

# The Political Economy of the Resource Curse in Russia

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**Abstract:** The resource curse is a concept that is becoming increasingly relevant to describe the politico-economic risk that Russia's natural resource wealth poses to its development. This article discusses this adverse effect of the fundamental resource industries on the politico-economic development of a country. It explores the degree to which this logic is particularly applicable to Russia. It also discusses the counterargument to this logic and provides some comments on the possible extrication from this undesirable development outcome.

**Key words:** development, natural resources, oil, regulation, resource curse

## Introduction

The idea of a resource curse is a well-visited concept in political economy. It suggests a causal link between the inability of an economy to grow and develop in accordance with classical economic growth theory and the abundance of the natural resources it possesses. The resource curse is used in conjunction with underdevelopment in the countries of sub-Saharan Africa and Latin America, among others.<sup>1</sup> In its generic formulation, the idea of a resource curse remains unpersuasive to some scholars due to its deterministic logic and, more important, its inability to cope with resource-rich countries that also have advanced economies. A particularization of the resource curse is the notion that the presence of petroleum and mineral wealth (fundamental natural resources [FNRs]) generally retards politico-economic development. Specifically, a state and economy dependent on these sources for its wealth is more likely to experience difficulties in developing both a democratic government and a market-based economy. This observation is true even when buttressed with anecdotal evidence from the Middle East, where there is an abundance of oil and few democratic regimes.<sup>2</sup>

This article explores this logic more carefully and assesses the extent to which this logic is applicable to Russia, as well as the degree to which this is a critical

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problem for Russian democracy. Russia is slightly different than other regions due to its unique transition from an industrialized command economy to a market-based one and from authoritarianism to democracy. Such transitions present unique challenges that can complicate the usual analysis.

There are some key economic indicators on the Russian economy that are rather illustrative (see table 1). If FNRs are defined as fuel, gas, oil, and metals, then the first line of table 1 suggests that between 1998 and 2005 the Russian economy increased its reliance on FNRs in exports from virtually two-thirds to more than three-quarters. This suggests that FNRs crowded out exports from other sectors of the economy. This is related, as would be expected, to the trends in the export price index and the price of Urals crude over this period. With export prices projected to increase markedly in the near future the incentive to curb the current composition of exports, or to increase earnings through increased efficiency, is further diminished.

There is also a strong correlation between petroleum production and the share of budget revenue from the gross domestic product (GDP).<sup>3</sup> While petroleum production continued to grow from 1998 to 2005, it must be remembered that the production level in 1992 (just over eight million barrels a day) was surpassed only in 2003. The record levels achieved in 1987 (more than eleven million barrels a day) are yet to be surpassed. By most estimates, Russia is unlikely to produce at that level before 2010.<sup>4</sup> Generally, the reason for this is the myopic and inefficient management of certain FNRs. The effect of insider privatization on the aggregate capital of stocks in privatized Russian firms is heavily debated. Such firms were often inefficiently large and thus a decline in capital stock may not imply that asset stripping and the tunneling of profits are necessarily to blame. Nonetheless, from 1998 to 2002, the capital stock growth in Russia was negative and is projected to be only moderately positive in the future.<sup>5</sup> This trend is bolstered by the data on gross fixed investments as a percentage of GDP, which are not increasing. While ostensibly rather incriminating, are such data truly indicative of the Russian economy suffering from a resource curse?

#### **FNRs and Politico-Economic Development**

The development of the adverse relationship between the FNRs and politico-economic development can be explained by the following five observations. First, FNRs have a generic tendency toward market concentration. The exploration, extraction, processing, and transportation of FNRs are economic activities amenable to scale economies and the erection of market barriers and, consequently, some of these functions are commonly recognized as natural monopolies. In the absence of a monopoly, the market organization of most of these activities around the world suggests a predisposition to an oligopolist market structure. Second, the crucial contribution to state coffers made by many FNRs, as well as their pivotal upstream position in the production processes of many industries, motivates the state to take an involved or direct role in their management and functioning. Third, the state and private sector nexus formed in the fundamental resource sectors promotes a demarcation between these sec-

TABLE 1. Some Key Production/Economic Indicators

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Fundamental natural resources/exports	67.43	68.43	71.53	65.50	66.34	64.46	69.76	77.34	—	—
Export prices (indexed to 1996)	81.07	73.99	93.94	87.45	83.50	94.03	113.27	142.60	158.70	162.70
Urals crude oil (US\$ per barrel)	12.02	17.34	26.97	23.12	23.76	27.07	34.09	50.19	—	—
Petroleum production (barrels per day)	6,088.4	6,124.5	6,492.0	6,990	7,622.5	8,453.8	9,210.8	9,430	9,750	10,050
Budget revenue (as %GDP)	11.4	12.6	15.4	17.9	20.5	19.5	20.4	23.8	21.9	20.8
Capital stock growth (as %GDP)	-3.20	-2.90	-2.00	-1.40	-0.30	0.50	2.10	2.00	2.00	2.30
Gross fixed investment (as %GDP)	16.15	14.39	16.86	18.89	17.92	18.37	18.31	18.18	18.40	19.50

Source: The Economist Intelligence Unit and International Energy Agency. Figures for 2006–07 are projected estimates.

Note: GDP = gross domestic product

tors and the rest of the economy, resulting in efficient market forces that are unable to direct activity in either. Fourth, the state's emphasis on the development of the fundamental resource sectors compromises the development of other sectors in the economy, which can hold back economic growth.<sup>6</sup> Fifth, due to an amalgamation of state interests and the interests of the fundamental natural resource sector, there is resistance to change the political and economic status quo. Something resembling an implicit contract evolves between these players and the rest of the economy. The contract is enforced by contributions from the major economic players to the state (in return for the state's protection) and the state's provision of the services produced by the FNRs to the domestic economy and to other nations (in return for support to the state).

This article develops this logic more explicitly and considers contrary viewpoints. However, it is necessary to understand that these observations are not made with the intent of implying a deterministic logic, whereby the presence of FNRs inevitably leads to adverse politico-economic development outcomes. The extent to which the FNRs affect politico-economic development depends on the degree to which a country is susceptible to their influence and, when it is, whether it is proactive in managing their influence.

### **The State as Rentier**

An illustrative place to begin this discussion is by revisiting the idea of a rentier state. While this concept is sometimes loosely applied, a rentier state is generally defined as a state that derives a significant portion of its budget directly from a few vital sources. Rentier states are characterized as being adverse to democracy because the state bureaucracy must intervene and regulate the market that generates its most significant source of income. For states that are commonly perceived as being heavily dependent on oil, such as those in the Middle East, the idea of a rentier state provides some insight into their political and economic environment.<sup>7</sup> These states cannot tolerate democracy because they must suppress any efforts that would diminish their control over the sector that sustains them. Double standards, which must exist for the state toward economic activity that affects their budget, discourage market-directed investment decisions and marginalize the political environment. Double standards in rentier states hamper both economic development and democratization. In the economic sphere, the primacy of the resource sector stunts the development of other sectors. For instance, innovation and technology in the rest of the economy (including the finance and service sectors, where it is most suited) lags behind the resource sector (where it is more specialized and thus less suited to generating economy-wide growth). Without innovation and technology, the specialization of the labor force, which is a necessary condition for the creation of an advanced market-based economy and democratization, cannot be accomplished.<sup>8</sup>

In postcommunist states that are in transition, this situation is further complicated by the primacy of many FNRs in the functioning of the anterior, predemocratic, and overly industrialized economy.<sup>9</sup> This motivates the state to take an involved role in these activities since, in such economies, the FNRs sector is able

to create network effects that have social, political, as well as economic ramifications, making it too risky for the state to give up control. This is a reason, beyond the motivation, that rentier states want to control the FNRs.

To understand this point more explicitly, recall the idea of a “virtual economy” in Russia, where there was a prevalence of barter and wage arrears during the late 1990s because production processes inflated the value-added at each stage and used these products, which had an artificially high value as payments to factors of production.<sup>10</sup> By this logic, the size of the Russian economy was perceived to be larger than it actually was. The *raison d'être* of this system was, however, the prevention of an industrial collapse that would have been socially devastating as numerous Soviet-era firms

either shut down or scaled back too rapidly. This would have risked derailing economic reform measures and destabilized the political arena precisely when a stable, somewhat democratic government was seen as more palatable than an unstable one, even if it were, perchance, more democratic.<sup>11</sup>

Theoretically, the material rel-

evance of this system to the FNRs is very direct because it was the gas, oil, and electricity industries—the most essential upstream components—that needed to be employed to feed the various industrial production processes. A virtual economy, therefore, is evidence that the government used many of the FNRs as subsidies for society and the economy.<sup>12</sup> For the various targeted production processes, the emphasis was not on providing upstream raw materials at the lowest marginal cost, but rather preserving a minimum level of output, even if this meant subsidizing the difference.<sup>13</sup> This was, of course, not done purely out of a desire to provide a social safety net, nor was it a benevolent social planner keeping the economy on an elaborate support system to give a truly market-based economy time to take root. Although those might have been some people's motives, there is ample evidence that the FNR-based subsidization of industry was in the self-interest of insiders (predominantly from the Soviet-era *nomenklatura*), who took advantage of loopholes in the transitioning economy and employed practices such as tunneling, asset stripping, and tolling with great effect.

### The State as a Regulator

There are two common interfirm situations that are used to provide some useful insight to the FNRs sector in economies in transition. The first situation is the contracting between the upstream and downstream industries, especially when both industries are characterized by high initial outlays and fixed costs, and when contracting between the industries requires installing additional specialized capital that has limited or no salvageable value.<sup>14</sup> Such capital has high specificity.

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Asset specificity introduces the risk of postcontractual opportunistic behavior, where one party deliberately holds up the other, after the contract is completed, knowing that the other party's bargaining power is diminished. Long-term contracts that provide an amelioration of market risk are preferable to shorter ones that incur substantial transactions costs in practice due to constant renegotiation. Although well-specified, long-term contracts are desirable, the parties involved would not want a situation where they are locked into unfavorable terms for an extended period of time. Solutions to this dilemma include vertical integration and intermediation by third parties.

The second situation pertains to ascribing a suitable set of access rights to competitors for the use of an essential network facility owned by a single owner. This situation is typical when a natural monopoly such as a railways operator, a telecommunications firm, or an electricity firm is deregulated. Competition is infused into the industry by separating the incumbent firm's ownership of the essential network (i.e., the rail-track network in railways or the PSTN in telecommunications) from its other activities; and by allowing competitors access to it in return for a predetermined fee, which helps recover the incumbent's investments in the network and the adequate maintenance of it. The most controversial aspect in this situation is the nature of the access regime that the regulator installs.<sup>15</sup> To encourage competition it must be fair to the competitors, but to ensure the proper functioning of the network and safeguard the industry's future, it must not distort the incumbent's incentives for investment in the network by encouraging under investment or, as is indeed sometimes the case, over investment in it.

While solely market-directed outcomes may not be agreeable in these two situations, the crux and substance of these issues is that solutions exist when the market is adequately bolstered by the state. Specifically, the adequate protection of property rights encourages market-based outcomes; a strong legal system enables market-based contracts; and, with an impartial regulator committed to enhancing competition, genuine deregulation can be achieved.

While Russia struggles to instantiate these support mechanisms with varying degrees of sincerity, the interim solution to both these problems is the interfacing of state and private sector interests. In the oil and gas industries, for instance, the transportation sector is fully state-owned. By virtue of the state's ownership of the essential network of trunk pipelines, it subsumes the role of the natural monopoly regulator. State ownership of the essential network might be positive, or at least not injurious to private-sector activity, to the extent that the state-owned network operator conforms to a set of access principles that are enforceable, transparent, and, above all, impartial. However, in the Russian context, the state, through its ownership of Rosneft and part ownership and considerable influence over Gazprom, remains a major player alongside other oil firms. Nevertheless, it maintains that access to the network is fully impartial and based only on output volumes. The Federal Antimonopoly Commission handles the bulk of competition and natural monopoly regulation related issues and the Federal Energy Commission, which operates through presidential decrees, handles access regulation for the oil, gas, and transportation sectors. The separation of roles, if not indicative of regulatory cap-

ture by private interests, allows these key FNRs to operate in a manner that is not entirely in confluence with the federal competition authority's perspective.<sup>16</sup>

### **The Counterargument**

There is an important counterargument to the resource curse: FNRs provide an impetus for economic growth in a developing economy. A developing country may experience low growth until a resource discovery spurs economic growth.<sup>17</sup> This idea is based on the big push literature, which suggests that with imperfect competition and interconnectedness across sectors of an economy, adopting technologies that lead to increasing returns to scale in one sector will allow industrialization of the economy through a general increase in demand and improvement of infrastructure.<sup>18</sup> Relatedly, growth in resource-rich countries may primarily be due to foreign direct investment (FDI). Note, however, that growth via a big push is rather distinct from growth through FDI activity alone that eventuates in a resource-rich country where real disposable incomes are higher and perhaps even a degree of tariff protection exists. Genuine big-push growth is more multidimensional (it includes some FDI) than purely FDI-led growth especially when, as in Russia, the bulk of FDI is in a few key sectors.<sup>19</sup>

In the case of Russia, a number of economic indicators, including growth rates, consumer spending, and the federal budget, are tightly related to the global price of oil.<sup>20</sup> Despite this, however, any argument favoring the notion that Russia might be on its way to enable a big push in its economy and enjoy faster rates of economic growth is weak. One of the requisites for a big push (that is currently lacking in Russia's FNR) is the investment in and adoption of newer technologies. Some of Russia's FNR oligarchs are restructuring, which may eventually allow Russia's FNR sectors to become a genuine engine for growth.<sup>21</sup>

More important, the link between a big push and the FNRs is frustrated by the Dutch disease, or the phenomenon that exports in FNRs make other tradable manufactured good less competitive via an appreciating exchange rate, which promotes deindustrialization in nonexport sectors. Russian exports are gradually becoming dominated by the FNRs. FNRs are tradable commodities and, therefore, in contrast to nontradables, are unable to provide the fillip for symbiotic development across all sectors.<sup>22</sup> The worrisome problem is that ridding an economy of the Dutch disease is especially arduous because it involves implementing policies that curtail the sector that feeds the state's coffers.<sup>23</sup> It also involves implementing far-sighted policies that assist the non-FNR sectors in adopting new technologies so they do not lag behind.<sup>24</sup>

Auty argues that the resource sector only provides a spurt of short-term, construction-related economic growth and thereafter the effect stops.<sup>25</sup> However, after a period of sensible technological improvement and capital accumulation in the pursuit of scale economies, the resource sector boosts long-term economic development. This strategy is especially suited for larger countries with better integration across sectors and where larger FNR firms resist squandering away their advantage through X-inefficiency (inefficiency arising from complacency afforded by a dominant market status).

It is clear that if FNRs are the principal source of development in a country like Russia, to make this strategy sustainable, the sector would need to be regulated and operated in a sensible manner. Modernizing the FNR sector and its regulatory bodies; better integration with other manufacturing industries; and, most important, explicit policies that enable the modernization and development of other manufacturing sectors are some of the policies that Russia needs to implement to avoid becoming an FNR-dominated economy. Politically, there is a need for market-based regulation of the FNR sector and extrication of the state from FNR politics to prevent the FNRs from becoming the carrot one day and the stick the next in relations with other domestic manufacturing sectors and international trading partners.<sup>26</sup>

### The Way Forward

In assessing the way forward it is helpful to see whether it is possible to make a clean break from the current situation. To see why this is fraught with difficulty let us begin by revisiting some well-known concepts. The first is Schumpeter's idea of creative destruction, which suggests that an entrepreneur is most innovative when he sees the market approaching some form of stability. These "innovations" are intended to steer the market away from equilibrium, thereby affording the entrepreneur an opportunity to profit.<sup>27</sup> The political counterpart of this idea is best embodied in Riker's politician, who employs heresthetics to manipulate the political issue space without offering any real preferable choices.<sup>28</sup> The political economy in such a country would naturally evolve in a staccato manner, with the incumbents resisting change to maintain the status quo at all costs. Any change that occurs is only a by-product of the innovations used by incumbents and the policies used by political entrepreneurs to avoid any radical shift from the status quo, where the challengers might be new entrepreneurs, politicians, or incumbents that have more to gain by leaving the system and joining the ranks of rivals.<sup>29</sup> Periodic change does not signal a genuine shift in the overarching paradigm of the system.

The organizational structure of Russia's FNRs and their relation to the political elite mimics the logic of such creative destruction. Firms are constantly changing the boundaries of their influence to survive and maintain their place in the market. The hallmark of oligarchy is the presence of political entrepreneurs. A fundamental problem with oligarchy is its immunity to extrication due to the vested interests of the incumbents who profit from a partially reformed outcome.<sup>30</sup> The erection of entry barriers in politics and in the market results in stagnation.<sup>31</sup>

Given this context, reforming the FNRs in Russia is problematic because it unabashedly displays the original sin of the political economy of regulation—that of regulatory capture. Although it is evident that market-based regulation is desperately required in Russia, and that policies such as setting up regulatory bodies to oversee the natural monopolies, implementing access systems, and so on are a step in the right direction, genuine change will remain elusive.

### NOTES

1. Richard M. Auty, "Industrial Policy, Sectoral Maturation, and Postwar Economic Growth in Brazil: The Resource Curse Thesis," *Economic Geography* 71, no. 3 (1995):



257–72. Auty uses this idea in conjunction with Brazil by suggesting that the resource sector finances autarkic development but is unable spur reform due to resistance by vested interests. Jeffrey D. Sachs and Andrew M. Warner provide a cross-country empirical investigation in “Natural Resource Abundance and Economic Growth, Development,” NBER Discussion Paper no. 5398 (1995). NBER. <http://www.nber.org/papers/w5398> (accessed on July, 30, 2006).

2. Michael L. Ross, “Does Oil Hinder Democracy?” *World Politics* 53 (2001): 325–61. Ross provides a comprehensive assessment of the relationship between FNRs and democracy using some simple empirical work that also considers the concomitant impact of cultural history, income levels, and religion. He draws much of his causal argument from work done on the Middle East. For a survey of six countries that fail to convert oil discoveries into sustained economic growth due primarily to ill-conceived investment of oil revenue and macroeconomic mismanagement. Alan Gelb, *Oil Windfalls: Blessing or Curse?* (Oxford: Oxford University Press for the World Bank, 1988).

3. Peter Rutland, “Russia’s Oily Economic Growth,” *Eurasia Daily Monitor* 2, no. 158 (2005). Rutland cites Hokkaido University’s Shinchiro Tabata, who suggests that a dollar increase in the price of oil contributes \$1.86 billion to the Russian federal budget.

4. For a comprehensive review of petroleum output estimates for the future including the IEA and official Russian and private sector estimates, see Sadek Boussena and Catherine Locatelli, “Towards a More Coherent Oil Policy in Russia?” *OPEC Review: Energy Economics & Related Issues* 29, no. 2 (2005): 85–105. By most estimates cited by these authors, Russia is unlikely to exceed the 1987 figure even by 2020.

5. It is moderate, especially when compared to China or India, where these figures are closer to 10 percent.

6. Broadly, this is the logic behind the idea of a “Dutch disease.”

7. See Hazem Beblawi and Giacomo Luciani, *The Rentier State* (London: Croom Helm, 1987).

8. See Seymour Martin Lipset, “Some Social Requisites of Democracy: Economic Development and Political Legitimacy,” *American Political Science Review* 53 (1959): 69–105; and the literature on the modernization theory generally. For an analysis on the effect of increasing specialization of the labor force as a contributory factor in explaining why oil-based states fail to democratize, see Ross.

9. Jan Winiecki, *The Distorted World of Soviet Type Economies* (Pittsburgh: University of Pittsburgh Press, 1988).

10. See Clifford G. Gaddy and Barry W. Ickes, “Russia’s Virtual Economy,” *Foreign Affairs* 77, no. 5 (1998): 53–67; and other papers by the same authors on the subject of the virtual economy.

11. For an elaboration on this view, see Andrei Shleifer and Daniel Treisman, *Without a Map: Political Tactics and Economic Reform in Russia* (Cambridge: MIT Press, 2000), and Prateek Goorha, “Opening the Black Box: Understanding the Russian Economy,” *Communist and Post-Communist Studies* 34 (2001): 401–22.

12. Barnes makes the interesting observation that FNR-related sectors in 2002 are predominantly characterized by vertical integration (or what he terms deep business groups). His explanation is that such organization serves as a defense mechanism against takeovers from creditors along the production process. Of course, vertical integration also rids the virtual nature of the production process by internalizing the flow of credit to a single business group. Andrew Barnes, “Russia’s New Business Groups and State Power,” *Post-Soviet Affairs* 19, no. 2 (2003): 154–86.

13. This forced involvement of upstream resource industries by the government created, in essence, a case of excessive “virtual integration” in the production processes whereby upstream resources come at higher marginal cost than they would with purely market-directed outcomes.

14. For the interested reader, a seminal contribution to this vast body of literature is Benjamin Klein, Robert Crawford and Armen Alchian, “Vertical Integration, Appropriate

Rents, and the Competitive Contracting Process,” *Journal of Law and Economics* 21 (1978): 297–326.

15. As a representative article in this area, see J. J. Laffont and J. Tirole, “Access Pricing and Competition,” *European Economic Review* 38 (1994): 1672–1710.

16. Interestingly, the Federal Antimonopoly Commission brought the Federal Energy Commission, along with Gazprom, to court in 2003 for not following access pricing practices, per Russian competition law.

17. The idea, though similar in logic, is independent from the credible commitments literature in development economics that suggests how some developing countries experience a vicious circle of poor economic performance due to macroeconomic mismanagement by the government, which results in investors losing confidence.

18. A review of this literature can be found in Kevin M. Murphy, Andrei Shleifer, and Robert W. Vishny, “Industrialization and the Big Push,” *Journal of Political Economy* 97, no. 5 (1989): 1003–26.

19. The 2005 AT Kearney FDI Confidence Index report suggests an improvement of Russia’s attractiveness as an FDI location. However, it also notes that the bulk of investment has been in energy as well as automobiles and retail.

20. See, for example, Fiona Hill, “Energy Empire: Oil, Gas and Russia’s Revival,” (published in 2004 by the Brookings Institution’s Foreign Policy Center) <http://www.brookings.edu/views/articles/hillf/20040930.htm> (accessed on July 30, 2006). Hill also mentions that the performance of other major FNRs, such as steel, is correlated to the health of the oil sector.

21. For a brief synopsis on a generously objective view on the state of the Russian economy and its private sector, see Andrei Shleifer and Daniel Treisman, “A Normal Country: Russia after Communism,” *Journal of Economic Perspectives* 19, no. 1 (2005): 151–74.

22. For an excellent development of this argument, see Sachs and Warner.

23. Interestingly, this was the intended purpose of Norway’s Government Petroleum Fund established in 1990 with the explicit purpose of using oil revenue to help achieve long-term objectives for the economy. The fund also invests abroad to help create exchange-rate stability and prevent the mechanism behind the Dutch disease.

24. For example see Sweder van Wijnbergen, “The ‘Dutch Disease’: A Disease After All?” *Economic Journal* 94, no. 373 (1984): 41–55.

25. Richard M. Auty, “The Economic Stimulus from Resource-Based Industry in Developing Countries: Saudi Arabia and Bahrain,” *Economic Geography* 64, no. 3 (1988): 209–25.

26. Balzer has discussed Vladimir Putin’s thesis on the issue of the role of the resource sector in the Russian economy. While modernization of the sector and investment in it is a theme that recurs so does the theme of the principal role of the energy sector in the development of the Russian economy for the foreseeable future. He advocates the creation of vertically integrated firms and firms that are integrated with financial institutions that are closely managed by the state and that provide the engine for the economy’s growth. He suggests better and closer regulation of the industries by the state but reiterates that purely market-based governance of the sector is unadvisable for Russia. Harley Balzer, “The Putin Thesis and Russian Energy Policy,” *Post Soviet Affairs* 21, no. 3 (2005): 210–25.

27. See Joseph Schumpeter, *Capitalism, Socialism and Democracy* (New York: Harper and Row, 1942).

28. See William H. Riker, *The Art of Political Manipulation* (New Haven: Yale University Press, 1986). For a rigorous and insightful presentation of this logic in a democratic state see A. Wuffle, Scott Feld, Guillermo Owen, and Bernard Grofman, “Finagle’s Law and the Finagle Point, a New Solution Concept for Two-Candidate Competition in Spatial Voting Games without a Core,” *American Journal of Political Science* 33, no. 2 (1989): 348–75.

29. In the context of Russia’s experience see Lilia Shevtsova, “Russia’s Hybrid Regime,” *Journal of Democracy* 12, no. 4 (2001): 64–70. This article suggests Russia’s

bureaucratic quasi-authoritarian regime is willing to make reforms that further empower the executive rather than the society.

30. For an elaborate treatment of this effect, see Joel S. Hellman, "Winners Take All: The Politics of Partial Reform in Postcommunist Transitions," *World Politics* 50, no. 2 (1998): 203–34.

31. Interestingly, Acemoglu suggests that if taxes under democracy are higher and the distortions caused by entry barriers in the market are low then oligarchy can be more efficient than democracy. However, he notes that as the comparative advantage in entrepreneurial ability shifts from the incumbents to rivals its performance falls behind that of a democratic society. Daron Acemoglu, "The Form of Property Rights: Oligarchic vs. Democratic Societies," NBER Working Paper no. 10037, (2003). NBER. <http://www.nber.org/papers/w10037> (accessed on July 30, 2006).