abroad.” Nor is it likely that Russia is favorably positioned to be as efficient and just as the developed west in the foreseeable future.

## 2. Muscovite abnormality

The abnormality of Russia's private sector economy is easily established by comparing its traits with those of developed western market systems, without begging the question by assuming that the flaws exhibited by developing systems are self-remedying. The litmus tests are the characteristics of ownership, property rights, rule of contract law, price determination, market entry, profit maximizing, utility maximizing, efficient equilibration, and state regulation responsive to popular will. The existence of markets is a necessary, but not a sufficient condition for western economic normalcy (Gaddy and Ickes, 2002).

Ownership in Russia fails this test. The land and most resources, as well as a large portion of the capital stock still remain in the hands of the state,<sup>4</sup> and workers own a large share of the voting capital of industrial enterprises.<sup>5</sup> Proprietary rights of ownership and control over non-state assets remain tenuous, as demonstrated by the expropriation and de facto re-nationalization of Yukos.<sup>6</sup> Alienable proprietorships, especially lucrative ones operate more as rent-seeking than competitive profit maximizing entities. Directors live lavishly off cash flow, delegating coercive authority in the traditional manner throughout the organizational hierarchy without striving to maximize net current income, or present discounted asset values. And avaricious insiders use networking to obtain underpriced resources from the state, and exert market power. They act as Muscovite lords, overseeing the operation of the Czar's domains at his sufferance, coercing vassals and others unprotected by the rule of law (Rosefielde and Hedlund, 2006, Shlapentokh, 1996).

This may look like profit maximizing in the normal western sense, but isn't because oligarchs and lesser insiders are anticompetitive, capricious, inattentive to consumer demand, and do not pay factors the value of their marginal products. Likewise, normal self-regulating markets in the west are disciplined by the rule of contract law. No individual, agent, firm, or corporation is above it. They cannot arbitrarily impose their will, nor violate contracts without judicial sanction. In Russia, matters are the other way round. State insiders and oligarchs control the judiciary, and use judicial sanctions to suppress competition, and equal opportunity. As a consequence, moral hazard and adverse selection are pandemic. And conditions in the state sector are no better. Officials, especially the secret police (FSB) run their operations like feeding troughs, extorting bribes and protection money for services rendered and harassment withheld. Government programs are chosen by Putin and his deputies, not democratic

<sup>4</sup> "Seventy percent of assets still in state hands, says Russian audit chief," ITAR-TASS, reprinted in *Johnson's Russia List*, No.9022, Article 1, January 19, 2005. "Stepashin stressed that, according to experts' assessments, "70 percent of national assets have not yet been privatized. These include mineral resources, land and energy resources." In this connection he said it was essential for members of parliament to draw up a number of proposals for enactments and legislation on Russia's forthcoming privatization.

<sup>5</sup> Andrei Nesterenko, "Markets between Soviet Legacy and Globalization: Neoinstitutionalist Perspectives on Transformation," in Klaus Segbers, ed., *Explaining Post-Soviet Patchworks: Pathways from the Past to the Global*, vol.2 (Aldershot, England: Ashgate, 2001), pp.78-103. According to Nesterenko, by the mid-1990s more than half of public property was privatized, but many of these companies aren't truly private because their formal owners cannot exercise management and earn profit (p.97).

<sup>6</sup> "Baikal is Shock Winner of Russia's YUKOS Auction," *Johnson's Russia List*, No.8506, Article 1, December 19, 2004.

mandate in what is now an implicit one party state, and are operated opaquely by an administrative bureaucracy unresponsive to the popular will.<sup>7</sup> In short, Putin's variant of Muscovy and democratic free enterprise are mutually exclusive. Muscovy cannot be normal because the Kremlin is politically and economically sovereign, not the people. Of course, the west doesn't live up to its own ideals, but Russia's deviations are immensely greater.

### 3. Misleading counter evidence

Shleifer and Treisman choose to sidestep these essentials, pretending variously that they don't exist, are subsidiary, or transitory. They attempt to prove that Russia is "normal" by declaring that GDP has fully recovered, and by denying that the post-Soviet decline was exceptional for transitioning societies. In doing so, they tacitly assume that the internal rot of the Soviet system caused its collapse and subsequent depression, rather than the deficiencies of the successor system, and contend that rapid liberalization remedied the problem. It is therefore useful to bear in mind some essential facts. First, not all Soviet-type natural economic planning systems collapse, or implode trying to marketize. The statistics in Table 1 compiled by Angus Maddison in 1990 international Geary-Khamis dollars for the USSR, Russia and China demonstrate that Beijing began its great economic ascent in 1950 under Mao, and never looked back. Per capita growth decelerated after 1959, following a familiar Soviet-type pattern. Between the "great leap forward," and the end of the "cultural revolution" 1959-1976 it fell from 5.2 to 1.2 percent per annum, but it accelerated under Deng Xiaoping's marketization without ever skipping a beat. Second, although ownership of most productive assets, private business and entrepreneurship were illegal in large scale industrial enterprises throughout the twenties (Nove, 1982), Maddison's statistics confirm that the USSR's GDP managed to recover from War Communism by 1928, and the Soviet natural economy under Stalinist planning grew moderately during the thirties, and recovered briskly after World War II (Table 2). Consequently, it cannot be validly inferred that Russia has become a normal country just because it has partly, or wholly recovered from the trough of the post-communist hyperdepression. The USSR demonstrated a capacity to revive from disaster on two occasions, so that a post-communist bounce that is well shy of a full recovery fifteen years after the onset of "catastoika" cannot prove that Russia has transitioned to "normalcy."

Table 1

#### Centrally Planned Communist Growth Spurts and Decay (Per capita GDP growth, percent)

	1928-40	1950-59	1959-76	1976-91	1991-98
USSR	3.8	2.9	3.2	0	-7.5
Eastern Europe	-	3.2	3.5	-0.8	1.8
China	-	5.2	1.2	5.6	7.0

Source: Angus Maddison, *The World Economy: Historical Statistics*, OECD, Paris, 2003, pp. 100-1, 184.

<sup>7</sup> The recent conversion of social welfare benefits in kind to cash payments, and the Yukos case illustrate the point. See Yulia Kalinina, "There will be no Revolution," Johnson's Russia List, No. 9063, Article 1, February 28, 2005. Konstantin Smirnov, "A Frank Admission: The Cabinet Doesn't Play Any Significant Political Role in Russia," *Kommersant-Dengi*, No.13, April 4, 2005. "Presidential aide Igor Shuvalov has publicly admitted something of which the Kremlin had long been suspected, but without proof: the YUKOS affair is politically motivated, and the Kremlin won't hesitate to do the same again if necessary."

Table 2

USSR and Russia GDP 1913-2002 (billion 1990 international Geary-Khamis dollars)

	USSR	Russia
1913	232.8	-
1928	231.9	-
1929	238.4	-
1938	405.2	-
1940	420.3	-
1945	333.7	-
1950	510.2	-
1973	1,513.1	872.5
1989	2,037.3	-
1991	1,863.5	1,094.1
1998	1,124.9	655.4
2001	1,343.2	790.6
2002	1,405.6	825.3

Source: Angus Maddison, *The World Economy: Historical Statistics*, OECD, Paris, 2003, pp.98-99, 111.

Note: Maddison defines the figure for 1913 on the boundaries of the USSR. Figures for Russia are defined for the post-Soviet Russian Federation.

Indeed, logic suggests the opposite. Since, marketization accelerated Chinese growth, if liberalization really made Russia normal, the post-communist contraction should have been mild and brief. Shleifer and Treisman try to deflect attention from this in two ways. They claim, contrary to Maddison's estimates, that Russia fully recovered by 2003, when the data indicate that it was mired in a hyperdepression deeper than America's Great Depression. And, they go to great lengths to rebut allegations that Yeltsin's liberalization strategy was part of the problem, not the cure.

#### 4. Misadjusting gdp statistics

The contention that Russia's post-communist hyperdepression was only a mild depression, or merely a recession attacks the issue from both ends. Shleifer and Treisman allege that Soviet growth was overstated, and the decline which began in 1989 was shallower than official statistics indicate. These are complex matters, but it is easy to show that they are wrong on the first count, and fail to provide convincing evidence on the second.

The suspicion that Soviet growth rates were cosmetically enhanced has been part of the Sovietological landscape from the beginning. The consensus view has been that while Soviet physical production statistics may have been exaggerated, new goods pricing was the main culprit (Rosefielde, 2003, 2004, 2005). Enterprise managers padded the costs and value (price) of new products and improvements to make their performance seem better than it was. Abram Bergson and the Central Intelligence Agency made adjustments for this phenomenon in various ways, including the construction of purchasing power parity dollar series (Bergson, 1961, CIA, 1982). The data in Table 3 which contrast Bergson's and the CIA's ruble factor cost and dollar estimates with Maddison's demonstrate that they are well below the OECD's estimates (1990 international Geary-Khamis) dollars). And all are far lower than the Soviets

officially reported (Rosefielde and Kuboniwa, 2003), but not low enough to substantiate Shleifer's and Treisman's contention that the post-communist hyperdepression reported by Goskomstat is a mirage because the 1989 GDP level is significantly overstated. Of course, Shleifer and Treisman may have still deeper cuts in mind, but at this juncture the burden is on them to validate their position.

Table 3

Alternative Estimates of Soviet GDP Growth 1913-89 (ruble factor cost, and purchasing power parity; indexes)<sup>8</sup>

	<i>Bergson/CIA</i>		<i>Maddison</i> Dollars
	Rubles	Dollars	
1913	-	-	100.0
1917	100.0	100.0	-
1928	98.4	130.3	99.8
1937	258.4	-	171.3
1955	468.0	641.1	278.9
1970	1,031.8	1,520.6	581.8
1987	1,539.6	-	-
1989		4,473.9	876.8
<i>Growth Rate</i>			
1913-87	4.0		
1917-89		4.7	2.6

Source: Angus Maddison, *The World Economy: Historical Statistics*, OECD, Paris, 2003, pp 85-86, 98-99. Steven Rosefielde and Stefan Hedlund, *Russia After 1984: Wrestling with Westernization*, Cambridge UP, London, 2006, Chapter 5, note 15. The underlying sources are Abram Bergson, *Productivity and the Social System—The USSR and the West*, Harvard University Press, Cambridge, 1978, Table 5.7, p.67. Table 8.1, pp. 120-21. CIA, *Measures of Soviet Gross National Product in 1982 Prices*, Joint Economic Committee of Congress, Washington DC, November 1990, Table A-1, pp.54-57.

Shleifer and Treisman also challenge the notion that "first economy" Soviet products and services were really "goods" (had positive utility), implying that a substantial share of the output in series like Maddison's should have zero Geary-Khamis international dollar prices. The claim, a variant of the "value subtraction" thesis,<sup>9</sup> has some superficial plausibility because supply in Soviet times was unresponsive to demand. People had consumer choice, but not consumer sovereignty, and were forced to substitute what was available for products they desired. But no authority including Bergson, and the CIA who constructed purchasing power parities by matching Soviet and American products ever found that Moscow's goods were valueless (Schroeder and Edwards, 1981), or concluded that Soviet growth shown in Table 3 was illusory. While,

<sup>8</sup> Method: Bergson's dollar estimates (and the CIA entry for 1989) are computed by multiplying their comparative size statistics by Maddison's dollar GDP series. The Bergson/CIA PPP use multiple bases. The PPPs appear to have been revised upward over time causing the implausibly high Soviet GDP growth displayed in the Table 2.

Note: Bergson's estimates cover the subperiod 1917-55. The CIA's estimates are valued in 1982 ruble factor cost and apply from 1955-1987.

<sup>9</sup> It became fashionable in the nineties to allege that processing raw materials at various stages of fabrication instead of adding value, diminished it. Logs for example were said to be more valuable than furniture produced from them. This may have been true from the standpoint of foreign trade. Japanese for example were willing to pay higher prices for logs than for Soviet furniture. But the concept has little validity in an autarkic economy where domestic consumers gladly pay more for furniture than logs. See Gaddy and Ickes (2002).

it is true that some Russian consumers may have been more satisfied with the post-communist product characteristics and assortments, this doesn't disconfirm the hyperdepression chronicled in Maddison's GDP index. Likewise, one can sympathize with the argument that reduced weapons production was a positive development, without agreeing that arms should have been excluded from GDP. Soviet weapons weren't valueless (Rosefelde, 2005). Russia today is the world's second largest arms exporter after the United States, and the weapons which went unproduced during the nineties could have been exchanged for consumer imports had they been produced.

Shleifer's and Treisman's assertion that Russian GDP after 1991 is understated takes two forms. First, they contend that the official series and dollar valued alternatives like Maddison's are superseded by other indicators. "Although economic output fell initially after the Soviet Union collapsed, plausible estimates suggest that the decline had been reversed by 2003." No GDP series shows this; neither Goskomstat's, nor the World Bank's, IMF's, United Nations' or OECD's. But this doesn't give them pause because they insist that electricity consumption was a superior proxy for aggregate economic activity, and claim that tax evasion motivated post-communist businessmen to underreport profits and output. Neither rationale is sufficient. As every specialist knows, Russian industrial, government and household users paid virtually nothing for electricity during the nineties, and most industrial production was fueled by petroleum, coal and natural gas.<sup>10</sup> The electricity series therefore is a poor proxy for industrial activity. Likewise, while no one doubts that some Russian businessmen evaded taxes, this source of underreporting was offset by the "second economy's" legalization. Contraband goods and services omitted from official GDP statistics before 1991 were included as value added thereafter, offsetting the effects of tax evasion in part or whole. Thus while the 45 percent contraction 1989-98 reported by Maddison isn't unassailable, there are no grounds for accepting Shleifer and Treisman's claim that pre 1991 GDP statistics were sufficiently upward biased, and post 1991 figures were sufficiently biased in the opposite direction to warrant the claim that the post 1991 decline was reversed by 2003.

Moreover, the reality of hyperdepression is not only corroborated by sociological surveys (Field and Twigg, 2000), excess death statistics attest to the privation of the nineties. Even though most people managed to survive a catastrophic collapse in food and industrial consumer goods consumption by extending the service lives of their clothes and household durables, 3.4 million died prematurely 1990-1998 (Rosefelde, 2001). Since there were no wars, pandemics, or other extraordinary factors at play, it is reasonable to conclude that the hyperdepression indicated by Maddison's series was real, and lethal.

## **5. Coincident indicators of hyperdepression**

The abnormality of post-communist Russia judged by the characteristics and performance of the new system, rather than the Soviet past, is confirmed by a variety of other evidence. After claiming for years that unemployment in the nineties was just a few percent, Goskomstat finally admitted that the figure was in the mid teens, and even these statistics were biased downward by the omission of discouraged workers. Using Soviet census data, it can be easily shown that the real unemployment rate was closer to

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<sup>10</sup> Academician Valery Makarov, Director of the Central Economics and Mathematics Institute. Private discussion, Moscow, 1998.

25 percent, a figure in line with a 45 percent fall in GDP (Rosefielde, 2000).<sup>11</sup> Not only was negative growth and massive involuntary unemployment catastrophic, in sharp contrast to China's sustained market driven advance, but the distribution of wealth and income became drastically skewed. Billionaires sprouted like mushrooms amid widespread economic decline,<sup>12</sup> and the Gini coefficient jumped from 0.26 in 1991 to 0.41 in 1994, widening thereafter due, on the one hand, to rapidly accelerating unemployment, and, on the other, asset grabbing by oligarchs and others. Shleifer and Treisman try to interpret this as evidence of normality, arguing that the phenomenon was the natural consequence of switching from state imposed egalitarianism to negotiated wage setting. But the World Bank study *Making Transition Work for Everyone: Poverty and Inequality in Europe and Central Asia* shows that rising education premiums and wage dispersion explain very little of the rise in inequality. The causes of the huge rise lie "in the prevalence of widespread corruption and rent seeking, in the capture of the state by narrow vested interests, and in the resulting collapse of formal wages and income opportunities. People, except for the privileged few, are largely stuck in their low-paying jobs."<sup>13</sup>

## 6. Plunder and hyperdepression

Shleifer and Treisman also try to create the impression that asset grabbing, asset stripping, rent seeking and related criminal and quasi-criminal activities which dominated "business" decisionmaking, and reflected its character played no role in generating Russia's hyperdepression because "privatization came after 1994." Blame, they declare, doesn't lie with the "loans for shares" scandal, and derivatively with Shleifer for counseling "don't ask, don't tell" privatization,<sup>14</sup> nor with haste (shock versus gradualism),<sup>15</sup> because the irrelevant electricity index shows that the fall began before 1994. And, if they are somehow mistaken; if the plundering of state property did play a role, then they find virtue in necessity, insisting that kleptocratic privatization was constructive because the brunt of the contraction was borne by weapons and Soviet era consumer "bads."<sup>16</sup> Moreover, they go so far as to imply that the hyperdepression was a myth by labeling it a "recession," defined by the National Bureau of Economic research as a shallow fall in GDP of no more than a few percent, lasting at least six months, with a swift recovery thereafter.<sup>17</sup> Russia's recession began in 1989, so, applying their concept, it must have ended before the Soviet Union dissolved.

<sup>11</sup> Steven Rosefielde (2000). Even as late as the end of 2003 8.6 percent of Russia's economically active population (6.2 million people) were unemployed. The labor force was 65.2 million. But adjustment for discouraged workers puts the figure in the teens.

<sup>12</sup> For a list of Russia's richest oligarchs see Clem Cecil, "Russian Oligarchs Fear Putin Inquiry into Their Wealth," *The Times*, July 18, 2003.

<sup>13</sup> Ed Dolan, "Wolpin/Normality and Inequality/8087," *Johnson's Russia List*, No.8089, Article 16, February 27, 2004.

<sup>14</sup> "Tainted Transactions: An Exchange," (Spring 2000), and replies by Jeffrey Sachs, Anders Aslund, Marek Dabrowski, Peter Reddaway, Igor Aristov, Wayne Merry, Michael Hudson, David Ellerman and Steven Rosefielde, "Tainted Transactions: Replies," (Summer 2000). Also, see Wedel (1998, 2000a, 2000b).

<sup>15</sup> For a discussion of Shleifer's role a U.S government advisor to Russia, and his subsequent Federal prosecution for conflict of interest see Janine Wedel (1998), David Gellis, "Harvard in Settlement Talks with Forum," *Harvard Crimson*, October 30, 2002, "Harvard Settles with Mutual Funds Company Over Fraud Allegations," *Associated Press*, November 8, 2002, "Harvard Professor, Employees Liable in Fraud Case, But \$102 Million Claim Against University Fails," *Boston Globe*, June 29, 2004.

<sup>16</sup> Wedel (1998). Shleifer and Treisman's comparison of Russia and the Ukraine is disingenuous. They use their own favorably adjusted figures for Russian per capita income and compare it with official Ukrainian data. If they didn't mix apples and oranges there wouldn't be any significant disparities.

<sup>17</sup> Their fall back rationale is "the temporary dislocation that all countries experienced as their planning systems disintegrated." Apparently, they don't know that the Soviet system was also stabilized by guaranteed purchase and

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This wordplay is diversionary. Although many factors were contributory, Russia's hyperdepression was primarily caused by dysfunctional aspects of Russia's Muscovite rent-granting system, not by standard macroeconomic disturbances associated with recessions in western market economies. "Spontaneous" privatization 1988-92 under Gorbachev got the ball rolling (Rosefielde and Hedlund, 2006), exacerbated soon thereafter by the corrupt "voucher privatization" promoted by Shleifer with US AID funding, but the principal cause was the Yeltsin administration's "shock therapeutic" cancellation of most state contracts in the Spring of 1992 (Kleiner, 2001). Before this blunder (or callous attempt to facilitate asset grabbing), enterprises enjoyed assured purchase. They depended on guaranteed sales to cover their expenses. Suddenly and without warning, they had no orders, no credit, no saleable products, and established market institutions to aid them, allowing insiders to acquire assets for a pittance, and making hyperdepression inescapable.

Shleifer and Treisman similarly gloss over the venal antics of Russia's financial policy authorities, and duck responsibility for pathogenic "assistance" they provided the Federation on the U.S. government's behalf by blaming the 1998 economic meltdown on the Asian financial crisis. As John Kenneth Galbraith might have phrased it, they give Asia too much credit for knocking down Russia's rotten door. The Federation's financial crash was widely anticipated a half year before it occurred, without any reference to Asia, and Joseph Stiglitz insists that it was partly caused by the IMF's bad advice, not cured by it.<sup>18</sup> His observation is apt, but also obscures the deeper point. The Russian economic system forged when Mikhail Gorbachev gave the green light for state complicitous asset grabbing in 1988 was an abnormal throw back to Muscovy, destined to malfunction no matter what macroeconomic policy regime was adopted.

## 7. Normally abnormal

Shleifer and Treisman in a similar vein don't flinch in defending "crony capitalism," and "oligarchy," contending that those who plundered Russia's patrimony have transformed themselves into world class entrepreneurs like John D. Rockefeller and J.P. Morgan. Events however prove they are mistaken. The de-facto renationalization of Yukos without compensation belies the claim that Russia's "robber barons" are likely to become locomotives of westernization.<sup>19</sup> Nor are they chastened by evidence of the abnormal extent of Russia criminalization, citing World Bank and EBRD surveys showing that Russia ranked "right in the middle of its post-communist peers." Since "the burden of bribery and state capture" in other post-communist nations is unusually high, they contend that these vices aren't important. As long as Russia's behavior is coincident with its peers, it doesn't matter that the Muscovite system isn't consumer sovereign, and responsive to the people's will because "Democracies in this income range are rough around the edges: their governments suffer from corruption, their judiciaries are politicized and their press is almost never entirely free. They have high income inequality, concentrated corporate ownership, and turbulent macroeconomic performance."<sup>20</sup>

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contracts, which made it profitable for enterprise managers to operate at full employment without planning.

<sup>18</sup> Donald Rutherford (2000), p.386. Joseph Stiglitz, "Rewriting History," *Johnson's Russia List*, No.6578, November 2002.

<sup>19</sup> "Russia's Latest Auction Farce Eerily Familiar," *Johnson's Russia List*, No.8509, Article 1, December 2004.

<sup>20</sup> Shleifer and Treisman (2004), p. 22. Matthew Maly noting the same distortions says that Shleifer and Treisman define "normal" as "whatever you should do to satisfy my expectations." See Matthew Maly, "My comment on A



And they save the best for last. The opinion of the majority of experts and Russian human rights activists notwithstanding,<sup>21</sup> Shleifer and Treisman assert that Russia has been wrongly accused of authoritarianism (Tenet, 2004). "Russia's politics have been among the most democratic in the region. And the defects in the country's democracy resemble those found in many other middle-income countries."<sup>22</sup> Since Putin isn't much different than Leonid Kuchma, it follows on their logic that Russian democracy is "normal", a point they insist is confirmed by frequent and fair elections. Similarly, they claim that Russia no longer harbors Muscovite martial aspirations, "It's army has withdrawn peacefully from both eastern Europe and the other former Soviet republics, allowing the latter to become independent countries",<sup>23</sup> ignoring the fact that Russia heads the CIS armed forces, that its troops occupy the Transdnjestria, and that the Kremlin is ramping up for a major military modernization drive (Rosefielde, 2005). When Russia is assiduously developing new ballistic missiles to outmaneuver America's national missile defense (NMD),<sup>24</sup> and maintains 40,000 retargetable nuclear weapons (more with the simple reinsertion of nuclear triggers), they describe Russia as "a partner ready to cooperate on disarmament, fighting terrorism, and containing civil wars." And equally fundamental, they fail to notice that Putin used his position as head of the secret police 1998-99 to become president (Blank, 2004), and that the Federal Security Bureau (FSB) is omnipresent throughout the government, overseeing administration, the military, politics, and the economy.<sup>25</sup>

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Normal Country by Andrei Shleifer and Daniel Treisman," *Johnson's Russia List*, No.8081, Article 17, February 23, 2004. Cf. Ed Dolan, "Normal or Not," *Johnson's Russia List*, No.8087, Article 5, February 23, 2004. Shlapentokh calls Russia "normal," but uses the term to mean that Russian society as it was shaped in 1991-1994 is able to function and reproduce itself for an indefinite period. See Vladimir Shlapentokh, "Shleifer and Treisman's Economic Comparisons are Wrong," *Johnson's Russia List*, No.891, Article 16, February 28, 2004.

<sup>21</sup> Sergei Kovalyov, a human rights legend, who spent 10 years in Gulag, recently wrote "It turned out that 13 years after the fall of the Soviet Union, the society does not require democracy." See Anna Badkhen, "Democracy on the Brink: Russia Back on Track of Absolute Rule," *Johnson's Russia List*, No.8108, Article 1, March 10, 2004. Cf. Stephen Blank, "Is Russia a Democracy and Does it Matter?" unpublished manuscript April 2004.

<sup>22</sup> Shleifer and Treisman (2004), p. 32.

<sup>23</sup> Shleifer and Treisman (2004), p. 20.

<sup>24</sup> "New Russian Missiles to Outwit US Defenses," *Krasnaya Zvezda*, February 25, 2004, reprinted in *Johnson's Russia List*, No.8093, March 1, 2004. Russian forces will have the new missile, which will act like a swarm of bees against America's umbrella defense system, by 2010.

<sup>25</sup> Cf. Arkady Ostrovsky, "Is Russian Democracy Becoming an Illusion," *Financial Times*, reprinted in *Johnson's Russia List*, No.8042, Article 13, February 2004. Donald Rayfield reminds us that Russia "is ruled by a man who is, by career and choice, a successor to Yagoda and Beria," and today's FSB "has taken, in alliance with bandits and extortioners, the commanding heights of the country's government and economic riches, and goes on lying to, and when expedient murdering, its citizens." See, Simon Sebag Montefiore, book review of *Stalin and His Hangmen: an Authoritative Portrait of a Tyrant and Those Who Served Him*, Viking, 2004, reprinted in *Johnson's Russia List*, No.8114, Article 6, March 13, 2004. Cf. Montefiore, "Democratic Despot," *New York Times*, (Op-Ed), March 14, 2004: "Vladimir Putin, who will be handily re-elected president of Russia today, is never going to become a Western-style, liberal-democratic politician, no matter how much we wish it. He is a quintessentially Russian leader, with very traditional aspirations and interests, and until the West gets used to it, he will continue to be a tantalizing source of frustration and disappointment." "A reforming liberal leader in Russia is the Holy Grail of Kremlinology, but the search for one is as misguided and hopeless as that for the relic of the Last Supper. Believe it or not, some Western analysts in the 1930's insisted that Stalin was a 'moderate,' controlled by extremists like the secret police chief Nikolai Yezhov. Khrushchev became the next great hope after he denounced Stalin and ended the Terror in the 50's, but his real interests were personal power, state consolidation and Marxist Leninism. Mikhail Gorbachev was a reformer, but not a liberal - his real wish was to reform, not end, Marxism-Leninism." Also, Russia's pro-western orientation is shakier than Shleifer and Treisman acknowledge. In a recent story in the communist newspaper Pravda, it is easily observed that old attitudes persist. "Recently big anti-Russian campaign has been launched by European and American media depicting Russia as the new empire of evil where 'the state is terrorizing citizens, human rights are violated, businessmen are prosecuted and there is atmosphere of total fear to authorities.'" Their intention is to discredit Putin. This preamble, is followed with Soviet era invective, and the assertion that Russia is exceptionist, and superior to the west. Citing Alexander Sobyenin, the article suggests that

## 8. Eternal Muscovy

The Russia Shleifer and Treisman portray does not exist. Where they see a system firmly rooted in the market principles, and well along the path to full fledged free enterprise, displaying few signs of micro and macroeconomic pathology, despite "the grabbing hand" (Shleifer and Vishny, 2000), the regime actually is a throw back to the traditional anti-competitive, privilege preserving, rent-granting of Muscovy. Where they perceive a nascent democratic order, responsive to the people's will, committed to social justice, eschewing military superpower and fostering global harmony, the reality is more nearly an authoritarian martial police state. Gregory Yavlinsky expresses the essence of the matter this way:

There are six major features of Russia which must be taken into account today.

- First, Russia has no independent judicial system.
- Second, since December, Russia has no elements of independent parliament.
- Third, Russia has no parliamentary control or oversight of the secret services and law enforcement agencies.
- Fourth, Russia has no politically important independent media.
- Fifth, elections in Russia are manipulated by the government.
- Sixth, the Russian economy is an instrument of the state.<sup>26</sup>

Shleifer and Treisman's mischaracterization of postcommunist Russia as a "normal" westernizing middle income country on its way to becoming a fully normal democratic, free enterprise regime is Pangloss, but their article does raise the important issue of contemporary evidentiary standards. They aren't the first, nor will they be the last policy advocates to enlist elastic norms,<sup>27</sup> and mischaracterize evidence (Rosefielde and Mills, 2006). Can scholars do better?

## 9. Pareto – Bergson - Arrow normalcy standard

Of course they can. Vilfredo Pareto, Abram Bergson, and Kenneth Arrow, building on the enlightenment edifice of Adam Smith worked out the essentials more than a half century ago (Abram Bergson, 1938, 1948, 1954, 1966, 1967, 1976; Samuelson, 1977, 1981; Arrow, 1963, 1981). The "good" society which Samuel Huntington identifies with the "idea of the west", (Samuel Huntington, 1996) is efficiently consumer sovereign both with respect to private and public goods. Efficiency

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conflict between the Russia and the west is inevitable because Russians are virtuous collectivists, while westerners are depraved egomaniacs. See Mikhail Chernov, "West Against Russia," *Johnson's Russia List*, No.8114, Article 6, March 13, 2004.

<sup>26</sup>Yavlinsky's assessment coming as it did after the elections of 2003 in which his Yabloko party lost its parliamentary representation may overstate the extremity of Putin's authoritarian control, but is basically on the mark. Grigory Yavlinsky, Chairman of the Russian Democratic Party 'Yabloko,' "Russia: Before and After the Elections," Carnegie Endowment for International Peace, February 26, 2004, reprinted in *Johnson's Russia List*, No.8107, Article 11, March 10, 2004. The citation in the text is paraphrased. Cf. Anders Aslund, "The Russian President's Second Term Disaster," *Johnson's Russia List*, No.9012, Article 13, January 12, 2005. Peter Rutland, "Russia: Democracy Dismantled," *Johnson's Russia List*, No.9010, Article 2, January, 10, 2005; Ellman (2004), Reddaway and Gliniski (2001). Peter Rutland, "PONARS Scholars Condemn U. S. for ignoring Authoritarian Trends in Russia," *Jamestown Foundation Eurasia Daily Monitor*, February 9, 2005.

<sup>27</sup> Wayne Merry, "A Normal Country," *Johnson's Russia List*, No.8087, Article 6, February 26, 2004. Merry stresses these issues

here is Paretian. It means that given a voluntary Lockean social contract, and a corresponding fair play rule of law, individuals capable of rationally ordering their preferences and acting consistently on them, will seize every opportunity in education, training, employment, entrepreneurship, finance, production and distribution to maximize their utility, without coercing others. A system that generates these outcomes is consumer sovereign in the sense that supplies maximize individual utility, and hence social welfare under the conditions specified. Bergson and Paul Samuelson have shown the "plausible" existence of a Pareto class of social welfare functions, which allows individuals to voluntarily employ the state to acquire public goods, and redistribute income and wealth. The simplest of these welfare functions democratically determines transfers.<sup>28</sup>

Kenneth Arrow, as is widely known, has demonstrated that elected representatives acting on behalf of many individuals cannot optimize as efficiently as individuals in Pareto market exchange. Consumer sovereignty therefore is not as ideal as one might hope, and the concept is under assault outside the economics profession by post-modernists who consider it a fig leaf for "capitalist" oppression, insensitive to progressive special interests and rights. But still Bergson argued that the democratic determination of public programs by elected officials is second best; that democratic free enterprise is likely to outperform its rivals.

This is the standard Sovietologists used to summarily appraise the merit of the Soviet Union, and is the best measure of "normalcy" consistent with the idea of the west. Although, as Bergson made clear, ordinal indicators cannot be used to compare competing Pareto efficient regimes, or inefficient systems, he argued that it was reasonable to infer that Pareto efficient economies or close facsimiles thereof were superior to regimes that severely degrade consumer demand. The solution isn't perfect, but it is far better than conflating authoritarian martial police states with normality, twisting logic to deduce that what is normal is good.

The PBA (Pareto-Bergson-Arrow) standard easily dispels Shleifer and Treisman sophistry. A nation that has no independent judiciary, no independent parliament, no parliamentary control over the secret services, no politically important independent media and a public sector ruled by the state, as Yavlinsky contends, cannot be democratic, no matter how closely it approximates other development norms. Likewise, a country, where a rent-granting autocrat creates and manipulates economic agents with market power for his own purposes in the name of lofty social purposes, cannot be workably consumer sovereign. Outcomes necessarily violate the western requirement that it is the people's preferences which competitively govern supply, not those of the authorities.

It is useful to bear PBA in mind as well when contemplating the future. For reasons obvious to every neoclassical theorist, Pareto efficient, consumer sovereign democratic free enterprise should surpass the social welfare performance of authoritarian regimes. Theory teaches that perfectly planned or perfectly mixed systems can also generate per chance Pareto optimal outcomes, but the Soviet Union has demonstrated the improbability of satisfactory outcomes. Since no liberal democratic

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<sup>28</sup> Bergsonian social welfare functions are defined in terms of the ethics of specific individuals, who judge the weights assigned each person's utility score. Although judges might find non-Paretian outcomes superior, Bergsonian social welfare functions prohibit them from coercing transactors. If judges are systems directors however, they can set transfers to maximize social welfare within this constraint. Bergson favored restricting their discretion further, arguing that transfers should be democratically determined. This rule has the virtue of simplicity, but may not always be superior to righteous counter-assessments.

economy is perfect, this presumption isn't conclusive. Nonetheless, it is impermissible to assert as Shleifer and Treisman do that Russia's future will follow the positive trajectory of "normal" westernizing democratic, market middle income countries when Russia isn't a member of this set. The land of Rus isn't Mexico or Argentina.<sup>29</sup> The Kremlin plying its own unique rent granting, "patrimonialist" course (Hedlund, 2005), has tried unsuccessfully to keep pace with the west for more than half a millennium without abandoning its Muscovite brand of authoritarianism (Maddison, 2003), and to date there is no sign of fundamental change despite Russia's return to pre-Soviet managed markets, (Rosefelde and Hedlund, 2006).

## 10. Conclusion

Russia is everything Shleifer and Treisman deny, and some of the fault lies with Shleifer in his capacity as Boris Yeltsin's advisor. It is an abnormal country, shaped by pre-Enlightenment forces which differ fundamentally from those of Mexico and Argentina. All non-Paretian systems aren't the same, and some like Russia degrade human welfare more than others, a judgment that can be easily verified by applying PBA, instead of normalizing the abnormal.<sup>30</sup> Beneath the mask Shleifer and Treisman craft, Russia is an authoritarian martial police state with a mixed inegalitarian, rent-granting economic system well suited to the Kremlin's traditional geopolitical aspirations, but incompatible with the ideals of the West.<sup>31</sup>

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<sup>29</sup> The IMF and World Bank fresh from failure with the Latin American debt crisis were assigned the Russian "transition" portfolio by the G-7. Its Latin American experts at the time quickly assured outsiders that Russia and Mexico were essentially the same system (Personal conversations with IMF experts in the nineties.)

<sup>30</sup> Policymakers of course aren't the only ones who knowingly glamorized Russia. The New York Times reporter Walter Duranty for example in September 1933 deliberately set himself the task of "discrediting" what he called the "campaign about the alleged famine." See Bertrand Patenaude, "Omelets, Eggs and Eggheads," *Wall Street Journal*, reprinted in *Johnson's Russia List*, No.8083, Article 30, February 24, 2004. Cf. Engerman, (2003), Rosefelde, (2003). Most of the "revisionist" political science literature, especially dealing with Soviet foreign policy, suffered from the same tendency to depict the Kremlin as normal, i.e., benign.

<sup>31</sup> Dmitri Trenin, "Russia: Far From Free," *Johnson's Russia List*, No.9117, Article 1, April 11, 2005. "Gorbachev's reforms put Russia on a path of reform and openness. But as the current Putin regime demonstrates, the country is still fundamentally tsarist and the Duma, like that of Nicholas II, docile and acquiescent."

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