

DISSERTATION

THE ROLE OF INFORMAL INSTITUTIONS IN THE TRANSITION: HOW
HOUSEHOLDS IN KRASNODAR, RUSSIA ARE COPING WITH CHANGE

Submitted by

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In partial fulfillment of the requirements

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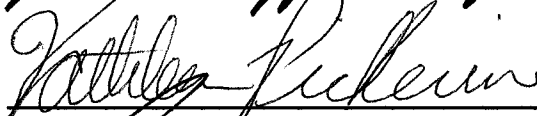
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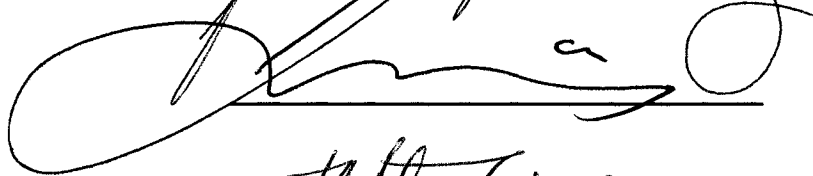
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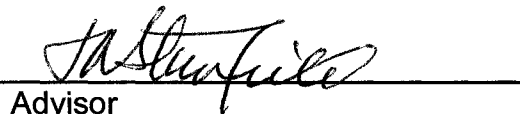
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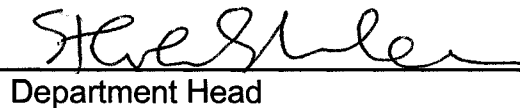
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ABSTRACT OF DISSERTATION

THE ROLE OF INFORMAL INSTITUTIONS IN THE TRANSITION: HOW HOUSEHOLDS IN KRASNODAR, RUSSIA ARE COPING WITH CHANGE

The events of 1989-91 began a period of transition in Russia that called for the overthrow of the Soviet model and adoption of a Western-style market system. To provide expertise on the events, policymakers recruited transition consultants sympathetic to the arguments of neoliberalism. This approach is predicated on the idea that instituting appropriate formal rules will be sufficient to create an environment supportive of competitive market development. However, the results of this approach have varied widely as to stabilization, growth, and efficiency. This non-uniform development challenges the neoliberal view of transition because the same formal rules did not produce the same results.

A new research agenda has surfaced that is evolutionary-institutional in nature which seeks to resolve the anomaly of variegated performance and contribute to understanding socio-economic change in general. This agenda is founded on the view that changing the formal rules of the game, difficult as this may be, is not sufficient. The informal rules of the game, the customs and norms of the social order, interact with formal rules and are, therefore, critical to the operation of the economy.

This study is focused on Russia, whose socio-cultural legacy suggests that informal rules significantly influence behavior and, in fact, may dominate formal rules in the decision-making environment. Therefore, transition analysis must consider Russia's informal institutions in order to render more complete explanations. In fact, the majority of analyses fail to consider these informal dimensions and the evolution of institutions within a socio-cultural context.

This study seeks to address this limitation by contributing to the ethnographic information on Russia. Of course, comparative analyses of the nature and effects of informal institutions on the transition process is needed, but before this analysis can proceed careful compilation of data is required. To promote this, a qualitative interview study was conducted in Krasnodar, Russia which focused on the role of informal institutions in the transition. This research is significant as it applies and extends established research in the economics discipline. In addition, it contributes generally to identifying the interaction between formal and informal institutions as part of an ongoing effort at cultural mapping.

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DEDICATION

For David Snider

I was lucky to have known you.

NOTE ON TRANSLITERATION

The transliteration of Russian words follows the Library of Congress system. Soft signs and hard signs from the Russian language are recognized with one and two apostrophes, respectively.

General exceptions have been made for accepted Western spelling of names (i.e. Yeltsin, rather than El'tsyn).

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Chapter 1: Introduction

The events of 1989-91 ushered in a period of transition that called for the overthrow of the Soviet model and adoption of a Western-style market system. To provide expertise on the events, policymakers recruited transition consultants sympathetic to the arguments of neoliberalism and the belief thereof that there is only one set of laws within which a market economy will operate. Moreover, this view seems convinced that Rational Economic Man will emerge spontaneously and quickly if these laws are in place. However, despite designing broadly similar policy packages, the results of this transition approach have varied widely as to stabilization, growth, and efficiency. This non-uniform development challenges the neoliberal prediction that the same formal rules will produce the same results. This suggests neglected factors were at work during the transition period. Furthermore, it suggests that these neglected factors have the potential to significantly affect economic performance.

Hence, a new research agenda has surfaced that is evolutionary-institutional in nature; this research seeks to resolve the anomaly of variegated performance and contribute to understanding socio-economic change in general. This agenda is founded on the view that changing the formal rules of the game, difficult as this may be, is far from sufficient. The informal rules of the game, the customs and norms of the social order, interact with formal rules and are,

therefore, critical to the operation of the economy. To illustrate this argument, this research work presents the results of an ethnographic field study conducted in the Russian Federation between October 2003 and March 2004.

This chapter provides the reader with an introduction to the theories, ideas, and arguments that will be discussed in subsequent chapters. To provide historical context, the rise of neoliberalism is first discussed, followed by a brief recounting of the events leading up to the collapse of the Soviet regime. Then, the shock therapy reform strategy is introduced. Following this is a discussion of institutions and the transition, as well as the introduction of a contrary reform strategy with institutions and the process of institutional change as its basis. After this, the reader is introduced to the methodology of the field study and is provided with a preview of its results.

1.1 An Introduction to the Neoliberal Agenda

Economic actors at all levels are currently in the midst of positioning themselves in markets that are now largely global in scale. Aided by a variety of factors—advances in technology and communication, reductions in trade barriers, and the development of capital markets among them—the rules of the game are rapidly changing. Within this movement a powerful agenda has surfaced which promotes a preferred politico-economic structure—a set of guidelines by which individual economic systems should operate. These guidelines have the market mechanism as their base; the market serves as the primary means by which individual activity is coordinated.

The overarching theoretical assumption of this neoliberal agenda is that the market, as the primary and superior coordinating mechanism, will transmit the appropriate information for economic actors to use in decision-making. With this (symmetric) information, individual actors are expected to act in rational economic self-interest to maximize a specified objective function. The ultimate economic outcome, given the incentives of the market, will achieve all possible efficiency gains and, therefore, superior economic performance. However, this result can only occur under a set of formal rules that allow for the unhindered development of competitive markets.

The neoliberal agenda's popularity and persuasive power began its rise in the 1980s as the world recovered from the supply shocks and stagflation of the previous decade. The deregulation regimes of U.S. President Ronald Reagan and British Prime Minister Margaret Thatcher, the debt crises of Central and South America, and the increasing power of international aid agencies all contributed to the advancement of neoliberal principles. Power was thus concentrated in the hands of advocates of the free market and their belief in the market's ability to promote efficiency, growth, and stability.

In connection with the rise of neoliberalism, a major shift was taking place in the 1980s in the Soviet Union. Popular criticism of the centrally planned system escalated both inside the system and from external sources. Assisted by advances in technology and communication which served to disseminate information into previously sheltered areas of the Soviet Bloc, pressure mounted against central planners to open their economies to the power of the free market.

1.1.1 Soviet reforms in the 1980s

Facing declining growth rates, Gorbachev acknowledged that the historical legacy of the Soviet system resulted in a “lack of inner stimuli for self-development” in Soviet enterprises which depressed Soviet economic performance (Gorbachev 1988, 71). He sought to reform the system from within through his *glasnost* (openness) and *perestroika* (restructuring, rebuilding) reform programs. These reforms aimed to improve Soviet economic performance by such measures as legalizing some small business, increasing the autonomy of enterprises, and encouraging enterprises to operate within a hard budget constraint.

Gorbachev's attempts at reform were generally unsuccessful and the decline of the Soviet economy continued. More radical reform was called for and in 1990 a committee was formed to determine a process by which a market-based system could be established in the Soviet Union. In *500 Days: Transition to Market*, a plan was outlined to replace the system of central planning with private property and free market prices (Yavlinsky et al. 1991). Russia's government under the leadership of President Boris Yeltsin strongly advocated the radical plan and the Supreme Soviet of Russia voted to approve it. However, Gorbachev continued to resist radical reforms and subsequently rejected the strategy outlined in *500 Days* (Kennett 2001, 496).

Over the course of the next year, Yeltsin and his cohorts for radical reform continued to amass popular support while support for Gorbachev dwindled. Reform legislation was adopted by both central and republic governments that

addressed such things as property ownership, ownership and disposition of land, operating rules for enterprises, promotion of small business, prevention of monopoly and de-monopolization, establishing a Western-style central bank and a commercial banking system, creating a uniform system of business profit taxation, setting up joint-stock companies and a securities market, and general conditions for investment and employment (Schroeder 1991, 463).

In August 1991, Gorbachev, largely assisted by Yeltsin, withstood an unsuccessful coup attempt by Communist Party leaders. However, Gorbachev ultimately could not maintain hold of his position and the legal breakup of the Soviet state soon followed as the constituent republics began to declare independence. On December 25, 1991, Gorbachev resigned as General Secretary and the Soviet Union ceased to exist (Kennett 2001, 496).

1.2 An Introduction to Shock Therapy

Following the collapse of the Soviet system, the reformers and their international and Western advisors, sympathetic to neoliberal arguments, advocated a series of reforms designed to transition the Soviet Bloc's centrally planned economies into free market systems. The defining elements of the end-state envisaged by reformers were: (1) generally free, market-determined prices; (2) generally independent firms, motivated by economic considerations; (3) a significant, if not predominant, role for non-state property; (3) industrial regulation in the place of industrial planning; (4) generally hard currency; and (5) a modern

financial system, including commercial banking, exchanges and other financial intermediaries (Ericson 1991, 23).

The neoliberal transition, so-called “shock therapy,” is predicated on the belief that the same formal rules will produce the same results. Based on the behavioral assumptions of neoclassical microeconomic theory, the targets of reform were the formal rules of the economy which provide the explicit parameters under which economic exchange takes place. These rules were to be altered to create a decision-making environment appropriate to a market-based system. Furthermore, it was argued that the interaction between the economy and polity meant that this could only be accomplished through simultaneous change of both the economic and political systems in transition countries.

A number of countries that used this reform strategy had similar initial experiences of hyperinflation and GDP collapse at the transition’s onset. In subsequent years, however, the results of this approach have varied widely as to stabilization, growth, and efficiency. It is now clear that some countries have been relatively more successful at marshaling functioning market economies. In others, the development of markets has faltered and human and social costs remain high. This non-uniform development challenges neoliberalism and its assumptions of universality. As a result, criticism of the neoliberal agenda has accelerated over the last several years (e.g. Stiglitz 1999; Florio 2002). Thus, the shock therapy paradigm has suffered a crisis along the lines of Kuhn (1970), inspiring a search for alternate explanations.

1.3 An Introduction to Institutions

A contrary research agenda is focused on examining why the post-socialist experience differs between countries. For answers, this agenda takes a non-orthodox approach to economic analysis. Drawing many of its arguments from institutional economic thought, this theory is evolutionary-institutional in nature and hence very critical of shock therapy. In this approach, the assumptions and methods of neoliberalism and shock therapy are challenged. Particular focus is given to critiquing shock therapy's treatment of the institutional structure of society.

More specifically, the institutional environment is argued to consist of both formal institutions and informal institutions (North 1990, chs. 5 and 6). Economic actors respond to the incentives provided by both institutional types. Both are humanly-devised constraints; however, only formal institutions are subject to top-down reform efforts. This is because formal institutions consist of the devised, explicit rules of the game—the laws, policies, and economic rules which require, permit or prohibit certain behaviors. In contrast, informal institutions are the culturally specific, implicit rules of the game—the norms of behavior, codes of conduct, and conventions that guide individuals in their interaction with others. These norms are pervasive, habitual, and resistant to change to a much greater extent than formal rules (North 1990, 45). Therefore, they are not subject to reform efforts in the same way as formal rules.

1.3.1 Institutions and the Transition

At the heart of the evolutionary-institutional analytical approach is the acknowledgement that the embeddedness of the economic sphere within larger society means the transition is not just a change in the economic system, but is a holistic change of the socio-cultural framework. Widespread changes in both formal rules and informal norms are required for the system to structure and operate as a market-based system. Acknowledging this role for informal institutions thus leads to the argument that informal institutions in transitioning countries can serve to either facilitate or impede the transition.

Therefore, the evolutionary-institutional approach criticizes the neoliberal agenda, noting that it suffers severely in practice from its neglect of institutions. Specifically, the shock therapy approach to reform is hampered by its assumption that behavior appropriate to a market system—the day-to-day, often informal, institutions of the market economy—will emerge spontaneously if the state changes the formal rules of economic life and then for the most part stays out of the way.

It is now becoming clear that conventional transition analysis cannot explain divergent experiences without ad hoc attention to issues such as culture and history. In fact, the majority of transition analyses do fail to consider the socio-cultural dimensions of the economy and the evolution of institutions within a socio-cultural context; this analytic neglect is a major limitation. Therefore, careful studies are needed to account for the “patterns of interaction” among the different spheres of society (Arensberg 1957, 100).

1.4 An Introduction to the Research Study

In consideration of the above, research focusing on informal institutions can provide a more complete picture of the Russian transition environment. However, this area is significantly underrepresented in the transition literature. Therefore, it was decided that analysis of the role of informal institutions in the transition could, potentially, make a significant contribution. To this end, a study was carried out with this pursuit in mind.

1.4.1 Goals and Contribution of the Study

In any society, regardless of the degree of heterogeneity, it is possible to identify common behavioral traits resulting in an institutional framework specific to that place and time. These traits may emerge from the larger cultural environment; for example, what it means to be “a Russian,” and the common behaviors that ensue regardless of socio-economic strata. In addition, group-specific traits will emerge within a socio-economic stratum. For example, the experiences of a “rich Russian” may often differ from those of a “poor Russian” due to situations and circumstances specific to the different socio-economic classes. In these instances, common behaviors may emerge in response to challenges unique to that stratum.

The events which ensued following the collapse of the planned economy resulted in a sharp class distinction in 1990s Russia which continues today. The upper and lower echelons of society have had quite different social and economic experiences during this time. While a small element of society has

achieved economic prosperity, the majority of Russians have experienced economic upheaval and hardship. The overarching goal of this research study is to contribute to an assessment of the workings of the market economy through discovery of the emic experiences of these “ordinary” Russians who bear witness to the changes. The focus of the study is, therefore, on the presence, development and functioning of informal institutions in the day-to-day operations of ordinary men and women. In this study, patterns in attitudes and behavior are identified which help define the transition’s institutional environment.

By recording the study of cultures, ethnography produces descriptive work. By its very nature, therefore, ethnographic studies produce information regarding the set of informal institutions as they provide descriptions of the cultural context within which economic exchange takes place. As such, an ethnographic approach was deemed particularly appropriate for this research work. More specifically, it was decided that direct discussion with involved participants would provide the richest source of data. Thus, ethnographic social research was undertaken using an exploratory field study. To wit, those directly affected by the transition will explain what it means to subsist in contemporary Russia.

1.4.2 Contribution to the Literature

Economic literature is, generally speaking, biased towards the collection of statistics in pursuit of quantitative analysis. The abundance of econometrical studies has made the pursuit and publication of in-depth, qualitative research

secondary. There is a particular gap in the literature with respect to field studies, an approach commonly left to fellow social sciences such as anthropology and sociology. However, while economists can, and should, draw on research in the other social sciences, there is a role for the economist-ethnographer.

Field studies present a valuable opportunity to contribute dimension to economic research where such dimension might easily lie beyond the capture of statistics. Particularly, it is the pursuit of understanding the role of informal institutions that can escape quantitative studies as this knowledge is often buried in deeper context. The qualitative nature of this study is designed to capture exactly such insights on current phenomena and trends that are poorly reflected through statistics.

With respect to the transition literature, field studies provide a significant and particularly unique contribution. First and foremost, they add to the fund of ethnographic information on Russia—knowledge vital for understanding the intricate complexity of any economic system and certainly the complexity surrounding system change. Second, field studies promote the role of the area specialist in transition analysis. The inextricable linking of the economic sphere with the larger environment requires analysts who possess multi-dimensional knowledge. Lastly, as noted above, qualitative research of this nature allows for direct observation of informal institutions. These institutions play an important role in the functioning of the post-Soviet socio-economic system. Therefore, transition analysis must directly address this element and the knowledge of such can often only be accessed through field studies.

1.4.3 Mental Models, Ethnography, and Informal Institutions

At its base this research work is an exploration of mental models—the tools used by economic actors to explain and interpret their external reality. More specifically, this work critiques the deductive rationality of neoclassical economic theory. Instead, what is argued is that real-world complexity of decision-making may cause deductive rationality to fail; human rationality thus becomes bounded (Arthur 1994, 406). To address this complexity, economic actors search for patterns to simplify the decision at hand. These patterns, or mental models, are used to assist in decision-making by bridging gaps in information and cognition.

As part of this process, economic actors receive feedback from their interaction with others. This feedback forms the process of institutional change (North 1991, 5). If their actions are consistent with the actions of others, a mental model is positively reinforced. If they are inconsistent, this implies a mental model is inappropriate or in need of alteration. In the case of the latter, a model will be improved upon or replaced with a substitute model more appropriate to the explanation at hand. However, hysteresis may occur when agents retain a mental model because it has proven itself apt in the past and must show a record of failure before it is discarded and replaced (Arthur 1994, 407). In addition, the absence of error can also lead to adaptation of a mental model if the agent takes the absence of error as a signal to improve the success of the model (A. Clark 1997, 281). Furthermore, mental models can be

transferred from one actor to another as communication leads to shared mental models (Arthur 1994, 408; Denzau and North 1994, 15; Mantzavinos 2001, 68).

As noted above, beginning in 1991 Russians were faced with the challenge of adapting to new rules of the game. During this process, the wide variability in information access means that, for many, decision-making takes place in an environment of significantly incomplete information. In addition, lack of historical precedent implies that computational ability appropriate to a market-based system may be asymmetric as well. As a result of the increased uncertainty, the mental models used by economic actors have had to adapt to the challenges faced in contemporary Russia.

The goal of the study is to identify how Russians are responding to the changes that have taken place since 1991. In-depth, in-person interviews were conducted in which participants were asked questions addressing a number of different topics. To briefly summarize, the questions fall into eight general groups: day-to-day functioning, structure of communities, networks of friends and family, the household's economic situation, views towards authority, subjective well-being, cognitive competence, and vision of the future. An English-language version of the full interview guide is attached as Appendix A.

1.5 An Introduction to the Research Results

In the chapters which follow, research results will show that the participants in the sample do not use the relatively simple and straightforward mental model assumed by the neoliberal agenda. In contrast, they possess

multiple partial models (A. Clark 1997, 270); these models are used to interpret the institutional environment of the transition. This study is an exploration of that environment and, more specifically, how Russians are explaining the new rules of the game to themselves. In sum, the researcher wishes to show to what extent the study participants are adapting to the economic changes and to what extent they are resisting those changes.

Following analysis of participants' responses, a number of patterns emerged. What quickly becomes apparent is that in contemporary Russian society there exists a curious blending of two systems. Native interpretations of the market system have led to old norms being abandoned in favor of new. However, certain aspects of the Soviet cultural ethos remain. As this discussion progresses, some questions to keep in mind include: Given the contradictions presented between the planned and market system, does lack of experience matter? Is there a lingering Soviet legacy that conflicts with the development of a market system? What is the extent of layperson adaptation to the system change? And, are Russians following "rules" or "norms"?

Much of the explanation of this duality lies in institutionalist arguments surrounding the process of institutional change. Evolution of systems proceeds unevenly. Some areas may lag in their adaptation, while in others change proceeds rapidly. Importantly, the pace of change depends on whether social norms and conventions support formal rule changes. As such, economic agency is critical to this process. Results, therefore, reinforce the institutionalist arguments that will be presented in this research work.

1.6 Conclusion

This chapter has provided the general historical context to the shock therapy reforms which began in Russia in 1991. In addition, several concepts and arguments were introduced which will be expanded upon in the chapters which follow. Chapter 2 provides the reader with information regarding the shock therapy approach to the transition. The intellectual foundation of shock therapy—the assumptions and predictions of neoclassical economic theory—is briefly discussed. In addition, the shock therapy approach to reforms is summarized, as is its application specific to Russia. As will be detailed in chapter 2, the application of reform strategies generally did not produce the results predicted by shock therapy's assumptions. This is due primarily to two major factors: (1) a lack of clarity in rules which has led to a series of power struggles in which reform attempts have been thwarted, or in which reforms have been modified from their original purpose to instead benefit certain interests; and (2) economic actors' refusal to play by the new rules, often due to the persistence of norms from the Soviet period.

Chapter 3 provides a contrast to shock therapy in the form of an alternative evolutionary-institutional approach to the transition. The intellectual foundation of the evolutionary-institutional approach—institutional economic thought—is briefly presented. Following this, the strategy of transition reform from the evolutionary-institutional perspective is outlined. In addition, elements of the evolutionary-institutional approach are used to explain some of the problems encountered in the shock therapy approach. The crux of the

evolutionary-institutional critique is that the shock therapy reform strategy fails to adequately consider the role of informal institutions in the process of institutional change. This analytical neglect resulted in unforeseen interference in the reform process. For example, resistance to change by the status quo and advantageous rent-seeking on the part of interested parties.

Chapter 4 provides the reader with additional methodological information regarding the research study. The process undertaken for the field study is detailed, as is the method of data analysis. In addition, specific information is given regarding the structure and content of the questionnaire. The location of the field study is also described. Lastly, the reader is presented with some important demographical data of the study's participants.

Chapters 5, 6 and 7 present the analytical results of data generated by the study. Three prominent themes are identified in the research results, each addressing a different aspect of the informal institutional environment. In chapter 5 the role of social relationships in the transition is analyzed. It will be shown that participants actively seek to reduce uncertainty or its impact through the use of social networks in a variety of capacities. These relationships are a vital element in Russian society used both to explain and adapt to new rules as well as to circumvent them. In chapter 6 the cultural preparedness of participants is assessed. A key transition issue remains as to whether the ongoing adaptation is preparing agents for economic activity within market rules. In many ways, cultural preparedness for market-based exchange remains incomplete while in other ways values are adapting to be more consistent with a market-based

system. In chapter 7, corruption and the pro-bribery culture in contemporary Russia are discussed. This discussion concludes that pre-existent mental models continue to distort and delay implementation of formal rule changes. This is due primarily to the ineffectiveness of authorities charged with implementing formal rule changes, thus leading to a culture in which market transparency is challenged.

Chapter 8 concludes this research work with a summary of the arguments presented in previous chapters. In addition, the research is critiqued with respect to its significance and limitations. Following this, the field study is placed in the context of its foundation as part of a larger project—an attempt at developing a holistic description of the transition through a process of pattern modeling—and ideas are presented for future paths of research.

Chapter 2: The Shock Therapy Approach

Following the collapse of the Soviet Union in 1991, the goal of Russia's reformers was to transform the command planned economy of the Soviet Union into a market-based economic system. Reformers spoke of the inadequacy of past attempts at reform within the system, citing as evidence Gorbachev's failures in the 1980s, and pledged a complete overthrow. Poland, having preceded Russia in the reform process, was used as a guide for Russian reformers and their Western advisors. In fact, many of the same economists who served as advisors to the Polish government were also involved in the Russian reform process.

At the time, many of the advisors recruited from the West advocated shock therapy as a reform strategy appropriate for all transitioning countries which wanted to adopt a market-based system. This reasoning stems from the intellectual foundation of shock therapy—a belief that if provided with the proper incentives, economic actors will behave according to economic laws universal in place and time. The purpose of this chapter is to summarize briefly this intellectual foundation of shock therapy. Then, the framework of the shock therapy approach will be outlined, including its application specific to Russia. This approach will then be critiqued in order to set the context for an alternative transition strategy presented in chapter 3.

2.1 Intellectual Foundation of the Shock Therapy Approach

The shock therapy strategy is rooted in the assumptions and arguments of neoclassical economic theory. The key to understanding the shock therapy approach lies in understanding neoclassical theory's treatment of economic actors and its assumptions regarding the decision-making process and environment. This information is provided below, therefore, in order to put the application of shock therapy into theoretical context.

2.1.1 Behavioral Assumptions

The core behavioral assumptions of neoclassical theory are profit and utility maximization; rational, self-interested economic actors attempt to maximize an objective function of maximum profits or utility subject to any accompanying constraints. Decisions are made with this singular pursuit in mind. Important to neoclassical analysis is the elimination of place and time as elements to be considered in analysis. If all actors are identical, then place and time become irrelevant to economic inquiry. There is no past or future; instead, they are compressed into a single present, whereby time becomes reversible. Thus, time is ahistorical and behavior is universal.

Economic actors are faced with choosing among a given and known set of alternatives. Full and perfect information provides probability distributions of outcomes for each alternative. Each of these distributions is weighed by the economic actor in the decision-making process. Thus, the economic actor is

assumed to have a high level of computational ability. Uncertainty is excluded unless it is termed “risk” and this risk is assessed through probabilistic calculus.

2.1.2 Decision-Making Environment

The decision-making environment in which choice takes place is the competitive market; the market is the natural outcome of individuals pursuing their own self-interest (C. Clark 1993, 379). In this competitive environment, prices accurately reflect relative scarcities and economic actors are able to make decisions in response to undistorted market signals. In addition, new information is immediately absorbed by actors to be factored into decision-making. Therefore, there are no lags in computation.

Larger society is comprised of the aggregate of individual, atomistic actors. Assuming these actors seek to maximize their individual welfare, this leads to the maximization of social welfare in the aggregate. That is, as rational actors pursue self-interest through the maximization of objective functions, the net aggregate result is an outcome that harmonizes the energies of individuals (Gee 1991, 84; C. Clark 1993, 375). The best interest of society is thus provided by the free exchange parameters of the market.

Social order is assisted greatly by the assumption of market-clearing—there is no involuntary underutilization of available factors of production. This is accomplished through the efforts of an “auctioneer” whose role is it to adjust the relative prices of goods. Through these price adjustments, excess demands are balanced between individual markets, resulting in a final vector of prices that

produce equilibrium in all markets. Resources are, thus, allocated appropriately given the needs of society and a superior economic outcome results.

2.2 Reform Strategy of Shock Therapy

Based on the theoretical foundation outlined above, shock therapy sought to simultaneously reform both the political and economic spheres in Russia in order to create a decision-making environment appropriate to a market-based system. Because the underlying assumption was that economic actors are able to optimize by using all available information, it was argued that releasing market forces that provide the appropriate signals to actors will result in a reallocation of resources. This reallocation will increase both micro- and aggregate performances to levels above those of the planned economy (Solimano 1993, 1824; Daianu 1994, 184).

The pace of change was, therefore, viewed as a value which would determine the overall success or failure of reforms (Schlack 1996, 624). The idea was to use the window of opportunity that emerged following the breakup of the Soviet Bloc to institute widespread and immediate reforms to affect a complete break from the old system. In this manner, rapidity would capitalize on public support for change that stemmed from the *glasnost'* and *perestroika* reforms of Gorbachev. That is, reformers argued they were chasing social and political forces rather than leading them (Daianu 1994, 186);

Other arguments for speed arose from fear of opposition. It was argued that rapidity in reform would minimize opposition from entrenched interests,

particularly those of the Communist Party elite, the *nomenklatura*. By making reforms speedy and irreversible, this would depress the momentum of those who desired to maintain the status quo (Roland 2000, 329-32; Sachs and Lipton 1990, 53-4). It was further argued that speed would reduce uncertainty, as it would quickly put into place the new economic rules that had to be followed. In contrast, a gradual approach to reform would result in internal inconsistencies and political resistance.

Comprehensiveness would also assist in combating the rent-seeking feared from entrenched interests. It was argued that partial reform would create rents for groups that may be threatened by further reforms. Therefore, partial reforms could inadvertently create constituencies that will tend to oppose further reform (Sachs and Lipton 1990, 53-4; Sachs 1992, 5; Daianu 1994, 185; Roland 2000, 332).

2.3 Elements of Shock Therapy Reforms

Taking their cues from the Polish reform process that was already underway, beginning in January 1992 Russian President Boris Yeltsin and Yegor Gaidar, his chief economist and Prime Minister, instituted a series of reforms that intended to address the inherited economic crises. This reform agenda focused on making changes to the formal institutions of society, introduced in chapter 1 as the devised, explicit rules of the game—the laws, policies and economic rules which require, permit or prohibit certain behaviors (North 1990, ch. 6). These explicit rules were targeted as it was believed the universality of economic laws

would be sufficient to induce any necessary behavioral changes on the part of economic actors for a market-based system to develop. More specifically, to create the decision-making environment of a market-based system required the development of competitive markets, the transfer of ownership from the state to the private sector, and the retrenchment of the state to a role more consistent with the liberal service states of the West. Shock therapy was, therefore, centered on these three mutually reinforcing goals of liberalization, privatization, and macroeconomic stabilization.

Shock therapy reforms had to confront initial conditions in Russia—a country in significant economic crisis. As of 1991, the Soviet Union had accumulated large budget deficits due to both decreasing revenues and increasing expenditures in the 1980s. Because of production levels insufficient to meet consumer demand, Soviets' ability to purchase consumer goods was limited. In combination with high rates of money and wage growth, this led to a significant "monetary overhang," a harbinger of future inflation once that money was released into the economy (Goldman 1994, 97; Aslund 1995, 41). Future economic problems were also foreshadowed by the absence of gold and hard currency reserves depleted extensively by Gorbachev during his administration. In addition, Gorbachev had also indebted the Soviet Union with significant international loans which Russia stood to inherit. Lastly, in 1991 the breakdown of Soviet trading alliances, the now-defunct Council of Mutual Economic Assistance, led to the disappearance of external demand (Aslund 1995, 46).

2.3.1 Liberalization

In order to institute a competitive market environment, reforms were needed that would establish a system whereby prices and output levels were determined by market signals (Sachs and Lipton 1990, 53; Bogatova 1992, 7). Therefore, price and wage controls of the planned economy would have to be eliminated, as would subsidies and directives. This began on January 2, 1992, when controls were removed on most wages and on 80 percent of producer prices and 90 percent of consumer prices (Goldman 1994, 99-100; Aslund 1995, 140).

In addition, competition would be effected through the liberalization of market entry and promoted by opening the Russian economy to international trade. Laws allowing private enterprise went into effect, as did a presidential decree on freedom of trade which allowed entry into both domestic and foreign trade (Aslund 1995, 142). It was argued that subjecting domestic enterprises to competition from world markets would assist in improving performance and instilling a realistic structure of prices (Sachs and Lipton 1990, 55; Bogatova 1992, 8).

In order to provide the necessary conditions for free trade, tariffs needed to be reduced, quotas needed to be eliminated and the bureaucratic licensing of trading firms had to end (Aslund 1995, 146). A free trade regime further required devaluing the currency and creating a convertible exchange rate, with a unified and market-determined exchange rate beginning in July 1992 (Aslund 1995, 148). This would allow domestic enterprise to freely buy foreign exchange,

without rationing, at a given official price, and would ensure that exporters receive the same price in domestic currency for each dollar earned abroad (Sachs and Lipton 1990, 54). Essentially, Russia introduced a foreign trade system that conformed to GATT (Aslund 1995, 152).

Economic liberalization further required the legalization of private property. It was necessary to adopt and enforce a rule of law appropriate to a market-based system, including a commercial code, company law, and contract enforcement (Sachs 1991, 27). In addition, legal changes were necessary to create favorable laws for new private investments (Bogatova 1992, 8). To further develop the private sector, property also needed to be transferred from state to private ownership; this will be addressed below.

The assumption was that by changing the rules to allow for the development of private enterprise, markets would develop spontaneously. Freeing market exchange relationships and eliminating barriers to entry, particularly from the international arena, would diversify the market, alter the structure of demand and exert competitive pressure on producers; producers would subsequently respond to market signals, production would respond to demand and efficient enterprises would prosper (Bogatova 1992, 8).

Though price liberalization would initially cause inflation, this would induce a natural reduction in demand and natural increase in supply. More specifically, a “J-curve,” or, alternatively, a “transformational recession,” was hypothesized: an economic contraction was likely initially, but as adjustments are made by economic actors the economy would experience a momentum in growth which

would surpass the initial contraction (e.g. Ericson 1991; Kornai 1994, 1995). In addition to the output response, it was also argued that there would be a positive effect on welfare for the consumer through the elimination of shortages and queues (Boycko 1991, 36). In this manner, almost exclusive focus was put on supply considerations under the assumption that supply would respond to market incentives and, therefore, lead to output increases and economic growth.

2.3.2 Privatization

The transition from plan to market required the transfer of production from the public to the private sector. Therefore, part of the shock therapy reform package included converting state-owned enterprises to corporate form and then privatizing the enterprises. A number of different approaches were presented, including direct sales and free distribution; however, more important than the actual method was that privatization was to be fast and comprehensive.

The case for rapidity is outlined in Lipton and Sachs (1990). There, the authors argue that a slow, firm-by-firm approach held too high of a risk that the privatization process would be derailed for political, economic, and financial reasons. Therefore, rapid privatization is preferred even if it initially leads to an inappropriate distribution of ownership. As they argue,

The potential costs of overly rapid privatization must be traded off with the high cost of maintaining the present system in which state-owned enterprises lacked clear incentives (or actually have perverse incentives) in the face of the market forces now being introduced...(297).

They subsequently add that an even greater risk to slowing the process is the potential that the process will be “paralyzed entirely.” Further arguments were

that rapid privatization would also prevent asset-stripping, achieve irreversibility, and close down unprofitable plants and firms as quickly as possible (e.g. Chubais and Vishnevskaya 1993; Aslund 1995, ch. 7; Roland 2000, ch. 10).

If any misallocation of assets ensued, this would be sorted out in the capital markets that would subsequently develop and strengthen following the reallocation of assets to private ownership (Lipton and Sachs 1990, 296).

Furthermore, capital markets would also create incentives for owners to profit-maximize. This should be sufficient to influence enterprise management to exhibit appropriate market behavior.

To begin the process, in 1992 the Supreme Soviet adopted the "Program of Privatization," which addressed all state and municipal property except for state farms, land, and housing (Aslund 1995, 241). These were privatized under separate legislation, though the privatization of farming and land would remain incomplete through the next decade.

Privatization of enterprises generally occurred through cash auctions, voucher auctions, or employee buyouts of leased property (e.g. Aslund 1995; Filatotchev and Bradshaw 1995). Cash auctions and employee buyouts were used for companies with fewer than 200 employees and less than 1 million rubles in fixed capital. Mass privatization through voucher distribution was the second phase in Russia's overall privatization process, and addressed transfer of ownership in medium- and large-scale enterprises¹. For a processing fee of 25

¹ State-owned enterprises with over 10,000 workers and 100 million rubles in sales needed special permission to enter the mass privatization program. In addition, about 30% of all enterprises, including energy companies and those in the military-industrial complex, were not subject to mass privatization.

rubles, each Russian citizen was eligible to claim a voucher with a face value of 10,000 rubles. This voucher could be used to obtain shares in a privatized company or investment fund, or could be sold for cash in a secondary market. These public voucher auctions began in December 1992 and lasted until July 1994.

The workers and managers of the firms slated for mass privatization were allowed to choose between three variants prior to opening the enterprise to the public in the voucher auctions. The variants were as follows:

(1) 25 percent of shares to be allocated to workers for free and managers given the right to buy 5 percent of shares at July 1992 book value. In addition, managers and workers could buy a further 10 percent of shares at a 30 percent discount from book value on a three-year installment plan. The remainder of the shares would be sold at auction for either cash or vouchers. This method was used by approximately 20 percent of all enterprises.

(2) 51 percent of shares to be allocated to managers and workers at a price of 1.7 times the July 1992 book value with at least 50 percent of the payment made in vouchers. The remainder of the shares would be sold at auction for either cash or vouchers. More than 75 percent of enterprises chose this method.

(3) A group of employees would take responsibility for the enterprise's restructuring and development under a one-year contract. If the obligations

specified in the contract are met, this group receives the right to buy 20 percent of the shares at July 1992 book value. The working collective of the enterprise could buy another 20 percent of shares at a 30 percent discount to book value on a three-year installment plan. This variant was available only to medium-sized enterprises that did not choose to be converted to public stockholder companies. Less than 1 percent of enterprises used this variant.

Privatization, in combination with liberalization reforms, would therefore provide the necessary conditions to support the development of the private sector (e.g. Sachs 1991, 1992). The goal was to create a class of private owners who would restructure enterprises to comply with the rules of a competitive market environment. It was anticipated that in the long run, patterns of ownership would gradually evolve in favor of outside owners (Buck et al. 2000, 380). Such outside ownership was a necessary condition for the restructuring effort, as it presented a challenge to the status quo and the entrenched interests of management. However, this would require the creation of an “owning group” with sufficient power to challenge the prerogatives of management; that is, not only was a break from central control required, but also a break from managerial control (Cowling 1995, 165).

2.3.3 Stabilization

Shock therapy macroeconomic reforms embraced the “grabbing hand” theory of Shleifer and Vishny (1998). This theory views the state as inevitably

corrupt when political authorities are in control of production and enterprise. This argument provided the basis for stabilization reforms, which called for depoliticization of the economy by reducing the overarching presence of the state as it existed in Soviet times. This would be partly accomplished both through liberalization and privatization, but also required certain specifically macroeconomic reforms.

At the onset of transition, the federal budget was faced with a planning legacy of massive government expenditure and an underdeveloped tax base. Therefore, macroeconomic reforms were focused on improving the budget balance and controlling the inevitable inflation brought about by price liberalization. This would be accomplished primarily through the elimination of subsidies, which in Russia totaled up to 20 percent of the federal budget during Soviet times (Fischer 1992, 88). Fiscal discipline was, as such, imposed through reducing spending on public goods, reducing or eliminating subsidies to enterprises, minimizing state-sponsored investment, and reducing the state bureaucratic administration. In addition to generating macroeconomic stability through budgetary stability, it was argued that forcing enterprises to operate according to a hard budget constraint would promote appropriate market behavior.

To generate public revenue, a reform of the tax system was also necessary; value-added, payroll, profit, and excise taxes had to be structured to comply with the institutional infrastructure of a market-based system. In addition, a public debt market debuted in 1993 when dollar-denominated debt and short-

term ruble-denominated treasury bills were issued. Six- and twelve-month bonds began issue in 1994 and variable coupon bonds in 1995 (Buchs 1999, 688)

From a monetary policy standpoint, policy needed to make money “expensive” through restricting domestic credit and reducing the growth of the money supply (Goldman 1994, 100). Contractionary monetary policy would also help to shape future private sector growth through promoting competitive sectors of the economy (mainly export-oriented) over non-competitive industries (mainly domestic-oriented). This would subsequently release factors of production for more profitable use (Brodsky 1997, 60). This would also create positive real interest rates.

In addition, as discussed with respect to liberalization, a uniform exchange rate had to be established. By so doing, it was argued that this would create a working monetary system that was based on a convertible currency and a stable price level. Another benefit to currency convertibility at a fixed exchange rate was that it forced the conduct of monetary policy by rule in order to maintain the exchange rate (Fischer 1992, 92). As Fischer argues, an exchange rate rule would be easily “understood” by the central bank and would provide direct stabilization to the price level through its visibility.

2.4 Shock Therapy Applied

What quickly became apparent is that the shock therapy strategy proved easier to construct than implement. The destruction of the old system proceeded far faster than the emergence of the new system, resulting in a costly economic

contraction. This economic collapse exacted significant costs on the vast majority of the Russian populace which included a dramatic decline in real incomes, the erosion of savings, an increased incidence of poverty, and declining health and quality of life. Table 1 below provides a brief snapshot of important economic indicators for Russia from 1991 to 2004. A review of the data shows an economic decline surpassing even that experienced by the United States during the Great Depression.

Table 1: Key Economic Indicators, Russia, 1991-2004

Year	GDP (constant prices, billions of rubles) ^c	GDP (percent change) ^{c,d}	Inflation Rate (CPI) ^{c,d}	Unemployment Rate (percent, ILO definition) ^{b,e}	Share of people living below subsistence (percent) ^{a,c,f,e}
1991	...	-5.0	92.7	...	9.9
1992	8828.41	-14.5	1353.0	5.2	18.5
1993	8060.34	-8.7	699.8	5.9	29
1994	7036.68	-12.6	302.0	8.1	25
1995	6748.17	-4.0	190.1	9.5	29
1996	6504.89	-2.8	47.8	9.7	21.2
1997	6594.64	1.4	14.8	11.8	21.2
1998	6242.24	-5.3	27.7	13.3	24.6
1999	6638.58	6.3	85.7	12.6	38.2
2000	7305.60	10.0	20.8	9.8	30.2
2001	7677.60	5.1	21.5	8.7	27.3
2002	8041.80	4.7	15.8	7.9	24.2
2003	8632.70	7.3	13.7	8.4	20.6
2004	9249.44	7.1	10.9	8.3	17.8

Sources: ^aSilverman and Yanowitch (2000, 47); ^bInternational Labor Organization Labor Force Survey, June 2005; ^cIMF World Economic Outlook, April 2005, Statistical Appendix; ^dIMF World Economic Outlook, October 1997, Statistical Appendix; ^eWorld Bank Russian Economic Report, April 2005; ^fDoyle (1996, 498)

2.4.1 Challenges to Shock Therapy Reforms

Throughout the 1990s, reform efforts ran into a series of challenges. This resistance to change manifested itself in a variety of ways including protectionist responses, special interest group bargaining, and increasing criminal control over market entry; each distorted the competitive market environment envisaged by reformers. As Aslund (1995) discusses, liberalization in Russia turned out to be “surprisingly difficult” to accomplish: “To a remarkable extent, the Russian intellectual paradigm was not transformed. Many Marxist prejudices, such as irrational devotion to production, disbelief in market allocation, and belief in regulations, were not crushed (173).”

For example, liberalization of currency markets was stymied by a state need for hard currency. This need resulted in a series of presidential decrees which required any party earning foreign exchange to sell a portion of the earnings to the Central Bank at an established (non-market) rate. This challenged exporter incentives, resulted in hard currency flight, and encouraged barter.

The liberalization of energy commodity markets was also stymied. Price controls were kept on petroleum, resulting in significant rent-seeking as traders were able to export petroleum to the world market (Goldman 1994, 117). The state retained control over raw materials that were deemed “strategically important.” Crude oil was also subject to state appropriation for its own use throughout the 1990s. And high export taxes were placed on energy commodities due to a state need for revenue.

Encouragement of market entry and competition was frustrated by protectionism and market control. When domestic industry proved unable to compete effectively in world markets, protectionist tariffs and quotas were instituted to shield domestic industry from competition. The mafia quickly instilled a protection system that has made being a business owner in Russia a dangerous proposition. In addition, regional authorities also became known for exacting high bribes for business licensing (Aslund 1995, 145). As Aslund admits, "(t)he heart of the matter is that power—not law—is what truly mattered in Russia. The legislation of liberalization was, therefore, a moot point (138)."

The results of the privatization program, while quantitatively successful (by 1996, over 120,000 enterprises were privatized), did not result in the necessary restructuring and efficiency enhancements as trumpeted by reformers at the start of the program. Instead, the literature on the voucher program suggests overwhelmingly a series of qualitative failures. These include lack of restructuring, insolvency, the fleecing of investment funds, insider information, regional bias, greater income inequality, low foreign investment, few new entrepreneurs in manufacturing, and a lack of corporate governance (e.g. Filatotchev and Bradshaw 1995; Stiglitz 1999; Desai and Goldberg 2000; Roland 2000; Supyan 2000; Baer and Bang 2002; Brainerd 2002; Ellerman and Stiglitz 2003).

In addition, reformer attempts at enforcing the macroeconomic agenda were often frustrated. For example, major industrial lobbies succeeded in thwarting the reduction of certain subsidies (Aslund 1995, 220). Tax evasion

also presented a significant challenge. As an example, imported goods were grandfathered into tax-exempt status if the contract was signed prior to January 1993, quickly prompting subterfuge in the re-writing of contracts (Buchs 1999, 703). In an effort to address this, in the late 1990s the Russian government began initiating action against those who had evaded tax enforcement and with those who had developed arrears with the state. However, powerful industrial groups were able to impede passage of many of the proposed measures (Buchs 1999, 706).

Russia's inability to service its debt led to limits in its access to international credit markets. This, combined with the inability to raise revenue through tax enforcement, meant significant budget deficits remained. These deficits continued to be financed by printing money, through Central Bank credit or by the Central Bank purchase of most state debt (Silverman and Yanowitch 2000, 146). This resulted in a high growth rate of money, as opposed to the restrictions sought after in reforms. In an attempt to stop this, in April 1995 rules were enacted that prohibited the Central Bank from financing the deficit. This resulted in the issue of short-term debt to cover the state budget. Though money growth was reduced, this reliance on debt-financed deficits effectively crowded the private sector out of the debt market and thus reduced capital investment.

A lack of clarity in rules generally resulted in power struggles between the executive branch and the Central Bank. The institution supervising the Central Bank, the Supreme Soviet, was dominated by factory directors whose primary interest was to maintain subsidy support. Instructions for monetary restraint

were, therefore, often ignored as the Central Bank authorities favored supporting domestic enterprise. Until the other former Soviet republics developed and legalized their own national currency, monetary restraint was also challenged by the printing of rubles in other republics (Goldman 1994, 107-8).

Further loss in monetary policy control came from the demonetization of the economy. Faced with liquidity crises, enterprises created their own money and credit equivalents, or they fell into wage, pension, and factor payment arrears. This demonetization took a variety of forms, including the use of “near monies” such as promissory notes and debt swaps, or alternative currencies such as the U.S. dollar. In addition, barter has flourished at both the household and enterprise level (e.g. Commander and Jackman 1997; Poser 1998a; Poser 1998b; Clarke 2000; Guriev and Ickes 2000; Ledeneva and Seabright 2000; Silverman and Yanowitch 2000). By the end of 1998, the level of barter was estimated at nearly 50 percent of GDP (Ledeneva and Seabright 2000).

2.4.2 One-Size-Fits-All Policy Advocacy

As will be argued by the research results presented in this work, the assumptions of shock therapy created a transition ideology which ignored the context in which change took place. That is, country-specific and culture-specific factors, having no place in neoclassical theory, had no place in transition analysis. Instead, what resulted was the adoption of a one-size-fits-all school of policy advocacy which rests on the fundamental assumptions of neoclassical

economics, ignoring real-world complexity and chronic problems such as imperfect information and limitations to computational ability.

The consequence of the simplifying nature of neoclassical theory is that the “informal institutions” of society, introduced in chapter 1 as the culturally specific, implicit rules of the game, are largely ignored. For example, as M. Clark (1993) argues, the exclusion of such issues as power and the naturalness of human nature and the market results in the sanguine efficiency assumptions of shock therapy:

Only if one holds that economizing behavior is part of human nature (instinctive), and that there is a mechanism that will balance the subjective energies of self-interested maximizers so that the net result is order and not chaos, can one assume that the spontaneous order will generate coherent results (376).

2.5 Conclusion

The economists who constructed the shock therapy reforms approached the transition from the perspective of neoclassical economics and its belief in the free market paradigm. It was generally argued that the incentive structure presented by competitive markets would be sufficient to induce economic actors to behave in a manner appropriate to a market-based system. From this perspective, reforms were designed around an intended end-state, emphasizing destruction of the old system and top-down construction of a new system. Reforms were, therefore, concentrated on the formal institutional environment. Focus was placed on instilling a price incentive, liberalizing exchange, reducing the presence of the state, and legalizing private property. With these changes,

any required changes in social norms to effect behavior appropriate to a market-based economic system will follow.

The application of reforms proved more difficult than its proponents envisaged. Power struggles arose, resulting in inconsistencies with respect to policy implementation. In addition, required behavioral changes did not always follow the change in formal rules, weakening the supposition that a market-based system will provide appropriate incentives for economic actors. Protective behavior surfaced, such as rent-seeking and corruption, as individuals sought to use the tumultuous times to their own advantage. These challenges either interfered with the implementation of certain prescribed policies or rendered them ineffective.

In the next chapter an alternative approach to the transition is presented which lies in direct contrast to the shock therapy approach. It is argued that this alternative approach presents a more appropriate theoretical framework for analysis of countries in transition, given the analytic attention paid to the institutional environment. In addition, an environment of such radical change presents a unique set of characteristics that make attention to informal institutions especially critical. As evidence, the evolutionary-institutional approach is able to address some critical mistakes of shock therapy and provide some explanation for the real-world interference with shock therapy's intended result.

Chapter 3: The Evolutionary-institutional Approach

There is a contrary body of literature on the transition which incorporates into its intellectual foundation many of the arguments of old- and new-institutional economics. This approach criticizes shock therapy's suppositions, arguing that its focus on formal rules is insufficient and that informal institutions must be considered in analysis. For example, given the complexity and uncertainty of the real world decision-making environment, analysis of behavior must extend beyond simple rationality to include more complex mental models that consider a variety of socio-cultural dimensions.

What follows is a discussion of some of the primary arguments and ideas represented generally within institutional economic thought. Space does not allow for a full rendering of all the different dimensions and arguments of institutional economics, including the demarcation between subsidiary fields within the institutionalist tradition, or the parallel arguments that can be found in such fields as social economics and evolutionary economics. Therefore, this discussion limits its focus on the arguments that most directly relate to the topic at hand, with ideas from both old- and new-institutional thought represented. Following this discussion, a contrary approach to the transition is outlined which analyzes economic change from the perspective of bottom-up organic evolution of institutions, rather than the top-down constructed change of shock therapy.

The shock therapy approach is then critiqued from this alternative perspective, with a critique of the privatization process provided as an illustrative example.

3.1 Intellectual Foundation of the Evolutionary-institutionalist Approach

As an alternative to the neoclassical belief in the market as the sole coordinating mechanism, the institutionalist school argues that all aspects of society construct the choice set available to economic actors and serve to coordinate economic behavior. As a result, the economic sphere is “embedded” in society (Polanyi 1957; Granovetter 1985). Social and economic practices are interrelated and, therefore, indistinguishable from one another. Thus, institutionalism seeks to define the economy’s place in society rather than separate it from its context. Analysis proceeds from this socio-economic context via consideration of the formal and informal cultural, religious, political, social, and economic institutions of society. Each type of institution serves an explicit purpose in coordinating the actions of economic actors and order results from the continuity and regularity provided by the institutional environment.

3.1.1 Behavioral Assumptions

The embeddedness of the economic sphere implies that the actions of economic actors cannot be only expressly economic. Behavior and actions are influenced by other factors that extend beyond economic calculation, making it necessary to study both economic and non-economic factors. For example, there may be social, cultural, or religious factors that are as relevant to decision-

making as an economic calculation of pecuniary costs and benefits. In this way, economic actors are seen as relational rather than viewed as autonomous, atomistic individuals. Thus, all decisions have a social context and bear social consequences. As Neale (1987) argues:

...a culture defines the permissible and the forbidden, defines right and wrong, the admirable and its opposite, gives content to these definitions with rules for behavior, and so provides opportunities as well as limits. A culture is collective action, a collective legacy of patterns of action, just like a language, which allows freedom of thought but not of grammatical expression and which is also collective action with a history (1179).

Institutionalism, therefore, rejects the idea that there are natural laws which exist *a priori* from the cultural context and which determine the structure and operation of the economy.

However, that the environment and interpersonal relations can shape (and, therefore, constrain) behavior does not imply the elimination of free will or self-determination. Though it is argued that economic goals cannot always be represented by a simple objective function, the social context to economic activity does not constrain the economic actor from acting purposively to promote her individual welfare if an objective function is targeted. Agency therefore remains a relevant consideration in institutional analysis. That is, an individual can act counter to, or independent of, socialization (M. Clark 1993, 374). As Miller (2003) argues,

Humans are born into a social environment with a particular set of mores and customs... But they also are animated by curiosity, workmanship, concern for fellow human beings, both present and future. As such, they effect change upon their societies, even as communal forces shape them (260-61).

Thus, the institutionalist perspective on human epistemology is almost a direct contrast with the environment envisaged by neoclassical theory, as outlined in the prior chapter. This contrast stems from the view of the economic system as embedded in society, rather than isolated as its own sphere. The economic actor, therefore, engages in behavior (shaped by economic and non-economic factors) in a decision-making environment that constitutes larger society and all its accompanying complexity.

3.1.2 Information, Knowledge and Learning

Economic actors gain information from the absorption of sense data. As introduced in chapter 1, information is translated into knowledge through the use of mental models which interpret sense data received. In this way, mental models provide the economic actor with the framework with which to understand new information. Incomplete information is endemic; it is impossible to assume economic actors can access each bit of data required for each and every decision as environmental conditions are constantly changing. In addition, access to information can be asymmetric due to differences in power and the exclusivity this implies. This indicates a partiality to mental models in that all gaps in information or cognition may not be fully eliminated.

Information does not become knowledge until the sense data is processed cognitively, given order, and learned. Cognitive competence may be asymmetric. That is, economic actors can run up against computational limits as sense data is processed and this can limit the ability to turn information into

knowledge and learning (Heiner 1988). In addition, learning is incremental and cumulative; what was learned in one period is built upon in the next. There may be lags in this process of information capture and its translation into knowledge and learning.

Tacit knowledge is also considered in institutional analysis (M. Polanyi 1967). Knowledge embedded in routines cannot always be fully captured in codified form and that which cannot be codified becomes tacit. A society's stock of tacit knowledge is acquired through a long historical process and is shaped by the institutions and organizations of that particular society (Murrell 1992, 84-85). This leads to further asymmetry in cognitive competence, as economic actors also possess different forms and types of tacit knowledge. This tacit dimension can be invaluable in decision-making, as it is inseparable from, and cannot be replaced by, explicit knowledge.

3.1.3 Habits

These informational and cognitive constraints lead to a continuum of decision-making whereby there are multiple levels of deliberation from which to approach each unique decision situation. As Hodgson (1997, 665-66) argues, each situation will have to address both the subjective knowledge and cognitive capabilities of the economic actor, as well as the objective characteristics of the decision problem. Habits come into play when full deliberation is constrained. For example, when actors do not have the computational and/or cognitive skills necessary (Nelson and Winter 2002, 29). Habits become particularly useful in

situations that are repetitive and non-unique and emerge when one particular way of resolving the situation gains predominance (Young 1996, 106).

Habits are no less purposeful than conscious deliberation and have a self-actuating character as they become established in the subconscious (Hodgson 1997, 664). As a result, they can be difficult to change even if the persistent use of the habit conflicts with expressed economic objectives or the formal rules of economic exchange. Resistance to change is particularly strong in cases where the transaction costs to adaptation are high (Waller 1988, 121). As such, the persistence of habits can be viewed as “rational” when change requires high costs or when habits serve to reduce conflict (Nelson and Winter 2002, 30).

3.1.4 Uncertainty and Instability

Informational and cognitive constraints, irreversibility of time, uncertainty of future-oriented decisions, interaction of economic and non-economic factors, and dynamism of the socio-cultural environment all contribute to a decision-making environment that is highly complex and uncertain. This uncertainty is so pervasive it does not lend itself to resolution by risk assessment, futures markets, probabilistic calculus, or other neoclassical tools. Lack of knowledge of outcomes is unavoidable, as is error-making. In addition, the continuity and stability of relationships among economic actors cannot be assured. That is, economic actors will not respond in a uniform manner in every instance and, therefore, their behavior cannot be fully predicted. Furthermore, the potentiality

of a principal-agent problem implies that all economic actors may not engage in activity that is mutually consistent.

This leads to the possibility of solutions that are irrational or erroneous from a neoclassical perspective. In addition, irrationality and errors can persist over time. This gives rise to arguments addressing cumulative causation, path dependency, and lock-in. For example, Veblen (1961) noted the cumulative process of adaptation undertaken by an economic actor throughout her economic life history. This argument was later importantly extended by Myrdal (1957) in his explanation for different levels of economic development among nations. He noted that when a change occurs within a system, this instigates supporting change rather than countervailing change. This supporting change furthers movement down the same path, creating a cumulative effect. Therefore, a country able to capture favorable internal and external economies can position itself along a path of development and growth. Alternatively, a country suffering from barriers to economic growth will have their problems reinforced.

That actions are cumulative implies there is feedback which reinforces or magnifies an outcome (North 1990, 7; Hodgson 1992, 758). Importantly, this means that the future development of an economic system is dependent upon its past and current paths. Evolution is, thus, path dependent. Furthermore, even if an optimal path is eventually reached, there is no assumption that it will remain stable. Therefore, a sub-optimal situation can become locked-in, and can be exacerbated. As a result, history matters to an institutionalist and it bears directly on contemporary conditions.

3.2 Institutions

Though the term “institution” can be interpreted in a variety of ways, as it is used in this research work, it will refer to North’s (1990) definition, whose treatment of institutions is the reference for much of the following discussion. Specifically, North states that “institutions are the rules of the game in a society or, more formally, are the humanly devised constraints that shape human interaction (3).” Institutions exist and gain credibility because they are routinely reproduced in society. They are arrangements that help to promote exchange and provide continuity and stability. Therefore, there is a contextual element to institutions. As society develops over time and place, institutions gradually emerge to reflect the idiosyncrasies of a specific cultural milieu (Schlack 1996, 619).

3.2.1 Formal and Informal Institutions

As introduced in chapter 1, a distinction can be made between formal and informal institutions, referred to here generally as “rules” and “norms”. As noted previously, formal institutions consist of the devised, explicit rules of the game—the laws, policies, and economic rules which require, permit or prohibit certain behaviors. These rules are subject to human intervention and change when it is deemed worthwhile to alter their structure. In contrast, informal institutions are the culturally specific, implicit rules of the game—the norms of behavior, codes of conduct, and conventions that guide individuals in their interaction with others.

Norms are pervasive, habitual, and resistant to change to a much greater extent than formal rules.

Rules can (1) complement and increase the effectiveness of norms; and (2) may be enacted to modify, revise, or replace norms. On the other hand, norms can themselves serve to extend, elaborate, or modify rules. Together, rules and norms symbiotically interact to define the choice set available to economic actors in the embedded economic system. They provide a series of constraints to behavior, identifying what is and is not possible, what is and is not permissible. In this way, they create the structure and operating procedures of the economic system.

3.2.2 Institutional Change

The institutional structure of society undergoes constant dynamic transformation. This process of institutional change is governed by the interaction between rules and norms; as rules and norms modify and elaborate on one another, the economic system evolves to reflect these changes. This process is continuous as current institutions, embodying past adaptation to change, are already dated and subject to further modification as they confront ever-changing circumstances. In other words,

Any institution or set of institutions emerged as an instrumental solution (the instrumentalism modified, of course, by the then existing institutions) to problems that have already been solved and thus necessarily reflects the past rather than the present or the future (Neale 1987, 1199).

The process of modification and elaboration of rules and norms is a matter of human volition in response to the incentives embodied in the institutional

framework. Typically, institutional change occurs either incrementally when the decision-maker recognizes that she could improve her position or further some set goal by changing the institutional framework at the margin (North 1990, 83). Because a single institution exists within a larger system of institutions, changing the structure of one institution means that others must adapt and change as well (e.g. Hodgson 1997). As a result, often the consequences of change cannot be foreseen and economic agency can work for good or ill.

A change in formal rules can create a situation of tension between pre-existing norms and the new rules. The new formal rules may replace or render needless some of the pre-existing norms; however, norms could continue to persist despite even the most comprehensive formal rule changes:

Although a wholesale change in the formal rules may take place, at the same time there will be many informal constraints that have great survival tenacity because they still resolve basic exchange problems among the participants, be they social, political or economic. The result over time tends to be a restructuring of the overall constraints—in both directions—to produce a new equilibrium that is far less revolutionary (North 1990, 91).

Therefore, in order for a significant system change to take place, a change in rules must result a change norms, thus promoting socially-sanctioned changes in behavior. That is, the change must be accepted by society via a process of (informal) institutional adjustment for it to become effective (Ibrahim and Galt 2002, 106).

3.3 Evolutionary-institutional Approach to Transition

There is an alternative to the shock therapy approach to the transition that draws on many of the theoretical arguments of institutionalist economics. In the literature, this approach is called, alternatively, the “institutionalist” approach, the “evolutionary-institutional” approach, or, more commonly, the “gradualist” approach. For purposes here, the term “evolutionary-institutional” will be used; this emphasizes the evolutionary aspect to the process of institutional and societal change, in direct contrast to the top-down constructivism of shock therapy and its accompanying assumptions of immediate and spontaneous institutional adjustment.

3.3.1 Characteristics of Transition

At the heart of the evolutionary-institutional approach is the belief that the transition is not just a change in the economic system, but a holistic change of the socio-cultural framework. Any attempts at reform would have to consider the characteristics of such radical change and the inevitable instability of such. As examples, drawing on institutionalist principles would presuppose the following as potential characteristics of the transition environment:

- uncertainty and information asymmetries, inherent in any economic system and magnified under such radical change;

- vulnerability to rapid and unforeseen change, creating the likelihood for policy mistakes and inappropriate reforms. This threatens lock-in on a sub-optimal path due to spillover effects, cumulative causation, and crisis contagion;
- a need to garner *ex ante* public support to reduce trepidation at the start of the process, alongside a need to develop constituencies to decrease the possibility of *ex post* reversibility (Roland 1994);
- power struggles and ceremonial opposition from the status quo as pre-existing positions of power and status are threatened; and,
- a steep learning curve in response to the constant inflow of new information, new knowledge, and the realization of adaptive requirements.

All of the above add up to the potential for significant conflict and tension between institutions and, therefore, to uncertainty regarding outcome of reforms. That is, there is no assumption that the adoption of the formal institutions of the market would create a similar end-state among transitioning countries. Instead, the initial conditions—the inherited socio-cultural context—inextricably embedded with the economic sphere, will interact with the new rules and this will determine a unique path and pattern of change (Portes 1991, 10; Jin and Haynes 1997, 92).

3.4 Reform Strategy

According to the evolutionary-institutional approach, the development of the numerous supporting, and reinforcing, institutions of a market-based system will take a significant period of time to form. In addition, economic agency will direct this process. Therefore, credibility of reforms is important in order to create a transition environment which promotes progressive economic change through the adaptation of new formal and informal institutions.

Angresano (1996, 435) argues that resistance to change may arise if: (1) such change is forced before economic actors are fully informed and trust that there will be rewards for adopting the new institutions; (2) economic actors show attitudes of learned helplessness; or (3) there exist entrenched interests who fear the loss of jobs, income, and privileges as a result of change. However, adjustment and change will be furthered as experimentation proceeds and feedback is received. That is, knowledge of the machinations of the new system can be acquired, but only through time and by learning (Giuriato 1997, 179, Stanfield 1998, 8). Thus as new knowledge is acquired this promotes adaptation and change as well as the development of appropriate supporting institutions.

As a result of the above, most writers in the evolutionary-institutionalist tradition avoid prescribing a specific reform strategy along the lines of the triadic recipe of shock therapy. Instead, a pragmatic approach to reform is emphasized, with affected constituencies allowed a voice in the reform process.

3.4.1 Speed of Reform

The necessary institutions, the rules of the game to support a market-based system, will only emerge over time. Furthermore, these institutions are developing in a transition environment characterized by a high level of uncertainty, information asymmetries, power struggles, a steep learning curve, and threats of crises and lock-in. As a result, according to the evolutionary-institutional approach, the transition environment presents characteristics which beg for prudence and pragmatism in a reform package. Therefore, a gradual approach to reform is advocated for the interregnum (e.g. Griffin and Khan 1994; Tsang 1996; Jin and Haynes 1997; Roland 2000).

Under this gradual approach, attention is paid to the specific sequence in which reforms are enacted. A significant benefit to sequencing reforms pragmatically is the flexibility and reversibility it provides (Marangos 2005, 268). As reforms proceed, feedback will allow reformers to respond to new needs as they are identified. In addition, radically changing circumstances could lead to a need to reverse reforms that are subsequently determined inappropriate, or that lead to unintended consequences. Pragmatic sequencing of reforms will thus minimize the dislocation costs inherent to such radical change. In contrast, policies that commit themselves to a specific end-state are not likely to be sustainable if learning and mistakes induce large transformation costs (Murrell 1992, 89).

3.4.2 Maintaining the State

The adjustment process is complicated by the radical nature of the changes required, so may be furthered by promoting elements of stability and familiarity. This can be provided by a critical balance between the old and new system that can serve to promote progressive institutional change. The evolutionary-institutional approach therefore calls for the identification of institutions that are in place that could positively affect the reform process. Prior existing institutions may appear, on their face, incompatible with the new system, but may serve to limit disruption and social unrest as new institutions develop which accommodate changes in economic structure (Jin and Haynes 1997, 83).

Thus, a level of state presence in the economic system may have to be maintained during the transition period. As a result, liberalization and privatization should proceed piecemeal over time in order to minimize disruption in society. Furthermore, macroeconomic policy should focus efforts on activist stabilization. This promotes economic well-being and support for the reform process.

3.4.3 Privatization

This argument is especially evident in the privatization literature, where rapid ownership transfers are highly criticized. The evolutionary-institutional approach argues that instead of only ownership transfer, the privatization process encompasses transformation of an entire system of social contracts and institutions. Such transformation requires a gradual decrease in government

presence and a gradual hardening of budget constraints (Summers 1990, 337-38; Roland 1994; Angresano 1996, 436-37; Roland 2000, 342-43). This would allow time for the development of a strong private sector, for the emergence of supporting financial markets and institutions, and for the state to maintain credibility and the ability to act against corruption.

In contrast, premature privatization may result in high transformation costs. Some potential costs include: the persistence of monopoly power in the absence of an adequate competition policy (Griffin and Khan 1994); the shuffling of assets as struggles over power and property continue in the absence of a clear and credible legal system (Elliott and Dowlah 1993); inefficient ownership due to informational asymmetries and free-rider problems (Lo 1995); future inequities as the result of inaccurate asset valuation (Summers 1990); and incentive for asset-stripping and wealth diversion (Ellerman and Stiglitz 2003).

As examples, evolutionary-institutional proposals for gradual privatization include:

- spin-off restructuring: a gradual spinning off of viable components of large enterprises, particularly enterprises which have tax, utility, or wage arrears. This would create a base of small and medium-sized enterprises, and allows for the preservation of social, organizational, and informational capital that has positive value (Ellerman and Stiglitz 2003);

- legitimizing shadow enterprises: the use of public policies to lower entry barriers for the small and medium-sized firms operating in the shadow economy. This would build on the networks, habits, and relationships that were active in the informal economy during Soviet times (Ibrahim and Galt 2002);
- selective state support: state identification of promising enterprises which would continue to receive state assistance. These enterprises might be withheld from the privatization process temporarily (Bogatova 1992);
- entry promotion: the provision of seed capital and other incentives to develop a broad group of small entrepreneurs and the middle class that will emerge from the entry of new enterprises, rather than the transference of already existing enterprises (Angresano 1996, 450-51; Ellerman and Stiglitz 2003);
- managerial turnover: to privatize where funds permit and maintain support for the remaining state-owned enterprises. Those would then be restructured organically as top management is replaced. This would overcome institutional rigidities and put into place managers familiar with modern production techniques (Angresano 1996, 441).

3.4.4 Stabilization and Liberalization

An output collapse may be inevitable in an economic environment characterized by such widespread uncertainty as that presented by the transition.

Given the infant state of market activities, leaving markets to their own devices could be catastrophic in terms of the transformation costs accompanying an economic downturn. For example, if rigidities leave economic actors unable to adjust to the changing economic circumstances, a prolonged and severe recession would result. This has implications for both current well-being and future economic growth, given the adverse effect of recessions on capital formation (Solimano 1993, 1824). In addition, the collapse of state ownership cumulates into a need for reform in other areas, such as pensions, housing, education, health care, and child care—benefits typically provided through the enterprise in the Soviet system.

The state should, therefore, conduct activist anti-cyclical stabilization efforts in the face of inevitable recession. Correspondingly, it is argued that full price liberalization will depress real wages and consumption, creating additional recessionary bias (Solimano 1993, 1824). In addition, rapid changes in relative prices can cause significant changes in income distribution which could undermine support for reforms (Griffin and Khan 1994, 98). As a result, a piecemeal approach to price liberalization is advocated alongside activist macroeconomic stabilization.

3.4.5 Credibility and Support

Without credibility, changes in formal rules will be ignored and reforms will be stymied. Credibility and public support of the reform process thus become an important element within the evolutionary-institutional perspective. By engaging

in programmatic reform while maintaining a stable macroeconomic environment, this creates an element of continuity and assurance during the period of transition which assists the reformers in gaining credibility.

Consider the example of legality. That is, the establishment of a rule of law, while a necessary condition for a market-based economy, is not sufficient. In fact, as argued by Litwack (1991, 78), the definition of "legality" must be viewed in two parts: (1) a mutually consistent set of laws; and (2) a belief in the stability and enforcement of these laws. Based on the latter, legality becomes a social phenomenon that is dependent upon social recognition of the rule of law. Without a credible and strong center which earns respect for its rules, the legal system will be insufficient for that required by a market-based system. As discussed in Koslowski (1992, 691), this has particular relevance to the legalization of property rights which, he argues, is not identical to the institutionalization of property rights as the institutionalization of property rights requires legitimacy. He notes that the state's role is to provide this legitimacy, making organized and institutionalized exchange possible.

However, social stability, and therefore popular support, is threatened in response to economic uncertainty. Radical changes translate into stress and other adverse effects on quality of life, implying the potential for high social costs. In addition, economic costs increase as state benefits such as gratis education and health care are withdrawn and market-induced risks surface. Therefore, a strong social safety net should be included as part of the macroeconomic stabilization program.

Additionally, any perceived unfairness or fear of excessive inequality can produce discontent, generating political and social instability that could interfere with achieving objectives (Tsang 1996, 184; Roland 2000, 337).

Correspondingly, reformers must also pay attention to who constitutes the winners and losers of change. For example, Griffin and Khan (1994, 97) argue that it is important to pay attention to the distribution of assets and to equitable access to productive resources to avoid polarization of wealth. This can be accomplished by prioritizing reforms which contribute to both inefficiency and to inequality; for example, improvements in the terms of trade for agriculture or the elimination of subsidies that benefit higher income groups. Koslowski (1992, 686) argues that with respect to privatization, simply selling assets to anyone who has the means to pay for them will overwhelmingly favor the former *nomenklatura*, as these individuals were the few with access to capital during Soviet times. Without some constraints on redistribution of ownership, the inequality that would result would undermine public support for private property.

Issues of credibility and support become even more acute once asymmetric power and the influence of special interest groups is taken into consideration. If the process is viewed as credible, reformers will have the power to pursue their objectives against opposition. As an example, Dewatripont and Roland (1992, 292) argue that government can use the threat of future reforms hurting one group to obtain approval for a current reform that hurts a majority. In addition, a government which garners credibility in its agenda can also foster

majority approval for intentions which may end up hurting majority interests intertemporally.

3.5 Evolutionary-institutional Critique of Shock Therapy

As introduced in chapter 2, the implementation of shock therapy reforms resulted in a series of events that proved contrary to the predictions of reformers and their consultants. Despite attempts to change the incentive structure of the economic system, behavioral rigidities persisted. These rigidities manifested themselves in a variety of ways, including factor immobility and lack of active change by managers and employees that evidenced an unwillingness to play by the new rules. Corruption and abuse of power, prevalent during Soviet times, was as commonplace under the new system. Special interest group activity surfaced from a variety of sources, both old and new. A small number of heavily influential business leaders control most large-scale production, particularly in lucrative natural resources, with the assistance of corrupt political authorities. Distortions also exist in markets for small businesses, whereby local and regional authorities, alongside the heavy hand of organized crime, control entry and distribution. The increase in criminal activity has exerted significant social costs on the population and interfered with market transparency.

As Koslowski (1992, 674) argued at the onset of reforms, if following reforms market exchange subsequently takes place on its own accord, this will validate neoclassical theory. On the other hand, problems in the development of competitive markets would support the institutionalist critique of mainstream

theory. It appears that this critique is, indeed, justified as much of blame for current economic and social conditions in Russia may be attributed to shock therapy and the method by which reforms were implemented. Therefore, opponents of the radical reforms have argued that the empirical results in Russia represent an invalidation of neoclassical theory and its place in shaping policy measures (e.g. Jin and Haynes 1997; Roland 2000, 336).

The evolutionary-institutional critique of shock therapy addresses a number of different aspects to the reforms. The primary criticisms are as follows:

- **Linearity:** The planned economy was perceived as a distortion from the optimum; shock therapy would succeed in effecting a mechanical transformation from an inferior state to an optimal state. Adherence to the free market paradigm obscured the important fact that a market-based system appears in the real world in a variety of forms and levels of development, influenced by the contextual characteristics of the individual countries.

- **Universality:** The assumption of universality in the shock therapy strategy implies that results should be congruent among countries, regardless of their heterogeneity. In this sense, there is no place for the context in which the reforms were taking place, including the historical, cultural, religious, and geographical uniqueness of each country. That is, that the strategy employed had worked relatively well in “similar” efforts led to the assumption that it was as

applicable to the Russian economy. As one example, in his argument for shock therapy Ericson (1991) comments in a footnote that:

...the command economy also comes with a necessary set of political and social institutions... that are mutually consistent with, and supportive of, that economic system. They are, however, far more readily amenable to change, as the experience of Eastern Europe shows (25).

- **Rapidity:** It was argued that the window of opportunity presented by the collapse of communism called for the rapid implementation of reforms in order to prevent the possibility of reform reversals. Social stability was sacrificed for speed, breaking social cohesion as different members of society were able to respond to the changing rules at different rates. The linear path of shock therapy, combined with the speed of reform implementation, led to an inability for reversal or correction. Negative results became locked-in, including rent-seeking, corruption, and power differentials.
- **Top-down approach:** The top-down approach of shock therapy ignored the organic nature of change and the importance of public support and the negotiation process among different interest groups that lead to change. The reforms proceeded regardless of popular will. Repeated breach of implicit and explicit promises then created a sense of cynicism toward the state and rule of law (Ellerman and Stiglitz 2003, 32).
- **Transformation costs:** A major criticism of the shock therapy approach is its lack of a "human face" in its approach (Gnos and Rochon 2004-05, 189). Insufficient

attention paid to negative consequences led to the use of policies that did not address the high social and economic costs of prolonged recession and decreases in social services, or the threat of unequal social, economic, and political structures that could result². Instead, it was argued that the benefits of a market-based system outweighed any temporary transformation costs.

3.5.1 An Application of the Critique: The Privatization Process

An evolutionary-institutional critique of the Russian mass privatization program reflects much of what might be considered the crux of the evolutionary-institutional appraisal. This evaluation will be presented for illustration.

To begin with, to the shock therapists, the manner of privatization and state of institutional infrastructure at the onset was less important than the speed of privatization. As noted in chapter 2, voucher distribution was viewed an appropriate means to rapidly transfer ownership from the state to the private sector. Supporting institutions such as debt and equity markets, a stable banking system, a functioning legal system, an entrepreneurial culture, and actors familiar with competitive behavior were not addressed prior to implementing the privatization program. It was believed that a stratum of private owners would create demand for this institutional infrastructure, thereby promoting its development as needed. For example, enterprises, responding to market incentives, would increase their effectiveness and innovative skills while higher

² Both Sachs (1991) and Sachs (1992) did warn of the negative consequences of a collapse of the social safety net and the potential impact on the most vulnerable of society. He called for Western governments to provide aid to abate these costs.

prices would stimulate production. In sum, this transfer in ownership would effect general financial stability and economic growth.

As introduced in chapter 2, the influence of the privatization program on the economic environment, while quantitatively successful, has not resulted in the significant positive social welfare effects trumpeted by policymakers at the start of the program. Instead, the literature on the voucher program suggests overwhelmingly a series of qualitative failures. These include lack of restructuring, insolvency, the fleecing of investment funds, insider information, regional bias, greater income inequality, low foreign investment, few new entrepreneurs in manufacturing, and a lack of corporate governance. The privatization process has been so disparaged that in Russian it is often referred to as "*prikhvatizatsiya*" or "grabification"—a play on words combining *privat-* (private) and *prikhvat-* (to grab).

Much of the failure has been attributed to the insider bias of the program. Though small scale enterprises were generally earmarked to be auctioned to the public for cash, employee buyouts generally dominated. As noted in chapter 2, more than 75 percent of medium and large-scale enterprises transformed into joint stockholding companies also remained employee majority-owned. As a result, outside shareholder influence remained low.

Other insider bias resulted from the lack of transparency that inspired abuse. Those with economic and political power used it to obtain information about favorable enterprises. After taking control, many of these "oligarchs" captured significant wealth through asset-stripping and preferential policy

treatment. This earned them a tremendous amount of political and economic power but did not promote a competitive market environment. In addition, many of the most valuable enterprises evaded mass privatization and instead were later transferred to the oligarchs in the notorious “loans for shares” program during Yeltsin’s 1996 presidential campaign.

The economic inequality resulting from the program perpetuated decreased public confidence in a market economy. For example, as early as August 1993, 56 percent of the population agreed with the statement that the distribution of vouchers was only for show, and did not effect any real change (Aslund 1995, 255-6). By 1998, polling showed 75 percent in favor for renationalizing the major enterprises that were privatized and 65 percent in favor of confiscating the wealth that was acquired (Silverman and Yanowitch 2000, 150).

3.6 Conclusion

The evolutionary-institutional approach provides a more realistic view of the transition process and the radical institutional changes that are required. The approach focuses on the means, not the end, of the transition through its attention to the decision-making environment and the institutions that serve as its constraints. There is no certain end-state that can be predicted as the process of societal change will have to unfold organically. This is in diametric opposition to the strategy of shock therapy and its ideological assumptions.

As Roland (2000, 329) argues, inherent in the evolutionary-institutional approach is the “philosophical skepticism” of institutionalist economics that results from society’s relative ignorance of its economic and social systems and how those systems change. The uncertainty of this results in an aversion towards a large-scale, top-down imposition of reforms. Instead, bottom-up organic evolution is emphasized which takes into consideration pre-transition circumstances and structures and acknowledges the problems inherent in such a massive change in economic and political systems. As a result, if a reform process seeks the end-state of a market-based system, it must emphasize a gradual withdrawal of the state and organic development of the private sector. By so doing, this allows economic actors time to respond to change, thereby promoting credibility and support of reforms.

The implementation of shock therapy reforms resulted in a series of events that proved contrary to the predictions of reformers and their consultants. Much of this may have been predicated, and thus avoided, had reformers paid attention to the evolutionary process of institutional change, the role of norms in economic decision-making, and the ceremonial power of entrenched interests. The results of the privatization process provide an obvious example of the consequences of this analytic neglect. Rather than the development of a large class of private owners, only a very small number of Russians have benefited from the changes, primarily due to access to information during the process. Asymmetric information and cognitive competence created a small group who were able to take advantage of the high uncertainty in the process to expropriate

Russia's most valuable assets. Many of these new economic elite come from the ranks of the former Soviet-era *nomenklatura* and used their insider status to their advantage.

The principles of institutionalist thought focus on the evolutionary nature of change. Economic agency is central to the process as purposive individuals are themselves responsible for shaping societal evolution. That is, the process of institutional change is underwritten by the emotional, intellectual, and practical stakes in the outcomes of the transition (Clark and Soulsby 1999, 218). Because of the important role played by the interaction between formal and informal institutions in the process of institutional change, investigation into this interaction has the potential to contribute greatly to transition analysis. Therefore, a research study was undertaken which focused on the informal institutional environment in Russia during the transition. It is to the specifics of this study and the results of its analysis that this writing now turns.

Chapter 4: Description of Field Study

Institutionalist theory has long expounded the value of empirical data drawn from surveys, case studies, and interviews. By obtaining first-hand accounts from actors within their specific institutional environment, further progress is made in understanding the role of the economy in society. This is particularly true for analysis of the informal institutional environment. Understanding the role that norms play in decision-making is significantly furthered through direct observation. Without this information, the interaction and interrelationship between rules and norms remains insufficiently determined. To this end, a study was carried out with this pursuit in mind.

From October 2003 to March 2004, a field study was undertaken in Krasnodar, a city in southwestern Russia, and the nearby state farm village of Korzhevski. As introduced in chapter 1, this is an ethnographic social research study consisting of well-prepared, extensive personal interviews from a limited number of participants. The focus of the questioning is on the presence, development, and functioning of informal institutions in the day-to-day operations of ordinary men and women. Given that this is a relatively underrepresented topic area in transition literature, it was decided that analysis of the role of informal institutions in the transition could, potentially, make a significant contribution.

In this chapter the methodology of the study is presented, including information on how the sample was obtained and how the analysis proceeds. In addition, the development of the interview guide and the content matter of the questions are described. The reader is then provided with a description of Krasnodar and Korzhevski. Following this, the demographic makeup of participants is provided for context. Lastly, three areas of informal institutional analysis generated from results of the field study are introduced. These themes form the basis of the three chapters of analysis to follow.

4.1 Process and Method

There are a number of reasons for choosing an in-person interview approach for data collection. Cross-sectional, in-depth, face-to-face interviews present a unique opportunity for insight, as the researcher is able to learn from participants their vision of their world through their own perspective. In-person interviews also allow for more detail, clarity, and spontaneity than alternative methods such as mail and telephone surveys (Oppenheim 1992, 67; Weiss 1994, 2-8; Willis 2000, 283-85). Additional advantages of the personal interview come from the researcher's ability to watch reactions. The researcher is able to distinguish when a respondent is hesitant. Thus, clarification or explanation can ensue if necessary (Salant and Dillman 1994, 134). The face-to-face nature of the questioning also contributes to establishing rapport. This provides a level of sensitivity necessary to obtain truthful answers to personal or intimate questions (Willis 2000, 285; Bertrand 2002, 243).

4.1.1 The Interview Guide

The interview itself was a semi-structured conversation between researcher and participant, meaning the interview was a scheduled activity, though open-ended, and followed a general script which covered a specific list of topics (Bertrand 2000, 203). The script in this case was an interview guide that was used in each instance in order to ensure that there was some measure of congruity and comparability between interviews. As part of the preparation process for the interview guide, a native speaker was used to translate the questions. Following this, the researcher then back-translated the questions to ensure accuracy.

The development of the interview guide was an iterative process as there was no opportunity to pretest the guide. As a result, awkwardly worded questions or inappropriate questions were sometimes discovered after the fact. These were changed or reworded accordingly as the interviews progressed. New subject matters of interest also arose as the interviews progressed. In these instances, new questions were added to the guide. Because these changes took place in process, many of the earlier participants were re-interviewed later in order to obtain responses to these new questions.

To begin the process of developing questions, a number of different questionnaires were consulted which addressed similar topics (United Nations 1996; Narayan 1998; Rose 1998; World Bank 1999; Office for National Statistics 2000; Grootaert et al. 2002; Pickering 2003). In some instances, questions were either borrowed directly from one of the above sources, or modified slightly from

the original to make the question more appropriate in the Russian context. In addition, some quantitative questions from the above sources were borrowed and then extended qualitatively in order to allow for free verse responses. As noted in chapter 1, adding qualitative dimensions to the predominant standard of statistical analysis within the economics discipline speaks to the depth and significance of this particular field study. Lastly, many questions were unique to this survey having been created by the researcher herself.

The questions asked were a combination of open-ended and fixed-choice. This combination was used in order to allow for some inter-subject comparison on simple frequency of responses, while keeping the main emphasis directed on the free verse responses (Casley and Kumar 1988, 14; Oppenheim 1992, 112-15). These free verse responses often formed the basis of a long and rich discussion on specific experiences. The advantage of this semi-structured process was that it demonstrated to the participants that the researcher was organized and provided direction for the conversation if the participant was feeling initially apprehensive or uncomfortable. However, it also left both researcher and participant free to follow new paths of questioning if the need arose. In addition, it allowed participants time to become comfortable with the process. This promoted the elaboration of responses to open-ended questions.

4.1.2 Areas of Questioning

The goal of the study was to contribute to an assessment of the workings of the market economy from a Russian's own perspective. Therefore, the

participants were asked questions addressing a number of different topics. Many of the questions focused on issues such as relationships and coping strategies, economic conditions, and access to resources. The questions can be divided into eight general groups:

- **Day-to-day functioning:** Participants were asked about routine daily interactions and exchange. For example, several questions addressed access to food, housing and other necessities, shopping habits, and other daily activities.
- **Structure of communities:** Interactions among neighbors, involvement in neighborhood organizations and events, and how the neighborhood responds to problems were all addressed.
- **Networks of friends and family:** The researcher attempted to analyze the participants' scope of and reliance on social networks. This included questions addressing the extent of networks, involvement in organizations, and socializing with friends and family.
- **Economic situation:** The economic position of the participants was assessed through a variety of questions. Examples include asking about employment, income, access to emergency lending, and precautionary savings. In all instances the researcher attempted to learn of all sources of income, both formal and informal. This is yet another area where the in-depth nature of the interview

was advantageous as information was obtained regarding material resources beyond what might be reported as formal income earnings.

- Views towards authority: The researcher attempted to assess how the participants perceive the role of authority figures and government institutions in contemporary Russia. Participants were questioned on their trust in and views of political and financial institutions, the relative influence each had to drive the course of events, and their levels of civic engagement.

- Subjective well-being: Many questions attempted to assess the level of satisfaction felt by the participant for his or her life in general. In addition, the participant was asked to judge what they felt to be the best and worst results of the changes that had taken place since 1991 and were asked to assess the nature and extent of any currently unresolved personal problems.

- Cognitive competence: Given the important role cognitive competence plays in the processing of sense data, the participants were asked several questions in an attempt to assess their understanding of the economic changes taking place around them. Examples include having the participants define what a market economy means to them and inquiring about their perceptions of the role of various economic actors that have emerged in Russia's current economic environment.

- Vision of future: The participants were asked of their expectations regarding Russia's future. This included their opinions on the political leadership and their expectations as to future changes that might transpire.

Recall that the full interview guide is attached as Appendix A.

4.1.3 Sampling Technique

The selection of research participants came from a non-probability sampling technique; specifically, a "snowball" technique. In this process, initial participants are selected and are then asked to suggest others who are likely to be willing candidates for the research (Bertrand 2002, 185). This technique presents several benefits. First, though the researcher had traveled to the former Soviet Union on previous occasions, the location of the field study was in a large city unknown to the researcher upon her arrival. The alien environment presented a challenge in identifying initial participants. The relatively short time frame available to conduct the field study, five months, meant that interviews needed to begin straight away. This did not allow the researcher the luxury of time to embed herself into social circles that might later yield participants. The snowball technique therefore assisted the researcher in developing her sample at a much faster pace. Importantly, the snowball technique also facilitates trust between researcher and participant, necessary for the sensitive nature of many of the questions (Weiss 1994, 34; Creswell 1998, 117).

The in-depth interview, with all its attributes, does also present some limitations, particularly with respect to sample size. The level of personal interaction and time-intensive nature required by in-depth qualitative interviews necessitates a smaller sample size than that required by randomized probability sampling. As the study was being prepared, review of the literature yielded little guidance on what constitutes an appropriate sample size for a non-randomized probability sample. Oppenheim (1992, 68) argues that a sample of 30 to 40 is typical for in-depth studies, but most methodology guidebooks simply state that the sample size depends on the nature of each research study. The researcher began with the goal of finding 50 participants for the study. At the conclusion of the field study, 47 participants had provided 70 interviews. This includes both primary interviews and a number of follow-up interviews. The relatively small number of participants allowed for lengthy and deep interviews which generated valuable detailed information. This provided an element of contextual reliability not easily captured by impersonal surveys focused on generating large numbers of quantifiable responses.

A translator was employed by the researcher to assist with the interviews. Though the researcher speaks Russian, the use of a native speaker for the interviews presented a variety of benefits. The translator was familiar with the city, which allowed for ease of movement. Often the translator made the initial contact and established the time and place of the interview. In addition, the fluency level of the translator ensured better understanding of responses during the interview. This allowed the researcher to develop important follow-up

questions which added dimension to the responses. The translator also assisted greatly in establishing trust and entrée with the participants, important to the in-person interview.

To establish first contact, the researcher prepared an introductory letter which explained the general nature of the interview. An English-language version of the letter is attached as Appendix B. Participants were, in the end, relatively easy to find as the study generated quite a bit of attention. Many of the initial interviews stemmed from contacts known personally to the translator and this provided initial impetus to the study. These participants then provided referrals and introductions with other potential participants, typically family members, friends or co-workers. Other participants arose when rumors of the interviews circulated. For example, when an interview was conducted at a participant's place of employment, co-workers often showed curiosity as to what was taking place and subsequently volunteered themselves as participants. In addition, as the researcher made personal contacts over the course of her tenure in the locale these also occasionally yielded interviews.

4.1.4 Remuneration

When appropriate, participants were compensated for their time or were given a gift in recognition of their participation. With each interview, the translator indicated what was appropriate for the given circumstances. Remuneration was used if, for example, the interview took place in lieu of the participant working or preparing for work. In these situations, the participant was typically compensated

for the opportunity cost of their time. Other participants were remunerated due to their especially fragile financial status, such as unemployed participants and pensioners. In several instances, remuneration was offered but subsequently refused. In some of these instances, the researcher offered a donation in place of remuneration. For example, a daycare worker was interviewed but refused payment. In this instance, the researcher offered a donation for the purchase of toys for the daycare and this donation was accepted by the participant. In other cases, remuneration was not offered based on advice of the translator. In these instances, the translator noted that the financial status of the participants would have resulted in offense taken. When payment was inappropriate, a small gift such as chocolates or similar was offered. In addition, whenever the interview situation required laying the table or other such extensive food offerings, the researcher often provided some food for the gathering.

4.2 Location of Study

As noted above, from October 2003 to March 2004 the fieldwork for this research study was carried out in Krasnodar, a city in southeastern Russia. A map detailing Krasnodar's location is attached as Appendix C. Krasnodar was not the researcher's original choice for the field study. Instead, the initial intent was to conduct the study in St. Petersburg, Russia. However, logistical difficulties led the researcher to search for an alternative location. Krasnodar was the hometown of someone known personally to the researcher and this contact suggested the city as a potential locale. Through this individual, the

researcher was introduced both to someone able to provide housing and to the translator that was subsequently employed by the researcher.

The logistical difficulties that resulted in choosing Krasnodar as the location for the study proved serendipitous. Generally, those that are in Russia's highest socio-economic stratum are inhabitants of St. Petersburg or Moscow. Certainly these two cities receive the bulk of tourist business in Russia, as well as most visits by foreign media, policymakers, and dignitaries. As a result, discussions in the popular media regarding life in Russia often cite the experiences of those living in St. Petersburg or Moscow. In the meantime, areas outside that corridor are often marginalized in discussion. In addition, the researcher traveled to those two cities during her stay in Russia and noted, from her own perspective, a significant difference in the goods and services available for purchase and in use—clothing, cars, restaurants and the like—and their price levels. This indicates a potentially significant difference in the transition experiences of those in Krasnodar and those in Moscow and St. Petersburg. Thus, this study has the ancillary benefit of shedding light on an area that is less frequently included in transition discussion and that may have experienced greater material hardship as a result of the transition.

4.2.1 Description of Krasnodar Krai

Krasnodar, Russia is the capital city of Krasnodar Krai, a region in the North Caucasus area of Russia. Approximately 1,500 kilometers south of Moscow, the Krai borders both the Black Sea and the Sea of Azov. There are

approximately 5 million people living in the Krai, with approximately 750,000 in Krasnodar (NUPI 2002). Given its southern location, the climate is fairly temperate. As a result, the Krai hosts much of Russia's agricultural production in an area traditionally referred to as the *Kuban*; a strong connection to the land is a large part of the local cultural ethos. Second to agriculture in the economy is tourism, as the popular Sochi resort area is also a part of the Krai. Hanson et al. (2000, 156) note that the predominance of agricultural production and tourism in the economy has caused the region to be severely financially affected during the transition period due to the decline in the agricultural sector's terms of trade and in travel and tourism.

The favorable climate has resulted in both Krasnodar, and the Krai in general, receiving high numbers of migrants from both the former Soviet republics and from within Russia. In the years immediately following the collapse of the Soviet Union, Krasnodar Krai had the highest level of migration of all the regions of Russia, resulting in a 10.7 percent change in the population from 1989 to 1996 (Heleniak 1997, 87). The population shift is generally attributed to two sources. First, ethnic and religious differences have served to polarize the populations of the Soviet successor states, particularly those in Central Asia. As Locher (2002) shows empirically, ethnic sorting is currently taking place in response to advancement of the culture and politics of various ethnic groups. Russians, finding themselves as the new minority, are migrating to Russia to escape backlash and ethnic violence. The primary destinations of Russian migrants are the regions of southern Russia, which includes the Krai (Heleniak

1997, 88). Second, as a result of its proximity to Chechnya, Georgia, and the North Caucasus, large numbers of people fleeing violence in these areas have migrated to Krasnodar. This population growth has stretched already strained financial and social resources even thinner and ethnic tension is palpable among the population.

4.2.2 Description of Korzhevski

In addition to Krasnodar, interviews were also conducted in a nearby state farm village. Korzhevski, with a population of approximately 4500, is 100 kilometers to the west of Krasnodar. The translator engaged for the research study had lived in Korzhevski for several years and still maintained a home there. The translator invited the researcher to visit the village and some of the individuals with whom the researcher came into contact volunteered themselves for interviews.

This particular state farm is one of the few state farms in Russia that specialize in the production of rice, a point of pride for many in the village. Due to its special status, agricultural authorities have resisted privatizing the state farm. In fact, the interviews conducted at the village evidenced that the governing rice institute maintains extremely tight reins on the farm. It is generally believed this is a detriment to the farm and its employees, and hence to the village as a whole.

4.3 Demographic Profile of Participants

As noted above, interviews were obtained from 47 people. In some cases, the interviews were with one individual while in others the researcher spoke with multiple participants at once. For example, couples occasionally answered the interview questions together. In another instance, the researcher spoke with a young couple and the maternal grandmother. Occasionally there were children present, including the translator's son. Of the participants, the most consistently sampled individual is a married female, in her late thirties or early forties, and employed full-time. The youngest participant is 18 years-old, the oldest 83 years-old. Most participants are either married or widowed. The sample also includes one single mother. The table below presents some key demographic data of the participants:

Table 2: Summary of Participant Demographics

	Number of participants	47					
Gender	Male	15	Education	Less than secondary	4		
	Female	32		(Special) Secondary	19		
				Higher	24		
Ages	20 or younger	1		Monthly Income (in dollars) ^{b,c}	<\$100		3
	21 to 30	9			\$100 – 150		11
	31 to 40	11			\$150 – 200		7
	41 to 50	8			\$200 – 250		5
	51 to 60	8			\$250 – 300		6
	61 or older	10			\$300 – 400		1
Tenancy in city or village	Less than one year	3			\$400 – 500		4
	1 to 5 years	6	\$500 – 600		1		
	5 to 10 years	13	\$600 – 700		2		
	10 to 20 years	11	\$700 – 800		1		
	Greater than 20 years	14	>\$800	1			
Marital Status	Single	3	Employment Status	Employed	26		
	Married ^a	35		Piecemeal work	3		
	Separated	1		Unemployed	4		
	Divorced	5		Pensioner	13		
	Widowed	3		Maternity leave	1		

^a The “married category includes one participant who considers herself married by common law.

^b All ruble-to-dollar conversions in this research work are calculated using the average Interbank rate over the time period that the translator was in the field (34.25 rubles/dollar).

^c Five participants refused to provide this information.

More demographic details are discussed below. In addition, demographic information will be provided in the following three chapters when important for context of the interview data.

4.3.1 Employment and Income

The participants represent a range of incomes and occupations. The average reported income for participants' households is approximately \$300US. With the exception of unemployed participants with zero monthly income, the household with the lowest monthly income earns about \$60US a month. The household with the highest monthly income earns \$2,100US, almost three times as much as the second highest household income of about \$760US. Fourteen households report that they receive unofficial sources of income, which in Russia typically refers to income that is not reported to the government for tax and pension purposes.

A few of the participants are unemployed, or are employed in piecemeal work such as private language lessons or selling insurance by commission. However, most participants have one full-time job. This includes three pensioners who continue to work though they have begun receiving a pension. In addition, 12 households have at least one family member who works multiple jobs, or who earns income through additional means such as selling fruits and vegetables grown in the household garden. Four of the participants have jobs which provide them extra financial or in-kind benefits, such as reduced housing

costs or bonus income for taking on additional tasks such as trade union leadership responsibilities.

The participants show a significant degree of occupation turnover. One participant has held seven different jobs since 1991, another six, and several more have had between three and five jobs since 1991. The participants with the most consistent employment history are those that have worked for the state farm in Korzhevski, most since their teen years. The employed participants represent a wide range of current occupations, including a tractor driver, the operator of a gas heating station, a chambermaid, a daycare worker, two librarians, three hair stylists, four language instructors, four teachers, a dentist, a neurology resident, three small business owners, a security guard, an inspector for the Department of Education, an employee of the State Land Committee, a fire extinguisher maker, a shop manager, a bank manager, an employee of Mars, International, a crane operator, a painter-plasterer and two Amway salespeople.

4.3.2 Neighborhoods and Tenure

The participants live in 14 different neighborhoods and villages in and around Krasnodar. Many of the participants have lived in the area their entire lives, or at least for quite some time. Others have recently immigrated to Krasnodar, including some who came to Krasnodar to escape dangerous conditions in the former Soviet republics. One, a woman in her 30s, came to the Krai with several members of her family to escape the violence in her hometown in Tajikistan. Another came to Krasnodar with her family from Alma-Ata, the

capital of Kazakhstan. She notes that after 1991, the lives of ethnic Russians were made very difficult there and that was the reason her family left. Two more participants, an Armenian couple, were living in Azerbaijan during Soviet times but left when their daughter was threatened as tension and violence between Armenians and Azerbaijanis escalated in the 1990s. The wife notes that almost their entire village has come to the Krasnodar area to flee the ethnic cleansing.

4.3.3 Gender

In this sample, 68 percent of participants are women, resulting in a gender bias to the responses. However, there is an ancillary benefit to this bias. In Russia today, women and men remain in fairly gender-specific roles; this was observed by the researcher and has also been noted in the literature (e.g. Richardson 1995; Rethmann 1997). Women have historically, and continue to be, tasked with maintaining the household. In addition, they also tend to have closer relationships with others in the community. Given that many of the questions sought answers to issues such as shopping and store patronage, the household economy, and neighborhood involvement, adult female household members may be able to provide more reliable and complete responses to these questions.

4.3.4 Living Environments

Twenty-two participants live in apartments. Eleven live in single-family homes. Eleven more participants live in part of a house—a typical situation in

Russia where many single-family homes have been subdivided into two or three separate residences in response to housing shortage. One participant lives with her family in a single room at a hostel. Two others live in what is referred to as a *vremyanka* (temporary structure), a term often used to describe a small outbuilding of a house such as a summer kitchen. Six participants are renters and the rest live in either homes that they have built themselves or in apartments provided by the state during Soviet times. All but four households have at least two family members, including children. Most participants live in households with multiple generations. Especially common is a situation in which a younger couple lives with one set of parents. In addition, often an older couple has at least one parent who is of pensioner age living with them. In two situations an adult sibling is living with the household.

4.3.5 Location of Interviews

The interviews were conducted in a variety of locations. Thirty interviews were held in the participants' homes. In these instances, the interview often resulted in a larger social event where a table of food was laid and there was general socializing both before and after the formal interview. Twenty-three interviews were conducted at the participants' place of employment, such as during a teacher's open class period or a hair stylist's free time between clients. Fourteen interviews were conducted in the home of the referring participant, which presented an advantage in establishing trust with referred participants.

The three remaining interviews were held in neutral locations such as a café or the home of a mutual acquaintance of the researcher and the participant.

4.4 Cultural Specialization of Participants

As noted above, the focus of the study is on the role of informal institutions in the daily lives of ordinary Russians. The purpose of structuring the research as a field study and conducting interviews was to obtain a layman's perspective of the transition. Therefore, the researcher had to ensure that research participants were selected that could reasonably be expected to have the necessary information and to relay it accurately. In order to assess reliability, the guidelines of Casley and Kumar (1988, 21-3) are applied. These are as follows:

- Knowledge: The participants' knowledge of their personal experiences during the transition is both direct and firsthand;

- Credibility: It is often difficult to distinguish boasting, exaggeration, or misleading answers. The researcher relied on her personal observation to assess the credibility of the responses. Though each participant appeared to take the process seriously, credibility of responses appears high but cannot, by virtue of its nature, be fully assured.

- Ability and willingness to respond: All participants voluntarily agreed to be interviewed and signed a consent form to that effect. An English-language

version of the consent form is attached as Appendix D. If any participants were unable or unwilling to answer particular questions, these questions were skipped. In addition, participants were allowed to take as much time as necessary for the interview to proceed. This contributed to their ability to thoughtfully and fully respond.

- **Ulterior motives:** The researcher tried to determine if there were any attempts to paint excessively positive or excessively negative pictures. Though no responses appear to be such outliers, again credibility cannot be fully assured.

- **Bars to spontaneity:** The interviews were conducted in private locations to ensure confidentiality. There was never anyone present in the interview that was not invited by the interviewee.

- **Desire to please:** Though admittedly sometimes difficult to detect, the researcher felt no indication that there was any desire on the part of participants to give the “right” answer. In fact, in many instances during general socializing the researcher was challenged to justify different activities and behaviors of Americans and the U.S. government. This indicates that participants generally felt comfortable expressing their opinion, even if there was potential for the researcher to take offense.

Based on the above, and given the nature of the questions, the researcher feels confident that all participants are competent to answer with authority the questions posed to them. In the parlance of ethnography, all are “culturally specialized” in the topics under consideration (Bertrand 2002, 191).

4.5 Data Analysis

In 68 of 70 interviews, the interview was recorded digitally from start to finish using a portable recorder³. From these recordings, transcripts were made and became the main source of data analysis. The transcripts are generally a verbatim account. That is, no text was prematurely reduced intentionally. However, in some instances the order of words was changed to conform to English speaking patterns. In addition, in some instances words were muffled on the recording and were subsequently left out of the transcripts with a note explaining such inserted into the written record. In this manner, the researcher follows the recommendation of McLellan, MacQueen, and Neidig (2003) who argue,

If an analysis focuses on providing an in-depth description of the knowledge, attitudes, values, beliefs, or experiences of an individual, a group of individuals, or groups of individuals, a greater number and possibly lengthier units of text need to be included in the transcript (67).

The steps of transcription were standardized. Specifically, from the recording, the translator produced a Russian language transcript for the researcher. This was then translated into English by the researcher. The Oxford

³ In one instance, the batteries failed during the interview and in another instance, the minidisc recorder was forgotten. Luckily, both of these were short, simple follow-up interviews during which copious notes were taken and following which the researcher made an immediate written record of the conversation.

Russian-English dictionary was the primary reference in this process. Folk sayings and other idiomatic expressions, often difficult to translate into another language, were generally translated literally. The essence of their meaning and/or implication was then discussed with native speakers and noted in the transcript. In addition, again following the guidelines of McLellan, MacQueen, and Neidig (2003, 66), the researcher attempted to include elisions, mispronunciations, slang, grammatical errors, nonverbal sounds, and background noises in order to preserve the original voice of the participants as much as possible. There was one exception made to this standardized process. One interviewee was a non-native Russian speaker who spoke poor Russian. In this instance, the translator corrected much of the participant's speech in her Russian language transcript to make the translation manageable for the researcher.

Though the transcripts provide the primary source of data for analysis, other data are consulted. Descriptive field notes were prepared by the researcher following each interview. These notes were used to record environmental details of the interview, participants' reactions to questions, participants' general behavior during the interview, and other items of interest. In addition, the researcher kept a diary during her time in the field in which information learned through participation observation was recorded. In this the researcher is following the advice of Bertrand (2002, 369-70) who argues that diary analysis is necessary as it assists the researcher in interpreting transcripts

and descriptive field notes and makes the researcher aware of any personal biases during data interpretation.

4.6 Conclusion

The methodology undertaken for this research study is important to the economics discipline as it represents a historically marginalized approach to research. Though the nature of the study does not allow for a large sample size selected through randomized probability, in-depth interviews present a number of advantages over more impersonal forms of data collection. Particularly, there is a level of depth and clarity reached in the in-person interview that is not available from other types of survey instruments.

The questioning of the interviews is structured so as to allow participants to tell of their experiences as they perceive them and the transcripts were generated in a manner intent on preserving a participant's voice as much as possible. Using these transcripts, analysis proceeds through identification of prominent themes that lend insight to the informal institutional environment of the transition. In fact, many commonalities emerge from an interpretive study of the interview transcription text.

Over the course of the next three chapters, the researcher will report on three specific themes that emerged from the interviews: the prominent role of social networks in daily life, the uneven adaptation of cultural values, and the persistence of a pro-bribery culture in the transition. These results evidence the strong and inevitable interaction between rules and norms that serve to define

the institutional environment in which economic activity takes place. Thus, they lend credence to the theoretical framework of institutional economics and its views towards the process of institutional change, and therefore support the appropriateness and veracity of the evolutionary-institutional approach to transition.

Chapter 5: Social Capital and Uncertainty

This chapter begins the reporting of the field study's results by addressing the nature and essence of participants' social relationships and networks. In this analysis, "social relationship" is defined generally as "anything from a disposition of attitude... to a culturally defined and construed kin, ethnic, or social group identification... or to a joint, voluntarily adopted social tie (Narayan and Pritchett 2000, 279)." As will be shown, those connected through social relationships provide a substantive mechanism to navigate the socio-economic environment. In fact, as argued by Sweeney (2001, 153), man as a social animal necessarily implies that he may habitually engage in such collective approaches to pursue mutual benefit.

With respect to the transition—indisputable as a period of radical change—there are two primary reasons why an individual's social network might play an increasingly important role in the determination of her economic well-being. First, the heightened uncertainty resulting from the system change indicates the potential for greater use of personal ties as a coping mechanism. For example, the resources of friends and family may grow in importance with respect to the transmission and interpretation of information and in response to financial hardship. Furthermore, the use of social networks would be enhanced by continuing dysfunction in the formal rules of the Russian socio-economic

environment. Based on this, the role of social networks in response to the changes brought about by the transition may be investigated to further understanding of the role of informal institutions in this context.

The field study was, therefore, structured so that many of the questions sought to identify and classify access to what has been increasingly referred to in the economics literature as “social capital.” What is discovered is consistent with institutionalist arguments that note an unavoidable social element to economic transactions. Additionally, if external events act to influence mental models, and therefore economic strategy and decision-making, then one’s intimate inner circle of friends and family might, by its proximity, have a notable impact on the activities of economic actors. This argument is also consistent with the research results discussed below.

First, the concept of social capital is investigated. Various definitions are explored and its importance to economic well-being is established. Following this is discussion of the historical role of social capital in the Soviet Union and its implication for the transition. Then, social capital in the transition is addressed. Following this, research results are reported. These results are then typified within a reciprocity-redistribution-exchange continuum.

5.1 Social Capital

Initially, the term “social capital” was primarily used by sociologists and political scientists to discuss the relationships that define ethnic, political, and familial groups. With respect to the economics literature, the term was first

introduced by Loury (1977, 176), who contended that traditional labor market theory did not adequately reflect the significance of an individual's family and community environment on the acquisition of labor market skills. However, it was only after the concept was popularized and refined in the 1980s and 1990s that it became increasingly accepted in use and application in economics. Significant debate still remains over what constitutes social capital, particularly as it relates to use of the capital metaphor (e.g. Arrow 2000; Solow 2000; Bowles and Gintis 2002; Robison, Schmid, and Siles 2002; Schmid 2002). To date, this debate remains unresolved. However, the concept is now so widely disseminated in the economics literature that argument over semantics will be put aside for this discussion.

5.1.1 Defining Social Capital

Social capital is defined in a variety of ways. As noted by Small (2002, 10), much of the definitional variety is due to use of the concept as an umbrella for a number of ideas about the relationship between social resources and economic success. Some definitions emphasize only explicit relationships and communities, while others allow for the inclusion of more intangible elements such as reputation and trust. Some researchers define and/or measure social capital at the individual level, while others argue that the concept is best applied at the community level. The following summarizes the most commonly cited definitions from academic researchers considered influential in the social capital literature:

- The aggregate of the actual or potential resources which are linked to possession of a durable network of more or less institutionalized relationships of mutual acquaintance and recognition... which provides each of its members with the backing of the collectivity-owned capital... (Bourdieu 1986, 248-9);

- A resource available to an actor which (1) consists of some aspect of social structures and (2) facilitates certain actions of actors. These resources are useful if they come from (1) obligations, expectations, and trustworthiness of structures; (2) information channels; and (3) norms and effective sanctions (Coleman 1988, 104);

- Features of social organizations such as trust, norms, and networks that facilitate coordination and cooperation for mutual benefit (Putnam 1993a, 167);

- The expectations for action within a collectivity that affect the economic goals and goal-seeking behavior of its members, even if these expectations are not oriented toward the economic sphere (Portes and Sensenbrenner 1993, 1323);
and

- An instantiated set of informal values or norms shared among members of a group that permits them to cooperate with one another (Fukuyama 2000, 98);

Combining the ideas represented in the above definitions, this research work will use a most general definition of social capital. In this way, social capital is at once all relationship networks—both horizontal and vertical linkages—whether they are familial, political, communal, or otherwise and the elements contributing to its cohesiveness, such as trust, cooperation, and reciprocity (Taylor and Wrenn 2003, 4).

5.1.2 Economic Importance of Social Capital

The use of the capital metaphor is purposive, designed to draw attention to the productive powers of such relationships and the needed investment of time and effort for relationships to be formed and sustained. Extending along a continuum from an individual's intimate circle of friends and family to her more distant acquaintances, social capital creates additional opportunities through access to collective resources. What is embodied in the concept of social capital is, therefore, consistent with the arguments of institutionalism—that the relationships among economic actors and the associated societal norms which define and support those relationships influence choice and action.

Social capital produces something of value for the individual possessing it if it results in mobilizing the resources of those who are socially proximate, thereby providing access to something that was initially lacking (Bourdieu 1986, 249; Burt 1992, 11-17; Stephenson 2001, 534). Thus, social capital analysis can make use of Granovetter's (1973) discussion of "weak" interpersonal ties—for example, individuals connected by one or more degrees of separation. As

Granovetter argues, these weak ties function to connect people together in a larger whole, thereby exponentially increasing an individual's access to resources beyond the need for close personal relationships.

Academic literature has evidenced the role and impact of social capital in a variety of socio-economic areas. For example, social capital has been connected to entrepreneurial success (e.g. Meyerson 1993; Baron and Markman 2000), health (e.g. Balfour et al. 1996; Kawachi 2001), civic engagement (e.g. Putnam 1995; Brehm and Rahn 1997), ethnic mobility (e.g. Portes and Zhou 1992; Valenzuela and Dornbusch 1994), and economic development (e.g. Putnam 1993b; Fukuyama 1995; Keefer and Knack 1997; Woolcock 1998). This literature tends to focus on the positive influence social capital has on economic well-being, though social capital can also have a negative impact. For example, organized crime consists of well-developed networks of social relationships which may have negative social and economic impacts on society. In addition, social capital as embodied in ethnic identification may result in ethnic violence. However, for the purpose of this research work the researcher will focus on those social networks which have a positive economic and social influence on the participants of the study.

5.1.3 Production and Reproduction of Social Capital

If uncertainty and hardship cause people to turn inward towards their immediate community and draw on collective cooperation, then social capital and the values that it implies—trust, reciprocity, affinity, commitment—should develop

accordingly. In this sense, social capital becomes a strategic social mechanism for risk-sharing, hedging against uncertainty and crisis. It provides access to necessary goods and services, jobs, and social mobility. Indeed, if social capital does not surface under such conditions of uncertainty and hardship, this has important implications for economic well-being. As Kandiyoti (1998, 561-62) argues, the inability to maintain reciprocal ties based on mutual help and exchange is indicative of growing poverty.

What is unresolved in the literature is whether social capital arises spontaneously or due to strategic investment. For example, an individual may engage in purposive networking opportunities to pursue an employment target, social mobility, or other such goals. Or, alternatively, consider a chance meeting between two individuals which results in a relationship that later yields access to additional resources. According to Bourdieu (1986, 249), networks of relationships are the product of explicit investment strategies. These strategies aim to transform contingent relations into relationships that are necessary and elective. Fukuyama (1995, 95; 2000, 103) disagrees, and argues that social capital is created spontaneously through cultural mechanisms as people go about their daily lives. Fukuyama attributes the maintenance of this spontaneous social capital to iteration. If individuals know that they are committed to living in bounded communities, they develop an interest in their own reputation and in the monitoring and punishment of those who violate community norms.

5.2 Social Capital in the Soviet Union

Contemporary Russia's stock of social capital is partly a result of current conditions, but also draws from its historical legacy in the Soviet Union. Due to structural pressures of the planned system, economic activity in the Soviet Union was often necessarily socially-oriented. While the inner circle of the Party remained impenetrable to the vast majority of Soviet citizens, personal connections—between family, friends, neighbors, and colleagues—tempered alienation. For example, chronic shortages of goods led many to ask for collective help to fulfill needs. Personal connections were used to obtain such things as comestibles, medicine, cars, vacations, housing, promotions, and other such goods and services.

In this sense, money became less important than acquaintances, as it was access rather than ability which determined the goods and services obtained. Given these constraints on the mobility of money, money was generally less liquid than social and cultural assets (Dinello 1998a, 295). As Koroteyeva and Makarova (1998) explain:

Possession of goods or access to services in short supply were clear signs of prestige, indicating one's relation to power. Thus, not only access to goods and services, but, more importantly, contact with those who had this access, became the most valuable resource in the Soviet system... (This) reinforced the traditional system of social connections, providing incentives to invest in reciprocal networks (581).

This use of connections to obtain deficit goods and services, or to pursue other goals, has a very specific term in the Russian language. Called *blat*, this word has no direct English translation. A seminal reference work on *blat*, Ledeneva (1998), defines it generally as “the use of personal networks and

informal contacts to obtain goods and services in short supply and to find a way around formal procedures (1).” Essentially, *blat* was a system of favors and counter-favors of access—it was a distinctly Soviet form of social capital. *Blat* was considered necessary corruption under an economic system which produced chronic shortages and poor quality in many everyday consumer goods. Its use and importance is evidenced by the Soviet proverb “*Blat* is higher than the People’s Commissar.”

As many scholars of the phenomenon argue, *blat* introduced a dualism into the Soviet planned economy (e.g. Ledeneva 1998, 47-52; 2000, 184; Pesmen 2000, 127; Rehn and Taalas 2004, 248). First, it subverted the formal economic system by responding to formal market failures. Public goods were redistributed by those with access, thereby re-directing public, not private resources. Simultaneously, it maintained the formal economic system by satisfying consumer needs, thereby reducing social anomie. The use of *blat* was so effective that Ledeneva (2000) argues it should be considered the ‘reverse side’ of the socialist system of distribution which made the system both functional and tolerable:

In the Soviet period *blat* was less morally reprehensible and therefore more pervasive than other informal or ‘corrupt’ practices, such as informal economic activity or bribery. Being a specific form of social relationship embedded in personal (horizontal, non-hierarchical, compassionate and warm) networks, it became a socially grounded pattern of mentality and behavior, a form of exchange based upon certain ethical and cultural codes (186-7).

5.2.1 The Nature of *Blat* Exchange

The goods and services obtained *po blaty* (by *blat*) may or may not be exchanged in a simple and straightforward manner. Indeed, it could be something as simple as the granting of a specific and small favor—a direct social exchange between two individuals of similar status. Alternatively, the favor could involve several degrees of separation between the granter and the grantee, and could include people of different social strata (Ledeneva 1998, 121). Each favor carried the (unspoken) implication that a reciprocal favor would be granted in the future, though there was no need for the reciprocal favor to be equivalent in size or nature to the original. Ledeneva characterizes this as “reciprocal dependence,” noting that the original favor leaves a “memory” which engenders regard for and trust in the other over the long-term (142).

Blat developed through maintaining contact with past and current colleagues, friendships, kin networks, and so forth. *Blat* networks overlapped with personal networks, but also included occupational access to public resources (Ledeneva 1998, 104). In addition, once one “had *blat*” with someone, that transferred to having *blat* with that person’s social networks. As Rehn and Taalas (2004, 249) note, the efficient functioning of the *blat* system depended on including enough individuals into the network, preferably to the point of multiple redundancies. Generally speaking, diversification of *blat* networks was preferred. As Koroteyeva and Makarova (1998) argue,

Having powerful, high-status people or people with different social and occupational backgrounds in one’s network of social connections could significantly enhance one’s life chances and the possibility of material

return. Thus, the drive for diversification of reciprocal networks became very powerful in the Soviet system (586).

Institutionalist arguments of path dependence and cumulative causation would indicate that this reliance on social capital in the former Soviet Union may be expected to continue in the post-Soviet period absent the destruction of these networks. As is argued by Sik (1994, 2) one would not necessarily expect Soviet (Russian) reliance on relationships with others to automatically decrease due to displacement of the planned economy. As Sik notes, economic and social crises are occurring at least as frequently in the post-Soviet period as they did prior to the collapse of the planned system. Thus, within Russia continuity in the use of social capital is expected. This is consistent with the results detailed below, though the objects and services acquired with its use have changed somewhat with the change in system type.

5.3 Social Capital in the Transition

Though establishing social relationships with others may be viewed as a basic human pursuit, regardless of the accompanying economic system type, there are elements to the transition which may serve to encourage a greater use of social networks for specific purposes such as access to resources and information. The potential contemporary importance of social capital in Russia stems from both the heightened uncertainty during this period of system change and the ineffectiveness of many formal institutions. Both result in unsettling the environment in which individuals go about their daily lives. For example, the retraction of social safety nets, increased fluctuations in income, high inflation,

and lost savings may cause households to respond by calling on their social capital for material help.

As testament to this, documentation on the use of personal networks in the post-Soviet period has seen a recent increase in the literature (e.g. Lokshin and Yemtsov 2001; Caldwell 2002; Rose 2002; Batjatgal 2003). This literature argues that personal, informal networks and the social practices that surround them have become the post-Soviet dominate form of exchange in the flow of goods and services and in the resolution of personal problems. In many cases, individuals are choosing to resolve informally issues that rightly fall under the purview of one or more formal institutions due to the inefficacy of these institutions. For example, social capital can be used to resolve such issues as securing childcare, healthcare, education, and employment, as well as in the redistribution of resources, both monetary and otherwise.

A handful of research projects have begun to connect the concept of social capital to the Russian transition. Published social capital studies in Russia to date include an exploration of social and economic networks created and used by street children in Moscow for survival and social mobility (Stephenson 2001); research on the networks connecting agricultural producers (Small 2002); examination of the relative economic success of the Russian region of Novgorod through a deliberate attempt by local government to create social capital (Petro 2001); an analysis of the social and cultural profiles of new Russian bankers (Dinello 1998a); and the use of informal methods for coping with organizational

failures in Russian formal institutions (Rose, Mishler, and Haerpher 1997; Rose 2000a; 2000b; 2002).

5.4 Research Results

In seeking to identify the use and extent of social capital on the part of participants in this study, the researcher poses a number of questions and scenarios. More specifically, questions are asked which addressed such issues as:

- identifying the immediate and extended family members supported by a single household;
- assessing the extent of a participant's social network of intimate acquaintances, including enumeration of the network, geographical location, and amount of time spent socializing within the network;
- participants' use of social capital to access everyday resources such as housing, employment, food, clothing, and household services;
- participants' use of social capital in response to unforeseen shocks such as loss of a job, a health crisis, or urgent childcare needs;

- identifying formal and informal organizational membership and the level of involvement in such organizations;
- identifying the extent of involvement in the neighborhood, including collective responses to community problems;
- asking participants about their contact with influential people and whether that has rendered any favors or help; and,
- identifying the role of social capital in transmitting information about the transition itself and ongoing adaptation to the rule changes.

Expected difficulty was encountered in accessing information regarding social exchanges such as gifts and favors. These can be context- and culture-specific concepts that are elusive to enumeration or recall. Such exchanges are often rendered almost subconsciously, and certainly often spontaneously. As a result, many participants initially had difficulty specifically discussing the ways in which they give or receive assistance from others in their social networks. As one participant notes, this is difficult to recall as “it does not show itself somehow in the memory because somehow this does not become sharp.” As a result of the often subconscious use of social capital, these questions tended to require somewhat significant reflection and were often accompanied by comments such as the above.

5.4.1 From Soviet to Russian Social Capital

What was clear from the responses was that participants generally called upon what was familiar to them, those habits and norms used during Soviet times, subsequently altering them to respond to new challenges. Burawoy, Krotov, and Lytkina (2000) categorize this response as a “defensive strategy” whereby families transform routines characteristic of the Soviet period into coping strategies in the new period of uncertainty. For example, when asked whether *blat* still exists, the majority of participants (87 percent) state that it does. However, many append that answer to explain that *blat* in its current incarnation has evolved from what it was in Soviet times. It is generally agreed that *blat*, in connection with accessing shortage goods, no longer applies to the post-Soviet period as any sort of good, common or exotic, is available for purchase and consumption. That is, the market mechanism has replaced *blat* transactions as they were in Soviet times. However, *blat* is used in contemporary Russia to obtain those things that were once provided by the state with reliable automaticity but are now beyond the household budget of most ordinary Russians. For example, *blat* comes into play when trying to secure employment or entrance into institutions of higher education without having to pay extortive fees.

Responses indicate that, in contemporary Russia, connections of a more personal nature dominate social exchanges. Though less connected than through multi-layered *blat* networks, study participants rely significantly on their close circle of family and friends. That is, the social network has collapsed and now encompasses the more immediate social capital embodied within intimate

relationships. In this sense, households are turning to their immediate networks to meet basic needs; many such needs are out of reach if households were to rely solely on market exchange.

As evidence, one of the questions posed to participants was whether they believed any goods remained in shortage in the post-Soviet period. With the exception of two replies, participants agreed that shortages no longer exist⁴. However, some append this to remark that money is the new deficit good. As one woman answers when asked if she sees shortages: “Now, no. If there would be money. There is no money.” Another states, “Now, please, choose! If there would be money.” Whereas before, as discussed in chapter 2, a monetary overhang resulted from the inability to purchase desired consumption goods, now monetary resources are increasingly scarce as inflation has stripped away purchasing power and nominal wages have not kept pace with rising prices. A Russian folk saying—the reproach “[I wish] for you to live on only wages”—evidences this.

5.4.2 Social capital and the gifting of resources.

Food is particularly cited as something shared with others. Within the social capital networks identified by the participants, it is taken for granted that food is communal. To begin with, in addition to be provided by the host or hostess comestibles are, without fail, brought when arriving as guest to a social

⁴ The two dissents are trivial. One indicates there is a shortage only of high-quality goods and complains of the poor quality Chinese goods flooding the market. The other tells a story of searching on that day for a particular microwaveable meal and having to search six or seven shops prior to finding it.

event. In the words of one elderly pensioner, "I arrive, they fed me. I am a guest. I arrive as a guest or they arrive to me as a guest and I treat them. No one *gives* food (emphasis added)." Many others, however, disagree by noting that it is accepted social practice to look to others when there is no food. As one woman states, "On this street we do not have a big space between these nearby houses. If I have no bread, I am able to go to someone, to beg." Another says, "If you see that there is nothing [with which] to buy, you go, you ask, they give. You bring to them the same."

That food gifting goes beyond simple socializing is further evidenced by the treatment of the product from household plots. First, such plots are generally considered to be an extended family resource, rather than limited only to the immediate household. The plots of parents are regularly tended to and used by adult children; the same relationship holds true between adult siblings, where multiple households draw from the land. The majority of participants in this study (81 percent) either have their own plot (or multiple plots) of land or use the plots of other family members. This household production, or "householding" to use Polanyi's (1944) terminology, often plays a large role in a family's sustenance as it is used to bridge the gap between what monetary resources can purchase and what is needed to sustain the household.

Second, the surplus from the plot is often redistributed to others. Sixty-six percent of participants who grow their own food choose to give away surplus to neighbors, relatives, and friends and 53 percent admit to receiving food from others. As an example, in those situations where family members are too distant

to help on a regular basis—consider the situation of an adult child living in Krasnodar away from family who have remained in a state farm village—they may regularly receive food grown by those kin in rural areas. Another example comes from a female participant with a large householding plot who regularly gives buckets of fruit and produce to the friends of her children who live in apartments and do not have their own plots.

This sharing of food is considered by many to be part of the Russian culture, a matter of moral and emotional pride. When asked if something was expected in return for rendering such a favor, offense is often taken. As one woman remarks, “Not to give bread—this is simply a sin. This is like a sin. In any case, I must give bread... What else? Salt we also do not give back. Here, such small [things], without which a person is not able to survive.” The single mother of a toddler speaks of the generosity of her neighbor and the neighbor’s refusal to take anything in return:

She usually shares with me with everything. With fruit, with eggs. She treats me like a mother. She even brought tomatoes in buckets when I made tinned vegetables. I tried to give her money and she refused. She says, “You are like a daughter to me. I cannot take your money for these small things.” But she is a housewife, does not make money at all.

Only three participants choose to sell their surplus in any regular manner. One, an unemployed man in his forties, sells his surplus to earn income. A second case is a pensioner in the state farm village whose husband has received irregular money wages from the state farm for years. She sits by the highway or at the village bazaar and sells her surplus in order to earn money income. The third is also a pensioner whose gardening is a main means of subsistence for his

family and also a hobby to fill his retirement years. He regularly sits next to a tram stop to sell his surplus, or people come directly to him at his house. As he notes, "As I am a pensioner, I am always on my plot of land. I work on my soil for my own pleasure... Everything of this [that is] necessary for the family, I take this. [That which is] in abundance—the remaining—I take and sell." When the researcher asks if this is profitable for him, he replies, "I will say one [thing] to you. Here, [I sell] not because of profit. Simply, that the good is not wasted. How must I [waste it]? This is a service to the people. I sell to the people, to whom buys, at very low prices." He then states that he earns approximately \$40 monthly in summer selling his householding product.

In addition to food, surplus clothing and household goods, particularly children's clothing, are also redistributed among social capital networks. As evidence, 94 percent of participants state that they give away things they no longer need. When asked to whom they give these goods, only five participants mention unknown person(s) as recipients, such as donating to a general church fund or to an orphanage. One participant mentions simply putting things out on a street corner, noting that those who need know to come and look for things: "You put things and those that pass by will take. They know that it is always so." The remaining participants state that family and friends are the recipients. In addition, 47 percent acknowledge receiving such things as clothes and household goods, all from those known to them in their inner circle.

5.4.3 Social Capital and Transaction Costs

Social capital also becomes an important resource when an individual is faced with information and search costs as participants call upon those with whom they have social relationships to reduce those costs. For example, 56 percent of respondents reply that if they lost their job they would use their social capital as a resource when searching for a new job. Furthermore, 45 percent of respondents found their current job through the use of social capital. This includes using the connections of family members, particularly parents, to secure employment, contacting friends and asking if jobs are available at their place of work, or receiving invitations to apply for jobs from individuals met in the course of conducting duties at past jobs.

Rendering such assistance in employment searches appears to be an organic reaction to the uncertainty caused by the system change. Employment bureaus are often viewed as ineffective, which prompts many to look to their inner circle of acquaintances. As one participant explains,

As we arrived here, it is natural, there was no kind of work for me. I addressed the father[-in-law] for a post... He offered me a place at a factory. When I decided to change the place of work, I was offered this place by [my friend] Roman. He spoke with the supervisor, he offered my candidature. He helped me. I was fixed up there to work. Then, I retired from there. I transferred to this job where I work now. It happened so that after a year, Roman retired from security and at this moment I offered him work, where he works now. It happens, how? Friend for friend, we so say. He helped me some time, pushed me through. Now, I helped him.

As further evidence of the use of social capital to reduce information and search costs, 83 percent of those renting apartments found their current housing using their social capital. One participant recounts how she had difficulty finding

housing when she moved to Krasnodar from a nearby village. While she was looking she stayed for free in the room of a hostel. This room was offered to her by a friend who worked at the hostel as a chambermaid. Eventually, she found rental housing through another acquaintance. As she explains,

For a month I had a problem. I looked for it [housing] and everybody refused me because there is a baby. So, a parent of my pupil, ex-pupil—I mean private pupil to [whose] home I came and gave private lessons—she helped me. She asked the owner of that house not to refuse me.

Lastly, 26 percent of respondents relied on the expertise and information of others, or decided in a council of family members and friends, regarding what to do with vouchers received in the privatization process. As noted in chapters 2 and 3, transferring ownership of former public resources has proven to be a difficult and corrupted task in Russia, primarily due to asymmetric information between those in the inner circle of business and government and the rest of the population. As one woman states, "...In general we didn't think [anything about the program when it started]. They said to us that this is for us, in general, the vouchers. Everything was new for us. We didn't understand... They said to us, 'Take' and we take." Due to the uncertainty surrounding the transfer of resources, many participants looked to others who might have a better understanding and asked them what to do. For example, one participant had a neighbor who worked as an insurance agent. She felt that this neighbor understood the process better and so she turned to her for advice. Other participants gave their vouchers to family members that they felt would best know how to put the vouchers to use. As one participant recounts,

[I gave them to] the father of my son-in-law. I gave them to him. I say, "Take." He worked then, at that time still. I gave to him: "Take. It will prove useful to you"... What [was there] for us to do with them? With these vouchers? ...I'm not even interested [in what he did with them].

5.4.4 Social Capital and Monetary Crises

The use of social capital is a popular means of coping when faced with a monetary shortfall. Given little ability to actively participate in formal lending markets, participants are limited to borrowing and lending from those within their social network to navigate a crisis situation. The results collected show problems in need of immediate attention are often solved with the help of others, giving borrowing and lending a social dimension as well as an economic one. According to many participants, the ability of friends and family to help is assumed *a priori*, adding much to a sense of security.

As evidence, 96 percent of participants lend money to those within their social network while 74 percent also borrow money within the network. Fewer than half of the participants (40 percent) say that there is a single person who routinely asks to borrow money and even fewer (13 percent) identify a specific person that they typically ask for money. Instead, the entire network is generally viewed as viable for the asking or taking, as there is little economic difference among members of the network. In fact, when asked how they compare with respect to "layer of the population," 89 percent of respondents indicate that they are generally within the same socio-economic strata of those they lend to and 82 percent of respondents indicate that they are generally within the same strata of those from whom they borrow.

There is an interesting exception to the above. In the village of Korzhevski, the owner of the grocery store is recognized for his material position—reminiscent of the “big-man” literature in anthropology (e.g. Sahlins 1963). Generally considered better off than the average village inhabitant, he extends credit to other villagers, most of who depend on the state farm for their income and as a result have significant wage arrears. The owner keeps a list of debts and individuals pay them back as they are able. One participant refers to this as giving goods “under signature,” noting that the act of generosity on the part of the store owner has much to do with the sense of community in the village: “In the town [of Krasnodar] there is no such thing... There, everyone is a stranger... Simply, we live together in one small village and [that is] everything.” Small (2002, 19) notes a similar situation in her Russian social capital study. She states that business contributions to easing burdens on the local community are embedded in societal expectations and calls this a “naturally occurring” form of social capital.

If participants engage in borrowing and lending, this is generally a short-term transaction. The majority of those who engage in borrowing and lending (80 percent) state that the terms of return are made exact at the time of the transaction. Typically, the borrower will say themselves that they are borrowing for a short period of time, or “until wages.” With respect to the remaining 20 percent, many of these participants mention that for small sums the terms of return may not be made exact but for larger sums it will. Generally speaking, participants do not seem concerned that the money will not be returned. One

exception is a woman who had borrowed from a friend on behalf of another friend. She had difficulty collecting and had to repay some of the funds with her own money. She states that as a result, she no longer feels comfortable engaging in such transactions with her friends. Typically, the result is the opposite—participants give freely and remained unconcerned that those they lend to will renege on their requital obligations. Witness the following exchange between a husband and wife:

(Wife) If he says, "I did not manage (to get the money)," then nothing is terrible. But if he tries not to show himself...

(Husband) No. If a person begins to hide from you, we simply will not give to him another time. No, if he has a valid reason, then for us this 'does not burn,' it is not necessary. Then, when it will be [it will be].

One exception to the remittance of loans is the generational transfer between parent and child. These are typically not considered short-term transactions and in fact, for younger participants who borrow from their parents, often the money is not expected to be returned, or is refused if return is attempted. As one participant explains, "For example, the parents are able to give us money. They are able to remit our debt. But if, for example, this [loan] is from someone of the friends, it is necessary to return this money all the same. Not as they require it, but because it is necessary to return this money." Another participant notes that "My mother never, in life, *lends* me money. She will just give it to me (emphasis added)."

Inter-generational monetary transfers generally follow a standardized life cycle. Older adults often materially support their children, including adult children living at home and those who have left the household and started one of their

own. However, once a certain stage of life is reached, typically around the time that the parent begins to collect a pension, transfer payments are reversed from child to parent. In fact, 36 percent of participants note that they expect monetary help from their children when they are too old to work. In return, elderly parents often provide childcare and share the householding surplus with their adult children and their families. This cycle is embedded in Russian society and is taken as an implicit assurance that when a child or parent is financially vulnerable, they will receive help from their immediate family. As one participant states, "Earlier our parents helped us and now we stand on our own legs... And now it happens that we help our parents. Then, help was necessary to us. Now our [help is necessary to them]." Another participant reflects of her pensioner future: "Maybe the children will help us. When we arrived here, who helped us? Only the parents in the first place. And we hope [that our children] will grow and will help. These are the first helpers." Another jokes, "If my daughter marries a businessman, this means that, then, mine and my husband's pension will be enough." As another participant explains,

Children, it seems to me, always will help. There are, somewhere [there] live such people, an old woman alone. Of course, it is so difficult if there is not one *cotok* (one-hundredth of a hectare) of land, only an apartment alone. I understand that it is very difficult to live so, if you are a single person. But so, if there are children, it seems to me [there will be] maybe no shortages.

5.4.5 Maintenance of Social Capital

From conversations with participants it quickly becomes clear that a strong effort is made to maintain a good reputation among family, friends, and

neighbors. By practicing accessibility, this further insures that others will be available to you should the need arise. Thus, social capital is maintained. As an example, time spent socializing with others, such as visiting and receiving visitors, is an important element in post-Soviet life. Among the participants, 40 percent say they receive visitors at least once a week and 43 percent report that they go to visit others at least once a week.

Further maintenance of social capital is interpreted by the majority of participants' willingness to extend spontaneous favors to one another. These favors range from the trivial to the significant, but all are important in communicating a willingness to be called upon in times of need. A sampling of the types of favors provided include urgent childcare, going to the grocery store for an acquaintance that has fallen ill, providing medical advice, helping with household and automobile repairs, and providing transportation for those who are without their own means. Help with burials is particularly mentioned as something important for friends and family to do for one another. This includes collecting money to contribute towards expenses, providing clothing for the burial and laying the table with food and drink at a memorial gathering.

Often, households are called upon to use their own personal and specialized knowledge to lend assistance. For example, a taxi driver who has specialized knowledge of auto mechanics is asked by a neighbor to help prepare a car for testing in order to receive a registration. A state farm tractor driver spends his personal time in the spring helping others plow their private land plots. Though, in a change since 1991 he notes that he now has to account for

all petrol consumed for personal use. A dentist is asked to render dental services to acquaintances and provides these free of charge. Stylists in a salon are often asked by their friends to provide haircuts free of charge. Furthermore, participants are as willing to receive as to give help. A neighbor cooks for one participant's son while they are away on vacation. Several participants receive help with home or car repairs. In addition, childcare is received as well as given.

A reputation for being accessible is further maintained by time spent engaging in social activities with neighbors. Sixty-eight percent of participants say that they knew "many" or "most" of those that live in their neighborhood. When asked if neighbors usually help one another or if each household tends to rely on itself, 79 percent of respondents say neighbors usually help each other. Seventy-nine percent of respondents also say they will ask neighbors to watch their home if they go away and 87 percent say they will do the same thing for their neighbors. This neighborhood socialization includes, for example, celebration of big purchases with one another and "congratulating" one another on national holidays. One participant speaks of making dinner regularly for an elderly pensioner neighbor who is routinely short of food. In instances of medical emergencies, neighbors provide such help as giving injections or tablets. Neighbors with cars provide transportation to work or for errands. As one participant explains, "It is natural. We have very confiding relationships between neighbors, yes. We help each other. In grief and in gladness. Very good people live in our entry."

The *subbotnik* remains as a legacy of the Soviet period. From the Russian word *subbota* (Saturday), the state would designate a certain day and time for citizens to gather and participate in public clean-up efforts. This has remained an important element of neighborhood socialization, though now *subbotniks* are primarily scheduled by neighborhood leaders—typically pensioners well-established and respected in the neighborhood. Neighbors often get together for projects and repairs—83 percent of participants state that neighbors will assemble to respond to a problem in the area. These gatherings are reported to occur at least once or twice a year, and sometimes as often as 10 times a year. Two respondents from the state farm village note that collective gatherings to accomplish repairs and such are non-quantifiable as they are “continuous.” Examples of neighborhood projects include building a soccer field and sandbox for children, collecting money for private security guards, installing a coded door, making road repairs, repairing a roof, and repairs to the sewer system. As one participant notes, “It is necessary to live friendly with neighbors. They say, ‘Do not buy a house, do not choose a house, but choose neighbors.’ This means much—good neighbors. Because at any time you can rely on them.” Another participant states that helping one another is, essentially, compulsory: “This is simply... the sacred duty of a neighbor. To help each other. A mutual connection. Mutual help.”

Neighbors also help to defray costs for those with limited means, or for those who fail or refuse to pay. One participant reports that when apartment house repairs are necessary and some cannot afford to participate, others will

pay for their share so that the repair project can move forward. In another instance a participant tells of a regular problem with seasonal dacha users not paying utility bills for electricity used there. In order to avoid having the electricity shut off for the entire area due to outstanding debts, the permanent residents will collect money to pay for those delinquent in their bills:

...(O)nce in half a year or once a year they collect. Who is a normal person, conscientious person [contributes]. Since we live there, all the same we are interested. Our way of life depends on this, that there will be light. This means everything will be [okay].

With these results, the researcher disagrees with Rose (2000a, 48-9), who argues that social networks (termed “pre-modern networks” by the author) used to produce services with non-wage labor have little to contribute to an individual’s income security as they are outside the money economy. Instead, this researcher argues that the rendering of non-wage labor within a participant’s social capital network appears to have a significant effect at reducing uncertainty by establishing a support group of individuals to be called upon in times of crisis. In this sense, social capital is used proactively in anticipation of future needs. The fact remains that the assurance others will be available to help in times of need acts as an acute reduction to uncertainty.

5.5 Social Capital and Implied Reciprocity

What is also clear from the responses is one element of Soviet *blat* that has remained—the results show a strong relationship remains between the rendering of gifts and favors and the implicit, though not explicit, requirement of reciprocal action. As one participant notes, “It is possible to give a gift [in return

for a favor], but not compulsory. Simply from respect. If I give to her as a present, I do not say to her, 'This is for you for this.' All of this is unselfish." Obligation is, as such, created from the regular and on-going nature of social exchanges; social transactions become part of a flow of goods and services that extends beyond the initial act. For example, one woman explains an exchange that occurred between her family and a neighbor:

(A)t our dacha there lives a man, probably he is...How many years? Like our grandfather, probably 75 if he is not 77. At our dacha we heat with firewood and here we stored firewood. That is, we sawed it to a definite size and packed up the remains in a bag and brought it to him, in order that he will be able to warm himself. He was very glad since he does not have the possibility to buy. He is a pensioner. But he, as a sign of thanks, came, looked at our garden—that is, the apples and pears—and said, "I will help you to prune in order that they bear fruit well."

Another man explains of an implied understanding between his siblings and himself: "When our mother died, then here I was not able to do anything, to give for the burial. Mainly, the sisters and the brother buried. But I compensate now. I go to the grave. I always tidy up more often than anyone." Another man tells of a current implicit understanding with some friends: "There were times when I gave a very large sum [of money] and for a big term. And I lost very big money because of this, because of inflation. Since these people still are my friends, here they consider it their duty to help me, namely, now."

Thus, the transactions may be characterized as a reciprocal form of integration (Polanyi 1957, 250). Defined as "movements between correlative points of symmetrical groupings," the reciprocal form of integration is governed by the implication that these social relationships will persist into the future. In this manner, a specified return for any favor or gift is absent. Instead of expectations

of obligations the reciprocal relationship is one of implicit knowledge that, in the future, others may be counted on by the gifting party. As one participant explains,

[Take], for example, Marina. She offered me... In the past I taught her and her son English. She was going to leave for America to work for the farm. And very often I visited her, maybe three times a week, and gave her lessons, taught her English. She offered me money not once [but many times], but I refused. I say, "Just remember me, that I would love also to go to America. Maybe if there is a possibility please remember me."

According to Polanyi, a smoothly-functioning system of reciprocal relationships requires a pre-existing definite institutional arrangement. More specifically, he discusses the pattern of symmetry as it applies to groupings. As argued here, this definite institutional arrangement was in place due to the pre-transition norm of *blat* and its embeddedness within the Soviet economy. That is, the reciprocal nature of an individual's social capital relationships was both organized and validated beforehand via the Soviet legacy of *blat*.

The results also conform with Polanyi's (1957) assertion that "the closer the members of the encompassing community feel drawn to one another, the more general will be the tendency among them to develop reciprocative attitudes in regard to specific relationships limited in space, time or otherwise (253)." That is, the norm of reciprocity is sustained by socialization and social sanction, resulting in transactions having simultaneous economic and social characteristics. The collective sense of mutual responsibility which ensues insures that resources will be available in times of need if they are so requested. As one participant explains,

We are on mutual assistance. In general, our Russian mentality is simply so, we treat each other humanely. So a friend arrives, or you go on the street, [they say to you], "Give a light!" [I say], "Take!" And [that is] everything. There are no such economic relationships. So, a rendering of a small service to each other. Today to me, and tomorrow to someone [else]. So, here, they build relationships for themselves.

5.6 Conclusion

Institutionalism argues that the economic sphere is inextricably linked to other elements of society, including the informal institutions that define social relationships. Furthermore, this holds true for all economic systems, be they market-based or otherwise. If man is a social animal, there is an unavoidable connection to and interaction with others. However, it is the opinion of this researcher that the dependence on social capital observed in this study far exceeds that which might be witnessed in advanced market-based systems. Economic upheaval and the resulting uncertainty have created an environment where basic needs cannot be met without the help of others.

The above discussion shows clearly there is a social norm of close bonds and dependence among a participant's circle of family, friends, and neighbors. Individuals and households do not live isolated from their larger extended family, nor from their communities or circle of friends. Social assets are used to diversify risk and a communal safety net is constructed and maintained as an informal insurance mechanism to reduce vulnerability. These assets are used for everything from the everyday acquisition of goods and services to securing a job to borrowing and lending money. Without these assets, these participants would find themselves in a much more precarious economic position. Social capital is

maintained through frequent socializing and a generosity of spirit in helping others. By so doing, an individual insures that he or she will be able to turn towards those they know at later periods if this is necessary.

Thus, in this chapter a step has been made towards identifying elements of the informal institutional environment in the transition. Social capital remains an important resource in contemporary Russia and is often used to meet even the most basic of needs. At the onset of transition, an institutional environment of inter-household networks was already present due to legacies from Soviet times. Thus, this presented an obvious resource to draw upon when confronted by challenges of the transition, though the pre-existing institutional arrangement has been rearranged to meet the needs of current times. Most significantly, networks have collapsed inward, replacing weak ties with strong ones.

The following two chapters will continue the researcher's qualitative data analysis through continuing discussion of informal institutions. To be addressed next is the role that cultural values play in the new environment. The change in rules necessitates a tolerance for new values and behaviors more appropriate to a market-based system. Given the potential for values from the previous era to persist, and thus interfere with the new rules, analysis of value adaptation may provide important insight into norm accommodation of new rules.

Chapter 6: Cultural Preparedness for System Change

Every socio-economic system type presents a unique set of values according to which economic actors operate. System change can, therefore, be stymied by a lack of corresponding change in cultural values which cause economic actors to reject the conditions under which the new system must operate. On the other hand, if the values of economic actors do change to accompany system change this may greatly promote the smooth functioning and development of the new system.

The purpose of this chapter is three-fold: (1) to discuss the contrast between particular values inherent to the Soviet planned economy and those required for a market-based system to flourish; (2) using results from the research study, to identify changes in values that have taken place to engender cultural support of the new system type; and (3) to identify whether evidence suggests that there may be legacies which remain from the values of Soviet times that serve to impede system change.

First, a cursory exploration of significant values from the Soviet period is presented. A few choice cultural patterns are discussed in order to put analysis of the field study results into context. Following this is a discussion of necessary value changes required in the Russian environment for transition towards a market-based system to proceed. The results of the field study as they pertain to

this particular topic are then presented and discussed. As is consistent with the evolutionary-institutional view of transition, the field study's results indicate that the process of cultural value adaptation is proceeding unevenly.

6.1 Soviet Cultural Legacy

Any attempt to fully capture the values and mores of the Soviet period would take much more space and depth than this research work will allow. As a result, a few choice Soviet cultural characteristics are presented as they most directly put results from this research study into historical context. Specifically discussed are: (1) cultural influences on the Soviet perception of the "market" and the use of money as an anonymous exchange mechanism; (2) the Soviet social dynamic of egalitarianism plus hierarchy; (3) Soviet civic culture; and (4) the maternal role of the Soviet state.

Much of what follows is inspired by Kornai (1985, ch. 7) which presents an excellent discussion on the contradictions between the ethical principles of a socialist economy and those of a capitalist one. More specifically, Kornai addresses the socialist principles of egalitarianism, solidarity, and security, as well as the emphasis on societal needs over those of the individual. He evaluates these principles in contrast to those exhibited in a capitalist society and concludes that in the Hungarian economic environment of the time, individuals and firms were not subject to the "laws" of a competitive market.

6.1.1 Perception of the Market

Suspicion of the anonymity of market-based exchange extends as far back as tsarist Russia, particularly in the more primitive agrarian economies of the peasant village where most exchanges were settled by communal decree through the *obshchina* (village commune) rather than the market (Gerschenkron 1965, 120-24; Pesman 2000, 126-7). The overthrow of tsarism and the establishment of a politico-economic system based on the tenets of Marxism-Leninism furthered a suspicion of market exchange as the ideological foundation in Marx's labor theory of value promotes the idea that real economic activity can only come from production. Therefore, the use of labor to generate surplus value in the form of monetary profits is tantamount to exploitation. This argument was solidified into public consciousness through routine reproduction in propagandistic speeches and slogans and was reinforced by the dynamic of the enterprise collective. In addition, the correlation between money, exchange and exploitation is supported by Orthodox Russian religious ideology (Dinello 1998b). As a result, a generally negative attitude towards money-based exchange, profiteering, and speculation continued during Soviet times.

In addition, as discussed in the previous chapter, chronic shortages resulted in unequal access to goods and services. The material ability to pay was insufficient to procure most goods. Instead, Soviet culture evolved to emphasize the social nature of exchange as relationships were used to access deficit goods. Therefore, money as a universal form of liquidity was never fully absorbed into Soviet culture. As Jowitt (1983) states:

Blat emphasizes the status and personal nature of social transactions. Social exchanges associated with the term *blat* are not simply or primarily functional arrangements expediting the performance of economic tasks in situations of scarcity, urgency, and unpredictability. *Blat* relationships and exchanges are status-type substitutes for the impersonal/individuated predictability and standardization of a market economy and electoral polity (280).

Thus, the “market” was predominately social, profiteering was suspect, and not everything was reducible to (anonymous) monetary terms. As evidence of this, Shiller, Boycko, and Korobov (1991) compare American and Soviet responses to a series of questions addressing attitudes towards free markets in May of 1990. They find evidence to indicate that Soviets were less willing than Americans to accept exchange of money as a solution to their problems, that there was less respect for businessmen in the Soviet Union, and that there was general opposition to speculation.

6.1.2 *Egalitarianism*

Notions of equality and solidarity are also fundamental to communist morality. The intention of the 1917 Revolution was to level the social and economic differentiation of tsarism. To accomplish this, private property was abolished and the means of production were socialized. It was argued that by so doing, there would no longer be fundamental differences in the economic position of individuals relative to one another. As an ancillary benefit, the elimination of private property also established the Party’s monopoly on power.

The lesson taught was not to improve oneself at the expense of others, as evidenced by the popular Soviet proverb, “It is not offensive that the wine is

expensive; it is offensive that the innkeeper is getting rich.” However, even if not viewed as a zero-sum game, individual initiative to improve one’s economic position was also stifled. As Kon (1996) argues,

Individuality was suppressed as a sign of bourgeois individualism incompatible with the virtues of the New Soviet Man. The primitive egalitarianism in wages, the fear of competition, and especially the bureaucratic mentality that equated the individual with a “cog” in an impersonal clocklike social mechanism conspired to stifle personal initiative (193).

The show of equal economic footing was accomplished, from a practical standpoint, by assuring that Soviet citizens were knowledgeable of where they fell relative to others. This transparency came from the sharing of financial information. For example, when pay was received the Soviet worker typically signaled his receipt via a signature on a paper which listed each individual and their pay. This served as a leveling mechanism, as did the requirement that each able-bodied individual provide her labor power to the state. Thus, equality in pay and effort was to be assured.

6.1.3 Hierarchy and Privilege

At the same time that leveling was accepted for the Soviet masses, a hierarchical structure was in place in the upper level of society. Power came from one’s political capital as measured by proximity to and placement within the Party-state apparatus. This was furthered by the establishment of the Soviet *nomenklatura*, the Communist Party’s ruling elite, which allowed the Party to control who was appointed to administrative positions. It was clear who was, and who was not, considered *nomenklatura* and thus individuals were reminded of

their place. Jowitt (1983) argues that this hierarchy was sustained through the socialized nature of transactions in the Soviet Union. As he states, "Exchanges based more on reciprocity than standardized exchange indicate and sustain a polity based on mutually exclusive status; e.g. nobles/serfs, big-men/small-boys, or Soviet cadres/Soviet citizens (280)."

Those that managed to obtain status and power found themselves at a significant advantage. Status and power meant that a preferred job could be secured, as could placement of one's children or other close relatives in coveted institutes of higher education or jobs with access to special privileges. There were also special shops for the *nomenklatura* which enabled access to deficit goods and imported products. Social position was, therefore, often demonstrated through consumption and use of coveted goods (Koroteyeva and Makarova 1998, 583). As another example, in Moscow there were special car lanes for politicians so as to make the commute to work more convenient. The *nomenklatura* also had access to special hospitals and clinics, vacation houses, and international travel (Shlapentokh 1989, 208). A loss in status would translate into a loss of such privileges; therefore, status had to be maintained. Loyalty to the Party-state apparatus was one way to assure that privileges would be protected. As a result, anything which served to alter the status quo was looked at with suspicion, further stifling individual initiative.

6.1.4 Civic Culture

Soviet civic culture tended to be predominately apolitical and passive. An individual's fate was relatively uncorrelated to his or her individual initiative. As a result, those without privileged status tended towards passive acceptance of the status quo. The popular Russian eponym *oblomovschina* is used to describe this cultural value. Derived from the name of the indolent lead character of Ivan Goncharov's 1858 novel *Oblomov*, *oblomovschina* translates generally into "sluggishness" or "indecision," though it represents something far more complex within the Russian character. It describes the disenfranchisement of the masses and the lack of individual initiative in Soviet culture. Faced with a certain frustration and futility, the Russian succumbs to *oblomovschina* by projecting an attitude of learned helplessness. As Dobrolyubov (1969) explains,

Even the best educated people, people with lively natures and warm hearts, are prone in their practical lives to depart from their ideas and plans, very quickly resign themselves to the realities of life, which, however, they never cease to revile as vulgar and disgusting... Many even reach such a stage that they cannot conceive of man working willingly, with enthusiasm (340).

This learned helplessness was apparent in citizens' treatment of the electoral process. The one-party system of the Soviet Union left most elected positions uncontested, or at a minimum created limited differentiation among candidates. This created a culture whereby voting was seen as a citizen's duty rather than an expectation of influence. Etkind (1996, 114) proposes that this is evidenced by the Russian word for the verb "to vote"—*golosovat'*—which translates literally as "to exercise one's voice." The author argues that this created the psychological impression in the electoral process that Soviet citizens

had the right—and duty—to voice their approval for the leaders and their public pronouncements.

6.1.5 Maternal State

Ideology avowed that the Party and state had the Soviet citizen's best interests at heart; the citizen would be taken care of by the state. To this end, the state provided almost 100 percent subsidized housing, health care, and education. In addition, the state guaranteed employment and ensured that wages allowed for a minimum standard of living. Other benefits included an 18-month subsidized maternity leave for new mothers and enterprise-based child care. In addition, transfer benefits were provided to retirees, the disabled, and children. Additional transfer payments were also established for collective farmers, civil servants, and the military (Cook 2002, 107).

Thus, the role of the state in providing for the economic well-being of its citizens led to the expectation that most basic needs would be met even in the absence of significant individual effort. Bakacsi et al. (2002, 78-9) describes this as a strong "power culture," or a tendency on the part of individuals to avoid responsibility, depend on superiors, and expect care from them. The stability provided by the state further meant that the vast majority of the population was able to shield themselves from excessive uncertainty and risk. As a result, a strong culture of uncertainty avoidance developed which further contributed to stifling innovation and active pursuit of influence and change.

At the same time individuals looked to the Party-state apparatus to meet basic needs, they did so amid an air of distrust. This resulted in a duality to Soviet life. In public, most pronounced respect and support of authorities. In private, the tone was significantly more supercilious. The hypocrisy exhibited by those who abused their privilege, while at the same time demanding the ordinary Soviet accept that she had no such autonomous rights, resulted in disenchantment and disrespect of those in authority. As evidence, witness the following popular joke which surfaced in the 1950s and continues to be heard today: "God gave man three virtues—intelligence, honesty, and Communist Party membership. He stipulated, though, that any one person could choose only two of these three virtues." Levada (1996) discusses this duality of Soviet life and its impact on public consciousness. As the author notes, "On the one hand, this culture breeds widespread fear, obedience, and sycophancy; on the other, it encourages rebellion and contempt for any authorities or law among the Russians (300)."

6.2 Values and a Market-Based System

The development and functioning of markets as the dominant form of exchange requires a contrasting set of values to those discussed above. To begin with, an individualistic ethic must replace the role of the state in the assignation of responsibility. Instead of state provision of most basic needs, individuals must accept general responsibility for themselves and their well-being. This development of an individualistic ethic is naturally promoted by the

establishment of individual rights. That is, power must be dispersed to a degree that an individual has an appreciable impact on her fate. Much of this dispersion of power would result from the establishment of private property rights and the freedom to pursue entrepreneurial activities and engage in private enterprise.

However, the individualistic ethic requires more than a change in legal rights. It also requires economic actors to value individual initiative and innovation. This is promoted through reward for individual initiative. Because private enterprise is proliferated through the pursuit of entrepreneurship and entrepreneurship is most directly motivated by profits, the profit motive must become the dominant incentive. In order for the profit motive to become part of the public consciousness, reward must be commensurate with effort and competence. In addition, arbitrage and speculation must be tolerated as legitimate economic activities. The use of money as an anonymous facilitator of exchange must also be tolerated. That is, economic actors must be comfortable with an exchange relationship that is not based on a social relationship.

In addition, the Soviet ethos of egalitarianism must be replaced by a tolerance for income inequality. The social Darwinism of markets necessitates that economic advancement is the product of initiative, competition, and struggle. Success is rewarded through such mechanisms as private property and variegated wages. Thus, individual pursuit of economic success becomes a positive quality, rather than one viewed with suspicion and envy. As illustrated by the "tunnel effect" of Hirschman and Rothschild (1973), the relative economic success of others in one's peer group should imply a potentiality for upward

mobility. As Hirschman and Rothschild explain, "The tunnel effect operates because advances of others supply information about a more benign external environment; receipt of this information produces gratification; and this gratification overcomes, or at least suspends, envy (546)."

In addition to expecting individuals to take ownership of their economic well-being, a market-based system also implies an activist civic culture in which individuals participate in attempts to influence the course of events. Therefore, the culture of *oblomovschina* must be displaced by one of political participation and engagement. In this manner, a democratic political system is promoted.

6.3 *The State of Affairs in 1991*

Thus, in 1991 at the onset of the transition there existed a set of cultural endowments that came into direct conflict with values more appropriate to the functioning of a market-based system. First, public consciousness in the Soviet Union generally reflected a suspicion towards money as an exchange mechanism and towards profiteering and speculative activities. Acquisition of goods was accomplished through social connections rather than monetary means. At the same time, speculation and arbitrage was denounced as contrary to the Communist ideology established under Marxism-Leninism.

Second, ideology sought leveling; however, this occurred in the face of a deep-rooted system of hierarchy. Those lucky enough to benefit from their privileged status were not inclined to upset the status quo for fear of alienating themselves from those on which their privilege and status depended. The result

of this egalitarian plus hierarchical dynamic is a Soviet culture which de-emphasized innovation and creative thinking, stifled the possibility for self-directed improvement of economic well-being, and promoted the needs of the community over that of the individual.

Thirdly, apolitical passivity and disenchantment led to the absence of political agitation and attempts to influence the state. This can predominantly be blamed on the perceived hypocrisy of state authorities, who preached for others to do as they themselves did not. Soviet citizens became sufficiently disenfranchised so that political participation was characterized by duty and obligation, with no expectation that any one individual may be able to influence the course of events.

Finally, the sense of security which resulted from the role of the state in everyday affairs left individuals with the belief that the state represented the interests of society. Furthermore, there was an expectation that a certain standard of living was to be guaranteed by the Party-state apparatus.

The question now becomes: How do these inherent contradictions translate in the new environment? That is, has the imposition of formal rule changes resulted in a change in values sufficient to promote the development of markets? Or, alternatively, do Soviet-era values persist and interfere with the transition reforms?

6.4 Research Results

To investigate these contradictions, this research study includes a series of questions which seek to identify the current state of cultural values. For example, participants' reactions are explored to such phenomena as income differentials, speculative activity, civic engagement, state retrenchment, and self-determination of economic well-being. More specifically, the researcher seeks to identify the proportionate levels of value continuity versus value change. As the results show, contemporary Russia is experiencing a dynamic and uneven process of change consistent with the institutionalist belief in the evolutionary and incremental process of norm adjustment. While some values consistent with a market-based system are becoming increasingly tolerated, others remain anathema to public consciousness.

6.4.1 Egalitarianism or Inequality?

Contemporary Russia is characterized by a level of income stratification greatly exceeding the income differentials of Soviet times. As argued in chapter 3, some of the blame for this may be assigned to the insider bias of the privatization process whereby there was significant asymmetry with respect to access to the most valuable resources. In addition, the move from public to private employment removed all wage controls which further exacerbated income differentials. As discussed above, this situation is in direct contrast to the ideological foundation of the Soviet Union; however, income inequality is generally consistent with the incentive structure of a market-based system.

From the perspective of the participants in this study, this increasing income inequality is viewed as detrimental to social harmony. For example, 45 percent of respondents state that differences such as education, wealth or religion cause problems and when asked which presents the greatest challenge, money and material position is most often cited as the most divisive element. These results indicate that income stratification in contemporary Russia is a cause for concern among participants, rather than welcomed for the opportunities it presents. That is, rather than acting as an incentive, income differentials are viewed negatively.

Thus, a “comparison effect” appears to be dominating a “tunnel effect” (Senik 2004, 2100). This effect is more consistent with the institutionalist literature, which argues that conspicuous consumption and invidious distinction both serve to detail differences in ability of goods acquisition. For example, Veblen (1909) addresses the relative nature of utility when he argues:

Indeed, it may, e.g., be true, as is commonly believed, that the contemplation of a wealthy neighbor's pecuniary superiority yields painful rather than pleasurable sensations as an immediate result; but it is equally true that such a wealthy neighbor is, on the whole, more highly regarded and more considerately treated than another neighbor who differs from the former only in being less enviable in respect of wealth (632).

As evidence of this comparison effect, many participants feel that rising inequality is affecting the relationships among people. Income inequality is often mentioned as resulting in people being less helpful and friendly to one another. As an example, one participant notes that those who have a higher economic position “push aside” those in a lower economic position. Another argues, “It seems to me that very many people work, they pay attention to how much money

to earn. And they pay less attention to the family and they socialize less with the neighbors. Simply, no time remains for this.”

Conversations with participants also evidence a palpable level of envy for those who have captured riches from the changes. Often, these individuals are described as “steep,” Russian slang for those who exhibit an air of superiority and/or invulnerability. As one participant notes,

Now, we have rich people appear, very rich people. Evidently, for them there was some kind of favorable period of time here, this situation, and they began... They found, where to apply themselves and now they are becoming rich. It is natural, they avoid people... Simply, it is cold between us.

Another states that, “...rich people, they, so to say coarsely, they got fat [from the transition]. For example, if a person is lower, of the middle level, they do not consider him as people.” In addition, the lack of a middle class is a cause of concern. As one participant notes, “We do not have enough people from the middle wealth in Russia. Because when there are people from medium wealth, then everyone stands united, supports them more.” At the same time, the rise in homelessness and unemployment is also a cause of shame for the national character, with the individual often blamed for his or her predicament. As one man explains,

If they ask me, “Are you for the poor?” I [answer that I] am a big opponent of them. They themselves made themselves so. How is it possible that a 35 or 40 year-old person does not earn a living, he does not support a family, if we are pensioners and do not leave work? Then, here, they loaf about, they do not work, they go begging. And this is only a disgrace to us.

However, notwithstanding the divisiveness of differentials, when participants were asked their views on the new Russian rich, the so-called

oligarchs, responses are mixed. For example, participants are more likely to say they agree that the new rich work hard (almost four times as many agree with this as disagree) and help the economy grow (almost three times as many agree with this as disagree). At same time, a clear majority agrees that those who have made money during the transition use connections to advance their material position: eight times as many say they agree rather than disagree that this is the case. Responses are more evenly split when participants are asked whether they believe these individuals take advantage of others and whether they believe that they are intelligent: an almost equal number agree versus disagree.

Lastly, when asked if they feel those with newly acquired richness act with honesty, most participants refuse to speculate though, on occasion, there is a derisive comment. Witness the following exchange between researcher and participant:

Question: [Do you consider those who have acquired riches to be] honest?

Answer: Honest and rich? It is difficult to say. The moment of attainment of riches is most likely not honest. When [there is] capital, then it is possible, an honest business and everything other.

Question: Therefore, in order to get the capital you have to be dishonest? And then you can be honest?

Answer: And then, yes, then a legal business.

Another participant states, "But you see some who do not have people work for him and [you think], 'From where is this money returned to him?' I do not understand." Still another argues,

...There is a caste of rich people who are able to receive connected information and to earn money... In the course of economic reform legally,

really, not one person increased his income. Like there is one American anecdote: Journalists address an American and they ask a millionaire, "How did you make your money?" He answers, "I am ready to reveal 100 percent for each cent, besides the first million dollars."

One participant actually finds a positive aspect to the emergence of this class of wealthy Russians. When asked what she would do in the event of a financial emergency, she replies:

In this crisis, I would find myself work, any kind of work, and I would not die of starvation. Now we have the possibility to find a job at any age, only do not be lazy. Yes. First of all, we have many rich people who have made an appearance who require a laundress, [someone] to cook in the kitchen and to watch after children. This is possible to find such work. And people will say "thank you" by paying wages and, more, will give out unnecessary things.

6.4.2 Development of an Individualistic Ethos

As argued above, self-reliance and individual initiative are at the foundation of a market-based system. As such, part of the necessary changes in informal norms would be the acceptance of the predominance of individual responsibility for economic well-being. Though the reality of individual responsibility becomes clear as the state retrenches from the provision of critical goods and services, this may or may not translate into acceptance of such retrenchment. As a result, the researcher attempts to assess the participants' perceptions towards the withdrawal of the state from everyday affairs.

Responses indicate that this change in values is proceeding unevenly and that participants are still in the process of struggling with what should be the appropriate level of state involvement in everyday life. For example, some participants acknowledge that the biggest change facing them since 1991 is

learning to rely on themselves in the new socio-economic environment. As one participant explains:

First of all, I understood that now you rely, mainly, only on yourself. If [to consider how it was] earlier, we felt that there was some kind of forecast, even the education of our children. You knew that when you would finish at the institute you would be assigned somewhere to work. And now, in principle, it is necessary to rely only on our own strength.

Another participant acknowledges that the state still provides necessary benefits that establish a minimum standard of living, but that the bulk of one's economic position depends on that person herself:

For example, [the state provides] medical insurance, 10, 11 years of education. We could say it so, that the government gave this, medical service. Here, some kind of step, yes, the government gives. But from this, what remains for you on this step, this depends on you.

Another participant feels the development of an individualistic ethos to be a positive influence on Russian society:

As I see that people used to have, in the past, stable work. They say, "Oh we were sure of tomorrow, because everything was stable." But now, not so stable. But you must work with your brains—[learn] how to survive, how to make things. And, in the past, people hoped for the state, that there are guarantees. I think, [this is] not very good. Because your brains are stable, not moving. And nowadays, your brains must work.

Another participant complains that the Russian culture has not yet developed enough of a forward-looking perspective on self-sufficiency:

[My sister] Zinaida and I talk about this, "Why do people sometimes borrow money?" Not all people think about tomorrow. Today—it is splendid. But nothing for tomorrow... Here when I served in Germany, the Germans were interested in this question. They had everything noted down—what was earned, what is spent. This is for tomorrow. They had a list, they wrote it down. For our Russian character, this does not occur.

Another participant explains that he understands well the nature and requirements of the new system:

Let it be so, here we will say what is the aim of the economy: this is the securing of unlimited wishes by limited resources. If the wishes of a person are unlimited, then simply as I consider it, a reasonable person must put together an estimate of his expenses. What he is not able to permit today, he must strive for in order to permit himself to receive this tomorrow.

Appreciation is often expressed for all of the positive changes that have taken place with respect to individual liberty; however, it is recognized that the dominance of individual rights over the rights of the state has come at a price. For example, the inability to vacation at health resorts is mentioned by several participants. Vacation passes to resort areas, previously given out by enterprises, generally are not available to anyone working in the private sector. Those in civil service do have access to certain passes, but these trips are not subsidized at nearly the extent they were previously. As a result, most ordinary Russians are priced out of the market. As one participant notes,

From one side, we began to speak freely—freedom of word. That people have the right to build what they want. And if there is a brain in the head then they have the possibility to earn money, to become richer than they were. But from the other side in the time of communism, officials and simple people [alike] were able to go to the health resort for relaxation. But now a simple person is not able to permit himself [to go], here it is so. We had Pioneer Camps, passes so that nothing could be taken from oneself (*so that it does not cost anything out of pocket*). But now you need money for everything.

Two other benefits that routinely come up in conversation are education and health care. Previously subsidized at very high levels, most Russians are not able to afford consumption of these services at market prices. Most students at state universities, for example, necessarily come from wealthy families given the fees involved. As one participant complains,

The worst thing, this is that all of the medical services started to be paid. Expensive imported medicine. For pensioners this is very difficult. And education. All the same, the middle and poor are not able to educate their own children for free. Money is necessary. Money, money (*these two words said in English*) decides everything.

There are more inexpensive private universities, referred to as “commercial” universities, but they are considerably less prestigious and graduates with commercial diplomas do not command nearly as much in the labor market. However, one participant who relies on the state to a significant degree to provide health care for a disabled child is quite glad for the help that she receives:

For example, he receives medicine for free which is particularly necessary. Of course, services are also free of charge. And, for example, if he has some kind of catarrhal sickness, some of the medicines are also given absolutely free. Some tests, they are absolutely paid for everyone... It would be very difficult [if the government did not help].

Lastly, the wages of civil service workers are a common subject of complaint.

For example, this research sample includes participants who are doctors, teachers, or daycare workers employed by the state and most make less than \$150 a month. One participant expresses a significant level of frustration as she talks about this:

They promise. Everyone promises to increase the wages of the children. Mainly, this. And our pension. Here, now we wait. They promise us. Here, now how many years? I think that we deserve such a pension, for it to be sufficient, for the children to learn. [I have a daughter] with higher education and [they pay her] 2,000 [rubles a month as a daycare worker]. We hope that she will receive [more] for that, that they study so many years.

In addition, notwithstanding the withdrawal of state-sponsored benefits, the vast majority of participants still expect the state to provide an old-age

pension. For example, 83 percent of respondents who are still in their working years state that they expect to rely on their state pension in their retirement years. Though admittedly, in fact most participants have little opportunity to save for retirement themselves; only two participants argue that it is not necessary for them to save while 66 percent of respondents who do not save now cite a lack of funds as a reason.

6.4.3 *Contemporary Civic Culture*

In an attempt to determine whether the development of a pluralistic political system translates into increased civic engagement, the participants are asked about their level of political participation. This includes inquiries of recent voting history, any demonstrative or protest activity, contact with politicians or other influential people, and any political campaign activity.

From the interviews, it is clear that this group of participants does not exhibit the *oblomovschina* of Soviet times. As one participant explains,

The questions of democracy for today stand more real. Therefore, I believe in that, that simple people are able to influence political methods with their own vote. That is, the elections, voting, you influence politics by such methods... Because during socialist times there was practically no choice during elections... Today there is choice, there is competition among political parties, in the course of political directions. Today there is competition, there is struggle, there is choice and subject to that, as far as I believe in someone, I give him my voice.

Though a few participants state that they do not vote as they believe elections are programmed, the vast majority of participants, 85 percent of them, state that they are active voters. In addition, 79 percent of participants voted in the two national elections during the researcher's tenure in Krasnodar—the December

2003 Duma elections and the Presidential election in March 2004. When asked why they vote, many participants cite feelings of patriotism and duty. As one participant notes, "You know, at the very least it is necessary to vote [even if it is] against everyone. That the right of voice does not disappear." And as another participant explains,

The main [reason to vote]—in order for there to be stability, that there will not be a new shock, in order that there will not be a new revolution. Although, the potential possibility still exists, this, the communist party and Zhirinovski and his "liberal" party. If they come to power, a crack will come again, a new revolution and new problems in connection with this. Therefore, it is necessary for us to choose, to attentively spend time on the programs of the deputies and to correctly orient ourselves in order not to choose a new revolutionary party, new people who will make a revolution. This is not necessary for us. For today we have a democracy, we must correctly utilize it, correctly make use of it.

Interestingly, one man is motivated to vote due to his suspicion of election officials. As he states, "To vote, of course, is necessary. Why? Because [if] the voting paper remains, they will take [it] all the same and will write who they wish there."

A number of participants are even more aggressively involved in politics through activity in a political campaign. Two participants are agitators for the political party *Edinaya Rossiya* (United Russia). One participant, a small business owner, has run for office himself, campaigning for a seat in local government. Unsuccessful in his campaign, he complains that the voters hold unrealistic expectations about local politics. As he explains,

Expectations from elections are such: tomorrow everything will change immediately... If the elections are local, it is necessary to decide local problems. What kind of idea [is it] for the deputy of the City Duma to talk about that, that he will repeal some kind of law in Moscow (27)?

Additional civic activism is apparent from other activities. For example, 17 percent of respondents have taken part in a demonstration or protest in recent years, typically organized by trade unions in attempts to increase the wages of civil servants. During the researcher's visits to the state farm village of Korzhevski, there was a grass roots uprising against the sacking of the state farm manager. They gathered together to meet with officials of the state farm's rice institute to lobby on the manager's behalf. In addition, 15 percent of participants have contacted a political representative in recent years while 21 percent have contacted someone they consider an "influential person." Lastly, four participants, two married couples that are close friends, have engaged in a long (and successful) campaign to re-establish student honor guards at what they refer to as "Post #1 by the Eternal Fire"—a memorial to soldiers lost in World War II. They explain that they are motivated to re-establish the tradition in order to educate youth about Russia and the war. As one of them states,

Unfortunately, not the entire generation, that is many of them do not even know that there was a war. That is, that all of this occurred. And now, we began to attract schoolchildren, in order that they stand at Post #1. Namely, [this is for] patriotic education.

This significant level of political activism, however, does not translate into a strong perception of increased power. In response to the question "How much are you able to influence your environment?" the participants are fairly evenly split between able to influence (53 percent) and not able (40 percent). In addition, though 45 percent say that their level of influence has increased since 1991, a closely similar proportion of participants (48 percent) say their level of influence is unchanged. A sense of solidarity is apparent in many of the

comments regarding the participants' ability to influence their environment. As one participant quips, "Without kopeks there will be no rubles." Another remarks,

One person is a drop in the ocean. But all the same, somehow, yes it is possible to unite people. That is, here it is so—one person cannot decide something. But here when [there is] one plus one more—it is possible to decide together. [But I have] no personal influence."

6.4.4 *Understanding the "Market Economy"*

In the interviews, the researcher poses the question "How do you define a market economy?" Though even in the advanced market systems of the West individuals may be hard-pressed to define a market economy as a trained economist might, the question is asked as it is believed that answers can illuminate, to a certain extent, how the participants explain the market economy to themselves.

The question is sufficiently difficult to cause 38 percent of participants to decline to answer. Most cite lack of education or knowledge as the reason for their refusal. A few state that they are not interested in discussing the subject. As an example, one participant states, "In general, I do not want to understand anything. I consider that this is stupid. I do not even want to look into the market economy. It is not possible to change anything."

When answers are attempted, definitions range from simple explanations—such as "when [there is] an abundance of goods, some kind of choice"—to more complicated explanations of production and exchange. Only two participants use economic vernacular, noting the relationship between demand and supply. However, most definitions tangentially touch on this. For

example, “trade,” “exchange,” or “relationships among market participants” are common themes in 29 percent of answers, particularly Russia’s engagement in international trade.

Proliferation of private business is also a common theme in 15 percent of answers, notably the development of small business and sole-proprietorships. As one participant explains, “[A market economy] is when people live by account of the sale of any of their own private products which they produce or which they buy in one locality, then transport to another to sell for another price.” One participant argues that a small business specializing in services is preferable to a large-scale enterprise in the new economy because “(i)t more quickly reacts to changes in the situation and, maybe, does not require such big capital investment from the side of government.” Another participant argues that in his view, a market economy is defined as a situation when “the owners of these businesses receive not much more than its workers.”

Two participants choose to define a “bazaar” economy instead, as they believe that is the system type Russia has become. As one explains, a “bazaar” economy is one in which “market relations are absolutely not regulated.” The second blames this on capital flight: “Because these who ‘strip’ Russia, they do not try to invest money in the peoples’ household of Russia. All the money is taken abroad... In any market there is some kind of order. But a bazaar, this is without order.”

6.5 Conclusion

At this point in this research work, the role of norms in the transition has been discussed from two different dimensions. In this chapter the researcher continues the discussion of norms via a contrast between the different sets of cultural values required by different economic system types. As is consistent with the evolutionary-institutional approach, results of the research study indicate that recognition of necessary changes in values and tolerance of market-based activity is proceeding unevenly. Analysis shows that the study's participants continue to associate with certain values of the Soviet period, while at the same time are beginning to accept other values more appropriate to a market-based system. To summarize:

- Increasing economic differentiation is a cause for concern and is believed to create social problems. At the same time, those who have been able to capture significant riches during the transition are not judged harshly, with the exception of a demonstrable level of envy.
- There is increasing recognition of the role of the individual in determining her economic fate. At the same time, there is palpable resentment of the retrenchment of the state in the provision of certain goods.
- Participants are not reverting to the Soviet-era climate of learned helplessness. Instead, they appear to take an activist role in the pursuit of political change. At

the same time, there has not been a significant increase in perception that they can influence their environment.

- While many participants are trying to understand the structure of a market economy, a significant minority believes that they lack the skills or education to comprehend and explain the dynamics of a market-based system.

Next, discussion will address the informal institutional environment from a third dimension. More specifically, participants' perspectives of bureaucratic corruption and its influence on the political and business climate are analyzed. This discussion will include the presentation of a series of case studies which showcase current problems in the contemporary climate that stem from accepted pro-bribery norms.

Chapter 7: Corruption and Legitimacy

Faced with the threat of loss in status and privilege due to system change, the ruling elite of Soviet times, the *nomenklatura*, sought to preserve their hold on political and economic power. Using insider status to their advantage, many of the former *nomenklatura* succeeded in reproducing their elite status by filling post-Soviet political positions. In addition, a new elite class has surfaced following the capture of valuable state assets during the privatization process. These oligarchs exert significant influence on the political process, lobbying for favorable treatment from sympathetic political authorities. These elite groups have enjoyed significant personal advantage during the transition. Much of this advantage stems from corrupt activity made possible in an environment characterized by high uncertainty, asymmetric information, and inadequate enforcement of rules.

This culture of corruption provides the context for the final discussion of research results. Though corruption can occur in a variety of situations and at a variety of levels, the focus of this discussion is specifically on bureaucratic corruption—instances whereby public authorities act contrary to their duties established under the formal rules of public organizations in order to serve their private interests (Kramer 1977, 214; Lotspeich 2003, 77). Examined in this chapter are participants' perceptions of, attitudes towards, and involvement in

such bureaucratic corruption. Responses indicate that pre-existent mental models continue to distort and delay implementation of formal rule changes. Furthermore, the state continues to lack legitimacy in the face of rampant corruption and ineffective enforcement. As a result, a pro-bribery culture is ingrained in the Russian way of life. This culture interferes with the efficacy of pro-market reforms as it subverts the development of transparent, competitive markets.

First, corruption in the Soviet Union is addressed as it provides a historical precedent to the pro-bribery culture of contemporary Russia. Then, the discussion turns to characteristics of the transition that promote bribe-taking and corruption in Russia. That is, there are aspects to the transition which may encourage the development and persistence of corruption, particularly attempts by the *nomenklatura* and other elites to influence the direction and dispersion of power, privilege, and economic rents. Following this, the research results are presented and discussed. These results evidence a high participation in corruption activities on the part of participants. The implications of this culture with respect to the development of a market-based system are then discussed.

7.1 Historical Legacy

Kramer (1977, 214) identifies two primary types of corruption in the Soviet Union—corruption for private gain and corruption for bureaucratic gain—which produced contradictory pressures on the formal economy. Corruption for private gain, or “illegal acts by public officials to provide themselves and/or others with

government goods and services,” subverted the formal economy by using an official position directly for personal benefit. On the other hand, corruption for bureaucratic gain, or “corrupt practices committed by officials to enhance organizational performance and efficiency to the benefit of the organization’s employees,” supported the formal economy by improving the operation of organizations.

Structural characteristics of the planned economy encouraged both types due to the opportunities and incentives that were presented. As Lotspeich (2003, 77) argues, the essential structural features for corruption are that “a potentially corrupt actor has control over access to an economic opportunity and the ability to allocate the opportunity subject to limited accountability.” Within the Soviet Union such structural features as significant bureaucratic discretion, imperfect monitoring, and a censored media all combined to create an environment whereby the opportunity cost of corruption was relatively low (Lotspeich 2003, 79). This environment was furthered by the uneven application of Soviet law which created the ability to manipulate enforcement and legal proceedings whenever accountability could not be entirely avoided. This potentiality for manipulation stemmed from a legal system based on the concept of exception (Randall 2001, 143). Disputes were most often resolved according to the personal relationships managers had with political authorities, rather than by the law.

Bureaucratic corruption resulted from the structural rigidities of central planning; it was tolerated because it improved production operations in the face

of rampant shortages. That is, in order to meet output targets enterprises were generally forced to engage in informal or illegal activity. Therefore, by facilitating production, informal practices tended to promote rather than subvert the formal economy (Jowitt 1983, 275; Leitzel 1997, ch. 5, 2). This type of corruption was often accomplished through the use of *blat* networks, as discussed in chapter 5. The primary player in these exchanges was the *tolkach* (fixer or go-getter), a factory representative responsible for finding necessary input goods and expediting bureaucratic processes. These *tolkachi* worked together in extensive *blat* systems, creating a facilitative, yet unofficial system of distribution for intermediate and final goods (Lotspeich 2003, 79). Kramer (1977) discusses the expansiveness of such networks:

The consequences of so many *tolkachi* is that enterprises producing commodities widely needed by other plants became inundated with them. At such locations, the *tolkachi* even maintain full-time offices and staffs... The enterprise manager might also overstate the plant's requirements for various raw materials. In this way, the plant accumulates a stockpile that its *tolkach* can use in trade with other enterprises (which have stockpiles of other goods) when supply shortages suddenly develop (217-8).

This redirection of goods formed the basis of a strong informal economy as dual markets led to opportunities for arbitrage and profiteering. Eventually, personal corruption developed alongside bureaucratic corruption as relationships which served to facilitate production could also be used to increase personal wealth (Randall 2001, ch. 10). As Lotspeich (2003, 79) argues, the growth of personal corruption was a natural outcome of the Soviet system:

Since corruption for the benefit of a state enterprise was kept hidden from higher authorities, and since there was virtually no accountability to the public, it would not be difficult for a venal manager operating in such an environment to take advantage for personal gain. This led to the Russian

joke that, as workers, we all understand that the enterprise manager steals, the question is does he steal for the enterprise or from the enterprise?

Cooperation and recognition of mutual benefit increased the gains from such activity. The feelings of solidarity which resulted from such corruption promoted a pro-bribery culture where redistribution was justified as necessary within the command planning structure. For example, expropriation was often justified by referencing the low wages paid to most employees (Leitzel 1997, ch. 5, 2; Humphrey 2000, 221). The high incidence of corruption, alongside its widespread justification, served to socialize Soviets to rule-breaking and created an atmosphere of exception that has continued in the transition period.

7.2 Corruption and the Transition

The tolerance and pervasiveness of corruption in the Soviet Union becomes a significant influence on the post-Soviet period. Despite highly publicized efforts at anti-corruption activity, the problem remains. For example, Transparency International, an international organization which ranks countries according to perceived levels of corruption among public officials and politicians, has included Russia on its Corruption Perceptions Index since 1996. As detailed in Table 3 below, Russia has consistently ranked low on the index; in seven of the last ten years Russia was ranked in the lowest quintile, indicating a high level of public corruption.

Table 3: Russia's Ranking on Transparency International's Corruption Perceptions Index

Year	1996	1997	1998	1999	2000 ^a	2001	2002	2003	2004	2005
Rank	47	49	76	82	82	79	71	86	90	126
Out of	54	52	85	99	90	91	102	133	145	158

^aThe 2000 index is based on multiple surveys from 1998-2000.

In addition to the historical precedent stemming from Soviet times, there are additional characteristics of the transition period that may further the environment of corruption. As argued in the evolutionary-institutional perspective outlined in chapter 3, such a decision-making environment is generally characterized by high uncertainty and imperfect information. This creates the environment of asymmetric access and limited accountability necessary for the development of corruption. In addition, corruption is further promoted by the power struggles that have characterized the transition as individuals search for opportunity and advantage in the process.

As examples, Lotspeich (2003, 80) identifies two specific results of privatization which increased the incidence of corruption. First, privatization resulted in more private economic actors becoming potential collaborators. Therefore, potential opportunity and support for corruption increased. In addition, the complexity and extent of privatization required tasks and responsibilities to be delegated to a large number of people. As Lotspeich explains,

With so many economic opportunities at stake and bureaucratic discretion required, the only way to avoid a surge in corruption surrounding the asset transfer is to establish a high degree of accountability. In the case of Russia this did not occur (80).

As another example, Gimpel'son (2003, 55) discusses the structural changes in government that have contributed to corruption, noting the advent of private and

semi-private companies affiliated with the state which now provide some functions and services previously under the state's purview. Examples include private mediation in issuing passports, customs operations, and licensing. As Gimpel'son explains,

In this case we are not dealing with a government bureaucracy, but with a "capture" or privatization of public functions by private companies affiliated with government agencies. Such symbioses frequently promote corruption and rent-seeking behavior (55).

7.2.1 Elite Reproduction

As discussed above, collaboration between enterprises and the political elite had maintained the duality of the Soviet system. With private markets becoming legitimate, these arbitrage opportunities between the formal and informal sectors were threatened (Randall 2001, 169). Faced with a potential loss of power, many political authorities successfully reproduced their elite status under the new regime. As evidence, one study shows that of bureaucrats in federal agencies at the federal level, 50 percent have been working there since Brezhnev's time (Gimpel'son 2003, 76). In the highest, chief, and leading positions, more than 60 percent of all bureaucrats have been working in the civil service since before *perestroika*. When combined with those that began working in civil service in the 1980s, this constitutes almost 75 percent of all bureaucrats in federal agencies at the federal level. Thus, the potentiality for collaboration extended to the transition period.

This elite reproduction has served interested parties well. For example, elite status became a critical variable in the privatization process. Those who possessed insider information were able to identify the most valuable enterprises

to target. Enterprises were then purchased at fractions of their actual value by a small class of owners benefiting from their connections. Thus, the connection between enterprise and political authority was once again reproduced under the new regime. This formed the basis of the political influence of today's oligarchs and financial-industrial groups—interlinked power structures of politicians, banks, enterprises, private security, mass media, and the military (Silverman and Yanowitch 2000, 145).

7.2.2 Regional- and Local-level Corruption

Much of the incidence in government corruption comes from the regional and local levels where corruption has increased significantly. A loss of control from the center has allowed regional and local officials to virtually escape accountability (Angresano 1996, 449). In fact, the Russian Constitution does not consider local government as part of state authorities. Therefore, municipal civil service does not fall under the basic laws for civil service in Russia (Kulikov 2002, 69). This lack of accountability combined with control over public resources and market entry has made local officials highly vulnerable to bribery, extortion, and other illegal acts.

For example, local government authorities have the power to create informal restrictions on private market activity and are able to enforce such restrictions through heavy-handed tactics. Local control over commercial real estate has provided a particularly significant source of leverage (Letizel 1997, ch. 5, 4). Kryshantovskaya (2003) provides other examples of local-level corruption

such as direct violations of the rule of law—for example, falsifying election results—but also notes that local-level corruption occurs more indirectly through the restriction of competition and other pressures. For example, the author cites evidence of authorities engaging in such acts as manipulation of the media, publicizing compromising materials and custom-made candidate “ratings,” registering candidates with the same names as those of main rivals’ to confuse voters, bribing plant managers to assure necessary numbers of votes, paying voters for signatures, and criminal prosecution of potential competitors.

This kind of manipulations means that the electoral equality principle—one man, one vote—is breached... Elections take place against the background of collusion formed between the political players, a category that includes not only the candidates and their parties, but also financial-industrial groups, the law-enforcement agencies, and election commissions at all levels (Kryshtanovskaya 2003, 40).

This corruption is furthered by elite reproduction at the regional level, predominately through the promotion of Soviet-era *nomenklatura* to new, higher positions. Data indicates that the main upward mobility trend has been the promotion from a city or district level to a regional or territorial one. For example, a large portion of post-Soviet governors are persons who previously had positions as deputy leaders at the same level and in the same region (Kryshtanovskaya 2003, 38).

In addition, the number of regional bureaucrats is rising, increasing the number of potential collaborators. One study finds between 1994 and 2000 an increase of 20 percent in employment in the executive agencies of regional and local self-government, in contrast to an increase of only eight percent at the federal level (Gimpel’son 2003, 62). In addition, there are many local and

regional posts that are now filled by election rather than appointment. As Kryshstanovskaya (2003) argues, this has rendered both positive and negative effects:

The system created the basis for an effective rather than declared division of powers, relations between equal subjects of the federation, and emergence of civil society. At the same time, the election of heads of the subjects of the federation destabilized the political system, generated the threat of a new wave of "sovereignty parades," and—in a catastrophic scenario—of Russia breaking down into a number of "appanage principalities" (35).

7.3 Persistence and Costs of Corruption

When public officials engage in corrupt activities, they are choosing between competing social norms. This choice is made by comparing relative opportunity costs. Public authorities will choose a particular norm the smaller the transaction costs of following the norm and the greater the transformation costs of changing behavior (Polterovich 2004, 31). Therefore, the opportunity cost of corruption will continue to remain low so long as a predominant number of officials routinely engage in corruption and bribe-taking and so long as the public continues to tolerate it.

Such low opportunity costs are promoted in contemporary Russia by a dysfunctional legal system and weak enforcement powers. Gaps in the law, a lack of familiarity with the new rules, and judicial misconduct all contribute to uneven enforcement of the rules. As an example, the absence of a unified regulatory framework for relationships between the federal authorities and the

regions and contradictions in legislation have both contributed to regional and local-level corruption (Kryshtanovskaya 2003, 35).

In addition, corruption is furthered by the fact that the opportunity cost of being sacked from an official position has decreased as the private sector grows, thus providing private job opportunities for dismissed state officials (Leitzel 1997, ch. 5, 5). As an example, the high-paying alternative of employment as a private security guard has lowered the opportunity cost of corrupt behavior by police officers. Further, their marketability in the private sector does not diminish even if they show a history of bribe-taking (Leitzel 1997, ch. 5, 5).

In fact, data from 2001 show that pay in the private sector was three to five times higher than analogous pay in the public sector (Kulikov 2002, 75). As a result, the most qualified bureaucratic employees are transferring to jobs in the private sector leaving the civil service increasingly young and inexperienced:

Such a distribution of employees, in which young people are concentrated in the lower part of the civil-service hierarchy, means that there is a long line waiting for promotion, which is not sufficiently transparent. The lack of clear prospects makes it foolish to stay in an organization where the pay depends significantly on one's position and seniority, and, consequently, compensation is substantially deferred... from the very beginning, young people spend their time making contacts that will be helpful in the future and looking for new, more promising work (Gimpel'son 2003, 67).

This challenges the loyalty of bureaucratic employees and may increase willingness to engage in corrupt activities.

As such, the transition environment is increasingly characterized as a pro-bribery culture. As an example, Stewart, Sprinthall, and Kem (2002) surveyed Russian public administrators regarding ethics and duties. They find that administrators are generally willing to accept a disconnection between the

principles that should provide a foundation for the system and bureaucratic life as it actually is. In addition, in comparison with Poland and the U.S., where survey responses indicate public administrators are largely guided by the rule of law rather than by other levels of reasoning, less than one-third of Russian respondents selected reasons which were guided by law and duty concepts as a basis for action.

As evidence of the general public's tolerance of corruption, results from the World Values Survey, a global research project directed by social science researchers, show increasing tolerance for someone accepting a bribe in the course of their job duties: in 1991 82.7 percent of survey respondents indicated this was "never justifiable" while in 1999 only 70.8 percent of respondents felt this way. In addition, in 1991 47.8 percent of respondents stated that cheating on taxes is "never justifiable" while in 1999 only 45 percent stated it as such. And in 1991 59.3 percent of respondents stated that claiming government benefits that you are not entitled to is "never justifiable." By 1999 this share of responses had declined to 55.8 percent.

This culture impedes with the efficacy of reforms. For example, self-interested cooperation between political authorities, enterprise managers, and organized crime interferes with market transparency. Price no longer becomes a transparent means for market participants to determine the relative value of a good. In addition, entry into markets is distorted as entrepreneurs must determine the social norms of business operations without clear enforcement of

rights and laws. Therefore, implicit costs on newer, less powerful firms are high (Ellerman and Stiglitz 2003, 35).

In addition, corruption creates legitimacy issues for the state. As argued in chapter 3, the establishment of a rule of law, while a necessary condition for a market-based economy, is not sufficient. Also required is belief in the stability and enforcement of the laws. Cultural support for reforms follows legitimacy, as without legitimacy there will not be compliance:

The enforcement of sanctioned rules and conventions is an equally important part of the process, for enforcement procedures carried out by legitimate monitoring organizations assure that the conforming entities and individuals are also seen as legitimate (Randall 2001, 158).

As evidence of the impact of such a culture on public opinion, as recently as 2005 surveys of small businesses show that entrepreneurs feel more likely to be victimized by officials and policemen than criminals, are uncertain they could protect their lawful interests against regional authorities in court, and believe that preferential treatment for enterprises with familial connections to political authorities is widespread (Wall Street Journal [New York], 27 April 2005).

Corruption can also interfere with the state's ability to provide necessary social services. For example, Lipset and Lenz (2000, 115) argue that a high level of state corruption may divert public resources from education spending to other areas. For example, public officials may shift government spending to areas such as airports, highways, and other larger, hard to manage projects that are more prone to fraud. Grigory Yavlinsky, the leader of *Yabloko* (Apple), a democratic reformist political party, notes the high social costs of state corruption:

No one doubts that these *nomenklatura* capitalists of insider deals and political connections stands in the way of an open economy that would benefit all Russian citizens. The robber-baron market cannot tackle important social and economic questions. It is primarily concerned with issues that affect its masters' short-term power and prosperity (Yavlinsky 1998, 69).

7.4 Research Results

In order to assess the impact of this culture as it relates to this study's sample, participants are asked a series of questions regarding their perceptions of, attitudes towards, and involvement in bribery and corrupt activities. For example, participants are asked generally about paying money to public agencies on the side in order to accomplish set tasks. In addition, participants are asked about illegal access to particular services such as subsidized housing and social benefits. Participants are also asked whether side payments would help settle any disputes with respect to owed wages or pensions.

Questions are also posed which address participants' perception of the incidence of bribe-taking and corruption in both federal and local governments. In addition, they are questioned as to whether they believed the incidence of such has changed (for the better or worse) since Soviet times. Participants are also questioned specifically on what they felt to be the extent of tax evasion and corruption and bribe-taking in the tax service.

It is important to note here that Shlapentokh (1989, 206) included Krasnodar on a list of national symbols of corruption in the mid- to late-1980s.

7.4.1 Corruption and Bribe-Taking

When asked of their perception regarding the level of corruption and bribe-taking in public institutions, the responses are mixed. For example, 39 percent of participants refuse to judge the level of corruption and bribe-taking in the federal government, stating they lacked the necessary information. Some respond that they are unable to determine the level of corruption as it is difficult to tell when you are paying officially or unofficially:

[At the cash window of an institution] you will not ask, "Do you take this money officially or unofficially?" Everything is done quite openly. It is not possible to distinguish where this money goes. Practically, they do not give out receipts.

However, 39 percent of participants state conclusively that they believe it happens very often. A young woman states that "it is often as it is everywhere." She later worries her quality of life will decline in the future as a result: "...[There is] much deception and everything that is done between officials is very... It seems to me that they do everything only for themselves, but not for the people."

Another participant argues:

If only because for them there was inviolability. And an all-permissive [environment]... A den. Earlier the deputies were really chosen. But not so [now]. How to say? It was possible even from the working class he was able to be a deputy. But now it is only criminals who cover themselves with deputy's documents.

A total of 17 percent of participants feel that corruption and bribe-taking happens, though it is not as widespread of a problem as it is made out to be. A few protest that this is not simply a problem in Russia but, in fact, it is "worldwide" and "a sickness of any country."

With respect to local government, most participants (74 percent) also refuse to judge the level of corruption in Krasnodar's government. Only 16 percent of participants claim they believe it to happen very often, and 9 percent feel that it happens, though is not widespread. The local police are occasionally mentioned as targets of corruption. As one participant states, "If the Citizen's Auto Inspector (*the police*) stop and I am without 40 or 50 rubles, this will never make do." A second area mentioned as significantly corrupt is the local state university, where payment for admittance is standard. As noted in chapter 5, *blat* networks are often used to secure entrance into the state university without having to pay extortion fees. If there are no such networks, bribes are necessary. Thus, low-income students are effectively priced out of the market. As one participant states,

Vzyatka (bribe), you must give *vzyatka*. To be sure that you will be lucky. State universities are much more expensive and no certain rate. Unofficially. Much more expensive. And here, I am sure... in the state universities you take an exam in each subject and they want you to pay *vzyatka*.

However, issues of corruption and bribery most often arise when participants are required to obtain official documents for personal needs or require assistance from public authorities in response to personal crises. For example, participants are asked if, in the past year, they or any of their family members have had to obtain any official documents. In the sample, 83 percent of participants have requested some type of necessary official document from a public agency. Of those, 13 percent paid extra money on the side to influence the process. In addition, requests for help from public authorities are often

accompanied by countervailing requests for bribes. Many of these personal experiences are discussed below.

7.4.2 Change since Soviet times?

In some cases the potential for corruption has decreased in response to changes that have occurred in the institutional environment. For example, in direct contrast to the Soviet era, subsidized housing is no longer accessible through bribes. Instead, to obtain any type of housing the standard answer is that money is necessary to (legally) purchase housing and that personal influence generally cannot help. However, when asked in general how they rank the level of corruption and bribe-taking with its level in Soviet times, 26 percent of participants perceive the level of corruption in the federal government to be about the same, that it is “permanent” or “continuous.”

Earlier, there was not this democracy. We did not speak strongly. But all the same, I remember when my daughter entered [the institute]—this was the year 1991—we paid everywhere for studies... Now, we pay someone, I do not know... this is to the institute, this is to the state, but officially. Earlier, you know, we gave to someone. But now you do not know to whom [the money goes]... I think that in our time, it is practically inherent in everyone.”

Twenty-four percent of participants feel that corruption and bribe-taking has increased since Soviet times. Much of this is due blamed on a weak central state that insufficiently enforces the rules. As one participant explains,

Yes, it has increased. Because now there is no control from the side of the Party. Earlier, the Communist Party... That is, it was possible to complain and if they were to find out that someone received a bribe, then they were expelled, [were punished] up to expulsion from the Party. And exclusion from the Party... practically, a person lost his career.

However, praise for Russian President Vladimir Putin is widespread; 75 percent of participants like him and approve of the job he is doing. Many participants feel that he is making a significant attempt at combating the corrupt culture of the state. They note positive changes that have been made due to his leadership and that he tends to live up to pledges he has made to his constituents. In the words of one participant, "his business does not part from [his] promises." Also mentioned often are his youth, intelligence, and manner. As one participant explains, "First of all, he is literate. Literate in what way? An erudite... We will say, there, he is tough in the way of struggle with sloven individuals, competent, in my opinion, in many questions. In any case, he tries." Another laments of corruption and bribe-taking:

This is permanent, probably. Our state is corrupted very much. For the four years of Putin's rule, of course, it is very difficult to do something but he struggles. He has some kind of improvement. He takes away one, another remains. This is all the same now.

With respect to local-level corruption, 14 percent of participants state that the level of corruption in Krasnodar is about the same as it was in Soviet times. However, 50 percent of respondents think the local government has become more corrupt. This is consistent with the arguments presented above regarding the effects of loss in central control and the impact this has had on corruption in local governments.

7.4.3 Personal Experiences

Participants were asked of their personal experiences with corruption and bribery. Several were able to easily recount instances where they themselves

had participated in bribing public officials for the purpose of obtaining necessary documents, in order to influence a course of action, or simply as a preventative measure when dealings with officials would be an ongoing task. It is worthy to note that in this relatively small sample size finding illustrative examples of participants' involvements in corrupt dealings was not at all difficult.

- An émigré from Kazakhstan tells of registering her parents for a pension after leaving Alma-Ata and coming to Russia. Though the pension systems are identical, she ran into problems convincing the Russian pension authorities of her parents' eligibility:

All the same, they began to doubt that, how much... namely, what kind of wages, what kind of pension they received earlier. It happened that I made a present in the form of coffee, cognac, and candy for the inspector who was occupied with their documents. In order that she would really pay attention, in order that they had everything correctly, that all the documents would be correctly registered. Simply, in order that she would pay attention and objectively give them the pension, objectively calculate the pension. She was glad.

- One woman, the mother of a disabled child, often runs into difficulties in her frequent contacts with authorities. She explains that it is possible to use a variety of methods to influence the process:

In one case, for example, friends are able to help. In another case, it is necessary to take not a bribe, but a present. And somewhere it is possible to address someone in a higher position. That is, it depends. Namely, it depends on what kind of organization... I try to get [my child placed in] kindergarten (*daycare*)... Simply, I go to the doctor, I make any kind of present there. I simply pay any kind of money [for] a paper, permission for my child to attend something there. [If] I want permission [to go to] the pool [with my child], it will also be necessary [to go to the doctor]... I gave a present, yes, personally "in the hands."

The same participant states that she also had to pay the daycare for her son to attend. Referring to herself as a “sponsor,” often used to describe some who gives a payment on the side, she states that she spent 2000 rubles (approximately \$60US) for some toy dishes for the daycare to secure a spot for her son.

The above cases represent transactional bribes, or payments to an official to speed up a process rather than influence an illegal decision or result (Reisman 1979, 69-75, Humphrey 2000, 219). Humphrey argues that in Russia transactional bribes are so ingrained in daily life that they are not viewed as an outright bribe: “Like a tip which is paid after rather than before a service, the transaction type of payment is seen as fundamentally innocuous, since after all no norm has been broken (219).”

- A small business owner states that he struggles “systematically” with obtaining official documents. He explains,

Many people do not want to take the responsibility for issuing documents on themselves. Many procedures are excessively complicated. Other procedures are constructed so, that, we will say, a large number of people need to address to one unique person in the city... Eighty percent of all the state institutions, officially or unofficially, take [money] for the issuing of documents that you receive.”

This participant also speaks of what he calls “hopeless situations,” when acquaintances of officials with whom he must do business—the health committee, the firemen, the police—arrive and ask for free services. As he

explains, "If I will say that they will pay me, they will pay. But then I am able to have problems."

- A second small business owner in the sample tells of his struggles to register his small business, a residential construction company that he is developing with an acquaintance. He explains that when a business is opened, it is necessary to register an official commercial address for that business. However, to lease such a space would cost approximately \$300 a month, a sum he refers to as "not real." Therefore, he explains that he paid \$70 for what he called a "fictitious agreement" which stated that he was leasing a space. However, when he went to obtain a license all necessary paperwork was issued without any review of this document. He then explains that the second time it was necessary for him to get a license he approached the process differently, thereby only costing him \$10, though by this time a false lease would have cost him \$150. As he explains:

Question: Why [did it only cost you \$10]?

Answer: Because [this time] I did not buy the agreement, the registered payment. I simply gave 300 rubles to the woman who fills in all of my current [papers] and she wrote that I have a legal address, Derzhinskovo [street], [number] 5. This is my private property, everything. Five stories and it is all mine (*laughs*).

Question: Was this in the open, did she ask from you or was it your offer?

Answer: No, she feels shy. This is normal.

Question: How do you know [to pay] 300 rubles?

Answer: Because that year, when it was the [application for] the first license, she wrote [the information] free of charge. That is, I bought the agreement for \$70, but she wrote everything fully, that it was my property

[without looking at the lease]. But at this time I thought, "Why not give money [to her] and she will again write the property to me?"

Question: But why the sum of 300 rubles?

Answer: It is better than to give nothing. In principle, she is able to write this free of charge.

Question: So, it could be 100 rubles?

Answer: 100 rubles, no. 300 rubles, this is like the minimum. This is simply [the minimum] it is possible to give. This is so, simply, I do not know, for candy. Less than 300 [rubles], this will be simply shameful and I will be red. Yes.

- One participant tells of his ex-wife being stalked by a mentally disabled person who at one point attempted to abduct his wife by car. He recalls that after this happened the perpetrator was arrested. Because there were no witnesses, the police did not pursue the matter. Instead, they recommended that he address "unofficial structures." His wife was later attacked by the same person and was admitted to the hospital with severe injuries. He recalls that he again attempted to pursue the matter:

I addressed other higher official structures. They showed a figure, how much I must pay them. I addressed various structures, moreover, government structures. I had a connection. And I was defeated. Everyone had one figure.

The same participant ran into difficulties when he tried to register his child in daycare. He explains that he had received permission from the government for his child to attend daycare without making a "commercial payment," referring to a typical "sponsor" payment of 10,000 rubles (approximately \$290US). However, the daycare refused to admit his child even in the face of the government order

and asked for a payment of 3000 rubles (approximately \$90US). He states that he waited a period of time and eventually managed to postpone his child's entry to the kindergarten until no payment was necessary.

- One participant tells a story of a friend who combated corruption in a unique way:

He was the owner of a private telecommunications company. And when the government licensed him for activity—it was necessary for him to receive a license from the regional government—the helper of this official explained to him that he must pay him [the official] money. My comrade did the following—he hired a good lawyer, prepared perfect documents, took a video camera and with the video camera entered the office of this official, put down the packet of papers and asked, “Please, sign”. Under the video camera. The official was shocked... He was in rage, but he was afraid to show all of his emotions and it was necessary for him to sign all the papers.

- Another participant tells of trying to renew her passport, for which she was asked to pay 500 rubles (approximately \$15US). As she explains:

But in fact, at that day, the passport was only 100 rubles. For example, I asked her, “Why is it so much?” She says, “For this and that and that.” But, most of that money she wanted to put in her pocket. Because I came to the office and I learned everything. How much this costs to put your data into the computer, to fill in these blanks. They told me how much it cost. The passport itself cost 50 rubles. Other services, another 50 rubles... So, in fact it cost me 200 rubles. I came directly to the [regional] office, to the person who gives out the passport. And he saw a baby in my hands and he agreed to make a passport urgently.

- A participant tells of her husband being attacked, resulting in a concussion.

She explains that the police asked for 500 rubles on the side to pursue remuneration from the attackers. As she explains:

[Without the bribe] (t)hey would have decided it, but simply... it was such a situation that money was necessary for medical treatment. And if these people did not pay us for the treatment, simply, the administration would have written a fine and that is everything. And since we supposedly shared with these policemen, they, therefore, secured it that they paid us [instead] for the purchase of treatment. Through other [ways], no how...

Shlapentokh (1989, 213) argues that there is a continuum of corrupt relationships. These relationships extend through three levels: (1) among superiors, (2) between superiors and subordinates; and (3) among subordinates. To typify the experiences above, most are characterized by the second type of relationship which Shlapentokh identifies as either inside an enterprise (between supervisor and employee) or between superiors and ordinary people who are not their subordinates. Participant responses indicate that resorting to such bribery is somewhat accepted as a way to accomplish necessary tasks. This is consistent with Humphrey's (2000) argument that though Russians tend to prefer mutual reciprocity (as discussed extensively in chapter 5), bribery is something to which people resort when they do not have the necessary networks of friends:

Thus, in everyday life for ordinary people bribery is something akin to other unpleasant economic necessities which are supposed to have disappeared with the previous regime (like queuing) and which are stigmatized partly because people with good connections do not have to engage in them (219).

7.4.4 Taxes: Evasion or Enforcement?

Given the high level of attention paid to the impact of tax evasion on the transition reforms, the researcher decided to specifically question participants on this topic. More specifically, participants are asked if they agree or disagree with

the following statement: "It is sometimes said that there is no need to pay taxes if you do not want to; the government will never find out about it." The majority of participants (79 percent) disagree with this statement. It is generally felt that it is necessary to pay taxes on reported income as it can be verified and most believe the government capable of enforcing debts. In addition, the important role of tax revenue in supporting state infrastructure is recognized. As one participant argues, she feels a personal obligation to pay: "Because we have a medical worker [in the family]. Who else will pay taxes? ...They receive wages for this." There is acknowledgement that the tax service was vulnerable to corruption in the past, but now it is generally viewed as being on a "very high level." Some believe that with time comes experience and improved enforcement: "The matter is not in honesty or dishonesty [of tax officials]. The period of time passes. This structure was young, new. Now, they try to work through the mechanism."

However, legitimacy issues remain. When asked whether it would still work to bribe an official to help them avoid taxes, 57 percent of participants agree. However, many qualify that not all officials are corrupt. As one states, "This is sometimes so. It depends on the situation and on the person and on what kind of sum they try and catch him [with]." One participant acknowledges that "professional investors" do evade some taxes, but argued that they do more for the country with the money than the government:

That is, we are grown-up people. That is, you will be a candidate [in economics], yes? Then we will say by what is better—professional investors, the majority pay little taxes. We will say it so. But they bring by far more uses to the government if they collect their investment, namely, in development. I think that the tax politics of the government must be inclined to [provide] incentive of investment in one's own economy.

7.5 Pro-bribery Culture

As argued above, there are significant economic and social costs which result from a high level of bureaucratic corruption. If indeed a pro-bribery culture is ingrained, and therefore tolerated in contemporary Russia, this has important implications with respect to path dependence and lock-in. In other words, this culture can continue to persist despite its implications for the transparency of markets. On the other hand, social norms can also increase accountability and reduce the propensity to act corruptly. As Lotspeich (2003) argues,

The agent often cannot exploit the opportunities before him without a collaborator. If collaborators have a tendency toward corrupt behavior themselves, they are less likely to hold the agent to account. A widely shared norm of ethical behavior in relation to the opportunity controlled by the agent would increase accountability and so reduce corruption, regardless of the agent's ethics (78).

The above results from this research study reinforce this perspective. The entrenchment of a pro-bribery culture stems from a variety of sources, including the acquiescence of participants to resort to bribes when faced with a situation in which a particular result is promoted through their use. Because this is so commonplace, the participants are socialized to accept this as part of their daily struggles. As Sik (1994) argues,

As to the role of culture, the actors socialize each other—and, through their networks, the rest of the society—in how to behave. Thus the emerging norm spreads quickly through networks, socializing other actors and producing a new cultural trait. But not just the rules of behavior spread out. Acceptance of bribery as a fact of life actually decreases the cognitive dissonance of committing a sin; a pro-bribery culture emerges or is reinforced (9).

Humphrey (2000) argues that in contemporary Russia, bribery does remain reprehensible and morally condemned. However, other transactions

equally a-legal or illegal are regarded as more “ethically neutral” in Russian popular culture. This is due to changing perceptions towards what constitutes a “bribe” and the scope of application of the term. As she explains,

Vzyatka (the bribe) as a representational category is applied unequivocally only to the public state sphere, and it is used with much less certainty with regard to unorthodox payments in private commercial life, which tend to be described in other ways, as ‘additional fees’, ‘tariffs’, ‘subsidies’, ‘gratuities’, ‘discounts’, ‘premiums’ and the like...

For the economically disadvantaged, bribery is abhorred and yet it is an essential survival strategy; for the radically impoverished, it is mostly out of reach and condemned as an unfair tactic of the better-off; and finally, among a small powerful elite, moral disapproval of bribery is swept aside in favor of a new ethic of commercial necessity (217).

7.6 Conclusion

Structural conditions in the Soviet Union promoted the use of informal and/or illegal means to accomplish productive tasks. This further evolved into the use of informal and/or illegal means for self-interest alongside the interest of the enterprise. As a result, the Russian transition inherited a population that was socialized to rule-breaking and the use of public resources for private gain. This culture has continued with the transition, whereby a period of significant uncertainty and asymmetric information allowed those in the position to do so to exploit the transition for their own personal gain. This has distorted the relationship between policy goals and their outcomes, thereby impacting economic performance. Furthermore, this continues to impede the development of a smoothly-functioning market-based system as it challenges the transparency of markets.

Results from the research study show that this corrupt culture continues today in contemporary Russia. It is difficult to accomplish even the simplest of interactions with officials without resorting to some sort of gift- or bribe-giving in order to accomplish set goals. This has contributed to a lack of legitimacy in the state. However, most believe that the current presidential administration is doing its best to battle corruption in the state apparatus.

Thus, in this chapter's discussion and analysis the field study's results conclude with presentation of a third dimension of Russia's informal institutional environment. Russians became socialized to rule-breaking when structural rigidities and the incentive structure of the Soviet Union promoted activity contrary to formal rules. This activity has continued in the transition period, enabled by high uncertainty and asymmetric access to information and resources. Given the high incidence of corruption, Russians passively accept its existence, creating a pro-bribery culture. This has implications for future development of transparent markets. And so long as social norms continue to minimize the transaction costs of engaging in corrupt activity, this culture will continue.

Chapter 8: Conclusion

This chapter concludes this exploration of the role of informal institutions during the transition. Evidence is presented regarding the outcome of shock therapy reforms which substantiates institutionalist arguments that institutional change is governed not simply by changing formal rules but also by the corresponding reaction to and modification of rules by social norms. Using this argument as a general starting point, a field study was completed which researched the role of social norms in the transition from a variety of dimensions. Evidence from the research results indicate that norms continue to play an important function in economic decision-making in the transition, particularly in light of the radical changes in formal rules.

This chapter pulls together the theoretical framework of the study and its results in summary form. Following this the field study is discussed with respect to its place within a larger research agenda that will attempt to build a pattern model of informal institutions in the transition. The chapter concludes with a discussion of future paths for this research to take in pursuit of this model-building.

8.1 Summary of Theoretical Framework

The analysis contained in this work focuses on the distinction between formal and informal institutions. As detailed in chapter 3, informational and

cognitive constraints, irreversibility of time, uncertainty of future-oriented decisions, interaction of economic and non-economic factors, and dynamism of the socio-cultural environment all contribute to a decision-making environment that is highly complex and uncertain. Formal and informal institutions exist to address this complexity and assist with decision-making by providing the agent with the parameters under which choice takes place. Institutional analysis acknowledges this by proceeding from the socio-economic context via consideration of the formal and informal cultural, religious, political, social, and economic institutions of society.

The process of institutional change is governed by the interaction between rules and norms. There is the potential for tension if change in institutions proceeds unevenly. As an example, a change in formal rules can create a situation of tension between pre-existing norms and the new rules if they involve countervailing signals. This tension will remain so long as the transaction cost of following the established norms is lower than the cost of changing norms to be more consistent with the new rules. Therefore, new rules will only be followed if this calculation concludes that it is beneficial to develop new norms. This interaction between formal and informal institutions is true for all types of economic systems at all stages of development. In all cases, social economies are evolving at various speeds along paths set by agents acting within interacting patterns of formal and informal institutions.

In consideration of this, the evolutionary-institutional approach to transition recognizes that interactions between rules and norms are highly uncertain in the

transition environment. Therefore, the evolutionary-institutionalist approach emphasizes the potentially significant role of inherited social norms with respect to their interaction with new rules. In addition, it is recognized that new norms will surface in light of the new rules. This interaction will determine the path of change in the transitioning countries. This path will vary according to the unique circumstances in the different institutional environments. In addition, economic actors will look for affirmation of their decision-making by viewing their behavior relative to the behavior of others. Therefore, there is a potential for social norms to be strongly reinforced between economic actors in their decision-making.

Under this approach, the mental models constructed by agents to facilitate decision-making are viewed as highly complex. In contrast to neoclassical thought and the assumptions of Rational Economic Man, the institutional actor is cognitively limited and has a complex goal structure. As a result, a gradual approach to reform is advocated in order to minimize transformation costs. This allows time for economic actors to adjust to the changing institutional environment and as such promotes complementarities between rules and norms. For example, this gradual approach may require only a piecemeal withdrawal of the state from its role in Soviet times. This allows time for the private sector to develop, including all necessary supporting markets and institutions. A critical role for the state in this process is the provision of a social safety net to minimize transformation costs. Providing a sense of security promotes public support of reforms and thus reform credibility, a critical element for norm adaptation.

In contrast, as presented in chapter 2 the shock therapy approach assumes a much simpler mental model used by economic actors. This transition strategy stems from the belief that if provided with the proper incentives, economic actors will behave according to economic laws universal in place and time. This argument stems from the neoclassical treatment of economic actors as identical with respect to a rational approach to decision-making. This enables shock therapy strategists to ignore context- and country-specific factors in their transition approach. According to its intellectual foundation, simply releasing market forces that provide the appropriate signals to actors will result in a reallocation of resources that will improve economic performance.

Shock therapy reforms, therefore, assume linearity in the development of competitive markets simply by changing the formal rules of operation this ensures the appropriate incentives for market development are in place. Citing the ineffectiveness at Gorbachev's attempts in the 1980s to reform the Soviet model from within, shock therapists called for a complete replacement of Soviet institutions. The idea was to use the window of opportunity that emerged following the breakup of the Soviet Bloc to institute widespread and immediate reforms to effect a complete break from the old system. Rapidity was considered essential to success, as it would capitalize on public support for change that stemmed from the *glasnost'* and *perestroika* reforms.

The shock therapy prescriptions thus focused on altering the formal institutional environment through three mutually reinforcing goals of liberalization, privatization, and macroeconomic stabilization. Liberalization reforms included

removing wage and price controls, legalizing private business and private property, and opening the economy to trade and other competitive pressures. Privatization was effected through a variety of methods including direct cash sales, auctions, and the mass distribution of vouchers. Macroeconomic reforms centered on reducing the role of the state through eliminating subsidies and directives, stabilizing the growth rate of the money supply, developing public debt markets, and creating a fully convertible currency.

The shock therapy analytic approach was, however, naïve in its conceptualization of institutional change. This has created a series of challenges to the efficacy of reforms attempts. To begin with, the reform process was manipulated by rent-seeking behavior of those in positions of power who search for personal gain in the reform process. Many of these individuals were elites from the Soviet period who were able to reproduce their elite status under the new regime. In this respect shock therapy failed to consider the strength of entrenched interests and their ability to stand in the way of progressive institutional change.

In some cases, the efficacy of new rules has drawn interference from the refusal of certain parties to adhere to the new rules. As examples: Central Bank authorities continued printing money to finance subsidies to factories, ignoring executive branch orders to reduce money supply growth; when domestic industry proved unable to compete effectively in world markets, protectionist tariffs and quotas were instituted to shield domestic industry from competition; regional authorities interfered with the liberalization of market entry by exacting high

bribes for business licensing; and the lack of turnover in enterprise management stymied attempts to enforce market discipline on former Soviet enterprises.

The efficacy of rules was also challenged by the ability of economic actors to find innovative ways of rule-breaking. Major industrial lobbies succeeded in thwarting the reduction of certain subsidies; enterprises engaged in non-monetized exchange; tax evasion challenged macroeconomic budgetary reforms; and demonetization interfered with the development of hard budget constraints.

An evolutionary-institutional critique of the shock therapy strategy references these institutional elements of post-Soviet society that interfered with the intended results of shock therapy. Reformers paid insufficient consideration to widespread and deep-rooted institutions inherited from Soviet times. These include, among others, tolerated social norms for rule-breaking, a willingness to conduct business in informal markets, an entrenched hierarchical capture of power, and a willingness to ignore edicts from the center in an environment of limited accountability. Informal institutions play an indisputable role in the functioning of the post-Soviet environment.

8.2 Summary of Findings

The purpose of this research work is to contribute to the debate over the role of institutions in the transition. The study is founded on the argument that research focusing on informal institutions can provide a more complete picture of the Russian transition environment. However, this area is significantly underrepresented in the transition literature. Therefore, it was decided that

analysis of the role of informal institutions in the transition could make a significant contribution. Ethnographic social research was undertaken using an exploratory field study. Results from the study lend evidence to arguments of the importance of social norms in the evolution of economic systems.

Chapter 5 discusses social capital in the transition. Social capital serves an important function as it produces something of value for the individual possessing it. More specifically, it facilitates resource transfers between different members of a social network. In this sense, social capital becomes a strategic social mechanism for risk-sharing, hedging against uncertainty and crisis. For example, social relationships serve a vital role in alleviating material hardship. They facilitate the transfer of food, clothing, and household goods among friends, family, and neighbors. This especially includes sharing the harvest from household plot production, an important household activity given the precarious economic position of most participants. Social networks are also used in a short-term system of monetary transfers. This system is maintained through attentive payment of debt. The exception is inter-generational monetary transfers which tend to be viewed as gifts rather than loans.

Neighbors, friends, and family maintain social capital through routine socialization and mutual assistance. Good reputations become important; by being accessible, this insures that others will make themselves available should the need arise. Correspondingly, there is a strong relationship of implied reciprocity in the rendering of favors. In the framework of Polanyi (1957), this system of reciprocity is enabled by a pre-existing definite institutional

arrangement. The reciprocal nature of these social capital relationships was both organized and validated beforehand via the Soviet legacy of *blat*, a distinctly Soviet form of social capital.

As such it is argued that social capital in contemporary Russia is an inherited trait from the Soviet Union. At the onset of transition a strong social norm was already in place due to the Soviet legacy of *blat*. This presented an obvious resource to draw upon when confronted by challenges of the transition, though the pre-existing institutional arrangement has been rearranged to meet current needs.

In chapter 6, this argument of norm persistence is extended to the transfer of cultural values and beliefs between historical periods. This chapter presents a contrast between particular values inherent to the Soviet planned economy and those required for a market-based system to flourish. Soviet cultural endowments come into direct conflict with values more appropriate to the functioning of a market-based system. For example, Soviet culture promoted suspicion towards money and profiteering, de-emphasized innovation and creative thinking, encouraged learned helplessness and passive acceptance, and promoted a strong reliance on the state. Research results are analyzed in this context to identify proportionate levels of value continuity versus value change.

Responses show a dynamic and uneven process of change in values. This is consistent with the institutionalist belief in the evolutionary and incremental process of norm adjustment. For example, increasing inequality is a cause for concern as a variety of social problems are blamed on this

phenomenon. This is in conflict with the incentive structure of the market where reward is commensurate with effort and social Darwinism determines economic advancement. This incentive structure is, however, consistent with participants' unwillingness to judge harshly those who have been able to capture significant riches during the transition. However, there is a demonstrable level of envy towards the new Russian rich.

Uneven change is also apparent when considering perceptions toward individual responsibility. There is increasing recognition of the role of the individual in determining her economic fate. At the same time, there is palpable resentment of the retrenchment of the state in the provision of certain goods. This analysis therefore concludes that an individualistic ethic is beginning to replace the role of the state in the assignation of responsibility. However, responsibility for self and one's own well-being is accompanied by observable resentment.

Civic culture appears to have fully evolved from the Soviet-era climate of learned helplessness to one of political activism. The *oblomovschina* of Soviet times has been replaced with political participation and protest activity. In this respect, the rights of the individual are being asserted strongly in the political environment. Importantly, however, this has not yet translated into a perceived increase in individual influence in the new environment.

A third dimension of the informal institutional environment is presented in chapter 7. This chapter addresses the pre-existing institutional arrangement of corruption and bribe-taking as structural conditions in the Soviet Union promoted

the widespread use of informal and/or illegal means to accomplish production tasks. This evolved into the use of informal and/or illegal means to further private gain alongside the interest of the enterprise. As a result, the Russian transition inherited a population that was socialized to rule-breaking and the use of public resources for private gain.

Results from the research study show that participants routinely participate in corruption and bribe-taking. It is difficult to accomplish even the simplest of interactions with officials without resorting to some sort of gift- or bribe-giving. These personal experiences, along with perceptions of bribe-taking and corruption in local and federal government, have led to the entrenchment of a pro-bribery culture. And so long as social norms continue to minimize the transaction costs of engaging in corrupt activity, this culture will continue.

This social norm continues to distort and delay implementation of formal rule changes. Self-interested cooperation between political authorities, enterprise managers, and organized crime interferes with market transparency. Preferential treatment discourages market entry. In addition, corruption can interfere with the state's ability to provide necessary social services. This creates legitimacy issues for the state. Reforms are constructed not according to social benefit but instead according to the personal advantage of insiders.

8.3 Future Paths of Research

All three areas of analysis support institutionalist arguments regarding the persistence of norms despite formal rule changes. The results, therefore,

validate the evolutionary-institutional approach to transition and its view of institutional change. As such, the research results provide evidence that the informal institutional environment in the transition remains an important topic area for research.

This is particularly true given the time-intensive nature of research devoted to capturing information on the informal institutional environment. The role of informal institutions can easily escape quantitative studies as this knowledge is often buried in deeper context. Therefore, research studies such as the field study presented here is the methodological approach well-suited for identifying information that is poorly reflected through statistics. However, the limitation of such a study is that it reflects the experiences of only a few individuals. Therefore, there is a continuing need for this kind of research to develop a much larger data set from which hypotheses can be tested and conclusions can be drawn.

8.3.1 Pattern modeling

This research project is the beginning of a larger agenda which seeks to detail many more dimensions to the informal institutional environment. As such, the information presented here only begins the process of constructing a holistic model addressing this period of change in Russia. As outlined by Wilber and Harrison (1978, 75-7), construction of a holistic model using such a participant-observer method generally proceeds in three stages. This field study is part of the first stage, when the theorist becomes “socialized” in the target environment

by cataloging themes observed in a variety of contexts. These themes become most apparent through the researcher's first-hand observation, as this gives the researcher the best chance of correctly identifying important themes (Radzicki 1988, 635).

The second stage begins once hypotheses have been constructed from the socialization process. In this stage the hypotheses are tested through data collection. Arguments and suppositions which are not supported are rejected and those which are supported are validated. As more and more data is collected, better and more accurate hypotheses will be constructed. As Wilber and Harrison (1978) argue,

Gradually, as socialization proceeds, the researcher becomes increasingly attuned to accurate perception and interpretation of the recurrent themes and formulation of validated hypotheses. The holist uses this experience and the various pieces of evidence to build up a many-sided, complex picture of the subject matter (76).

Themes that have been validated and are logically consistent with one another will detail the institutional structure of a particular socio-economic system (Radzicki 1988, 634). Therefore, in the third stage this institutional structure is identified by constructing a network or pattern around themes validated in the first two stages. These pattern models are then used to explain the influence of institutions on behavior. In this manner, each individual part of the model is linked to the larger whole; therefore, there is an appreciation of the interactions between the parts and the whole (Radzicki 1988, 635). As Wilber and Harrison (1978) explain,

It is in this way that the holist attempts to capture the interactive relationship between part and whole. As the holist constructs the system

model his earlier descriptions of the parts are continually tested by how well they fit together in a pattern and to what extent new evidence can be explained within the pattern. The holist is constantly seeking to obtain a finer and finer degree of coherence between his account of the system as a pattern of interconnections and the real system (76).

This process is on-going as continued socialization leads to more themes which are the validated and placed into the pattern model. In this way the pattern model is improved and expanded upon.

8.4 Conclusion

A narrow view of decision-making, like that of neoclassical economics and its assumptions of rationality, ignores the influence of socio-economic factors on behavior. In contrast, institutionalist theory argues that decision-making is highly complex due to the economy's embeddedness in society. However, due to analytic neglect there is a general lack of micro-level data which addresses the role of social norms in economic life. Thus, there is a clear need within the economics discipline for data which informs on the role of informal institutions in economic activity and decision-making.

This field study presents one such approach in the collection of this type of data. The transition period in Russia provides an ideal environment for informal institutional research as radical changes in rules can provide stimulus to even greater use of informal institutions in everyday life. Therefore, the study concludes with the goal of augmenting these results with additional research in order to pursue a holistic model on informal institutions in the transition.

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APPENDIX A: THE INTERVIEW GUIDE

**Household Survey
Fall 2003 through Spring 2004
Kransnodar, Russia**

Participant Number _____

Date of Interview _____

Time Started _____

Time Ended _____

Interviewer Observations

Type of Housing Structure:

- Multi-story flat with/without elevator
- Low-rise flat with/without elevator
- Single-family residence
- A room in a flat or house
- Hostel, dormitory, barracks
- State farm or collective farm
- Other _____

Gender of Participant:

- Male
- Female

A. HOUSEHOLD CHARACTERISTICS

1. This home is

- State or municipal property
- Housing cooperative
- Rented
- Owned, but still making payments
- Owned, and completed paid for
- Other _____

2. How long have you lived here?

2a. How did you get this apartment/house?

2b. Where did you live in Soviet times?

3. Is everyone who lives in this household a member of one family?

4. Household Roster

4a. Explain any instances where spouses are living apart.

4b. Explain any instances where minor children are not with parent.

4c. Explain any instances where extended family member is living there.

4d. Where do your close relatives live?

5. If you had something broken at home, what would be the best way to get it fixed?

- I or another member of the household would fix it
- Ask a friend to fix it
- Pay someone to fix it
- Send a complaint to communal housing services or owner of property
- Find someone who knows people in the communal housing service
- Nothing I could do

6. What should a person do to get a government-subsidized or enterprise-subsidized flat if not entitled to one?

- Offer a tip to the official allocating it
- Use connections
- Tell officials that special circumstances justify a flat
- Borrow or save money to buy a private flat
- Nothing can be done

7. What do most people have to have to get a house or flat in this neighborhood?

8. Do you own a dacha? How much time do you spend there? Does anyone else use it?

9. The last time you and your family were away from your home for two days or more did you ask a neighbor to watch your home?

9a. Do you do the same thing for them?

9b. Do you give / get anything in return for the favor?

B. GETTING FOOD AND HOUSEHOLD GOODS

1. Does your household have a plot of land where you grow fruits and vegetables?

- yes
- no

1a. IF YES, is this near your home or in a rural area (at a dacha)?

1b. IF YES, about how much time are you or other members of your household working this land during the season?

- several hours a day
- several times a week
- Saturday or Sunday
- occasionally

1c. IF YES, what do you do with the food?

- own use
- give away → to whom? _____
- sell → where? _____

1d. IF NO, do you sometimes help relatives or friends grow food on their land?

- often
- sometimes
- seldom
- Never

2. How often do you buy or get food from the following sources?

	often	sometimes	seldom	never
a. supermarkets	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b. local shops, kiosks, the market	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c. street traders (unofficial)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
d. we grow ourselves or on land of friends	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
e. given food by friends, relatives	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

2f. How can it be expressed in a percentage ratio? For example, 50% from the shop and 50% grown yourself.

3. Where do you typically buy household goods, clothes, etc.?

4. Do you give away things when you no longer need them?

- yes
- no

4a. IF YES, to whom?

4b. Do you receive any?

4c. IF YES, from whom?

5. In the past twelve months did your family have to limit itself in:
- | | often | sometimes | rarely | never |
|--|-------|-----------|--------|-------|
| a. food | [] | [] | [] | [] |
| b. heating | [] | [] | [] | [] |
| c. electricity | [] | [] | [] | [] |
| d. clothes, shoes that are
really necessary | [] | [] | [] | [] |

6. Has the situation changed, become better or worse, since 1991?

7. Do you ever barter for food? Explain.

8. Do you ever barter for other goods and services? Explain.

9. IF YES TO QUESTIONS 7 OR 8, did you barter before 1991?

10. Do you have a preference between buying on the street, at the market or in stores?

11. Do you see shortages of goods in the stores?

C. NEIGHBORHOOD

1. Would you say that you know...?

- [] Most of the people in your neighborhood
- [] Many of the people in your neighborhood
- [] A few of the people in your neighborhood
- [] None of the people in your neighborhood

2. If there was a problem that affected the entire neighborhood (i.e., crime) who would take part in sorting it out (*later changed to would people in the neighborhood get together to address the problem*)?

2a. IF YES, who would be the leader?

3. In the past year how often have members of this neighborhood joined together to address a common issue?

3a. What was/were the problem(s)?

3b. Were any of the actions successful?

3c. IF APPLICABLE, did you undertake this action yourselves because official channels would not?

4. Do problems arise in your neighborhood because of differences between people? For example, differences in education, wealth or religion.

4a. IF YES, how are these problems generally handled?

5. What divides people the most?

6. In the past three (*later changed to four*) years have you personally:

	yes	no
a. voted in an election	[]	[]
b. actively participated in an election campaign	[]	[]
c. taken part in a demonstration (a march) as a sign of protest	[]	[]
d. contacted an elected representative by telephone or by letter	[]	[]
e. made a personal contact with an influential person	[]	[]
f. made newspapers, radio and/or TV aware of a problem	[]	[]
g. notified the court or police about a problem	[]	[]

6h. Will you / did you vote in December? And in March?

6i. Explain why or why not.

6j. IF NO, do your friends encourage you to vote?

6k. Do your friends vote?

6l. IF NO, do you encourage them to vote?

7. How much do you think you yourself are able to influence the state of things in your neighborhood?

8. Has the degree of your influence changed since 1991?

[] increased
[] decreased
[] stayed the same

8a. IF INCREASED OR DECREASED, why?

D. RELIANCE ON OTHERS

1. How often, and with whom, in a month do you:
 - a. eat meals with people outside the home in a restaurant or café?
 - b. receive visitor's at home?
 - c. visit people in their homes?
 - d. get together with a usual group of people to socialize?

1e. Do you socialize with friends more often or less often than in Soviet times? Why?
2. How many close friends do you have?
 - 2a. Characteristics: age, gender, where live, how met?
 - 2b. Do you have more or fewer friends than in comparison with Soviet times? Why?
 - 2c. What was the last new acquaintance you made?
3. Would you say that neighbors usually help each other or does each household depend on itself?
4. On whom do you rely when you have a problem?
5. If you were sick, would you ask your neighbors for help?
 - 5a. IF NO, who would you ask?
6. If you were sick, would (did) you ask your neighbors to look after your children?
 - 6a. IF NO, who would (did) you ask?
7. Who usually looks (looked) after your children when you are (were) at work?
8. If you had to go away for a day or two, who would (did) look after your children?
9. Do you borrow money?
 - [] Yes → from whom? _____
 - [] No
 - 9a. Do they require interest?

9b. Do you borrow money more often or less often in comparison with Soviet times?

10. Do you lend money?

Yes → to whom? _____
 No

10a. Do you require interest?

10b. Do you lend money more often or less often in comparison with Soviet times?

11. When an individual borrows from you or you borrow from someone, are the terms of return made clear?

12. In what layer of the population do the people belong to:

- a. that you loan to, in comparison to you?
- b. that you borrow from, in comparison to you?

13. What would you do if you did not have the money to pay for your communal services or to buy food?

13a. Are there any other variants to decide the problem?

14. Have you helped someone in the community/neighborhood in the last 6 months (*later changed to the last month*)? Explain.

15. Has someone in the community/neighborhood helped you in the last 6 months (*later changed to the last month*)? Explain.

16. Do you rely on the help of others more, less or the same in comparison with the situation before 1991? Explain.

17. Do you consider yourself to be dependent on other people? To what degree:

- very dependent
- not very dependent
- not dependent

18. What does the word "blat" mean for you?

18a. Does it still exist?

E. ORGANIZATION MEMBERSHIP

1. Are you or is someone in your household a member of any groups, organizations or associations?

2. How does one become a member of the group?

Invited

Voluntary choice

Other _____

3. Are you/household member a leader in the group?

4. Do you have an active part in the group? Explain.

5. Do you or your family have any kind of benefits from being a member of the group? Explain.

6. Do members of this group often help each other?

6a. Can you give an example?

7. How long have you been a member of this group?

F. EMPLOYMENT

1. What is your main employment?

- Employed
- Self-employed, own business, own farm
- Unemployed, getting state unemployment benefit
- Unemployed, not getting state unemployment benefit
- Pensioner but still employed
- Pensioner
- Maternity leave
- Housewife
- Student

IF A PENSIONER:

1a. If there was a mistake in calculating your pension, what would you do?

- Write a letter to the pension office asking the mistake to be sorted out
- Keep going to pension office to demand action until it is sorted out
- Go to a friend to see if they can help you
- Offer a present to a person who controls pension administration
- Nothing I could do

1b. With what kind of regularity have you been paid your pension in the last 12 months:

- Always arrived on time
- A few weeks late
- A few months late

1c. IF LATE, how did you get by in the meantime?

1d. Is any of your pension still owed to you?

IF EMPLOYED:

1e. What is your job, place of employment?

1f. IF SELF-EMPLOYED what is the nature of your business?

1g. Are you occupied with the same work that you did before 1991?

1h. IF NO, please give a short biography since 1991.

1i. How did you find your current job?

2. At your place of work, about how much of the week do people really spend producing things for the enterprise?

- All the time
- Almost all time
- More than half time
- About half
- Less than half
- Very little, none

3. IF ABOUT HALF, LESS THAN HALF OR VERY LITTLE, what tasks/activities are they occupied with?

4. Compared to before 1991, how has this situation changed?

- Spend more time really working
- About the same
- Less time really working
- Don't know, wasn't at the same place

5. Do the people who are your immediate colleagues at work usually help each other when problems arise?

6. At your place of work, do people ask you for favors?

6a. IF YES, how often are you offered money for these services?

- Often
- Sometimes
- Occasionally
- Never

6b. Can you give an example?

7. If someone at your place of work was not paid money they had earned, what would you advise to be done?

- Ask the manager to pay what is due
- Go to your supervisor for help
- Offer a present to a person who controls paying the wages
- Take things from employer to sell and get your money that way
- Don't turn up for work, quit the job
- Nothing can be done

14. With economic reform, some people have been able to make more money. To what degree do you agree with the following statements about these people?

	SA	Agree	Disagree	SD
a. work hard	[]	[]	[]	[]
b. take advantage of other people	[]	[]	[]	[]
c. help our economy grow, create jobs	[]	[]	[]	[]
d. use connections	[]	[]	[]	[]
e. intelligent	[]	[]	[]	[]
f. dishonest (<i>later changed to honest</i>)	[]	[]	[]	[]
g. have foreign connections	[]	[]	[]	[]

15. In the past month, have you or anyone else in this family earned money by working at a second job?

- [] Yes → what kind of work? _____
 [] No

15a. Have you sold personal items when you needed money?

16. How much did your family earn last month from all sources for the work that you did?

_____ Rubles

16a. Did you earn any money unofficially?

16b. Do you earn enough money to pay for all of the things that you need?

16c. IF NO, What is a priority and what do you do without?

17. Have you ever received any alternative currencies for work that you've done? Describe.

G. ECONOMIC SITUATION

1. How do you rate the economic situation of your family today?

- [] Very satisfactory
 [] Fairly satisfactory
 [] Not very satisfactory
 [] Very unsatisfactory

2. How would you compare your family's economic situation with what it was before 1991?

-] Much better now
-] Somewhat better
-] Same
-] Somewhat worse now
-] Much worse

2a. Please explain why.

3. Some people live barely making ends meet, while others have extra resources to protect them. If there is a crisis, such as the loss of a job or ill health, some people become impoverished and others are able to survive. How would you consider your family's ability to survive such a crisis? Tell about it, please.

3a. Compared to before 1991?

4. What from the following list is first in line for determining your family's standard of living? Second in line? Third in line?

-] Growing own food
-] Repairing house
-] What we get as favors
-] What we get with the help of friends and relatives
-] What we get in foreign currency
-] Earnings in second job, own business
-] Money that we get on the side, tips
-] Earnings from regular job
-] Pension or unemployment money
-] Benefits given at work, like meals, holidays
-] Other _____

5. What did you buy with your privatization voucher?

5a. Did you receive / do you receive any revenue from your vouchers?

5b. IF BOUGHT SHARES IN A COMPANY, why did you pick that company?

6. What did you think about the voucher program when it first started?

H. SAVING

1. If a person is entitled to get a social benefit, such as unemployment pay or money for communal services, what should he or she do?

- File a claim at the appropriate office and the money will come
- File a claim but go back often until they give you what you are entitled to
- Find a friend or personal contact that can get your benefit paid
- Offer a tip or present to an official to make sure the benefit is paid
- Nothing you can do to get your entitlement
- Other _____

2. Have you or anyone in your family filed such a claim in the past year?

- Yes
- No

2a. IF YES, was it paid:

- Promptly
- After delays
- Not paid

2b. IF PAID LATE OR NOT AT ALL, how did you get by in the meantime?

3. Did you save in Soviet times?

4. Do you save now?

4a. IF NO, why not?

5. If you had some savings, where would you keep them?

- Commercial bank
- State bank
- Shares in companies
- Keep rubles in cash
- Hard currency such as Dollars
- Deutsche Marks
- Gold, precious metals
- Other _____
- Don't know

6. When you are too old to work, what do you expect to rely on? (*“Or on what do you live on now?” later eliminated from question.*)

- State pension
- Children, relatives will provide
- Private insurance, pension
- Savings in bank
- Own a house, land
- Don't know

I. PUBLIC SERVICES

1. What should a person who needs a government permit do if an official says just be patient?

- Offer a "tip" or a present to the official to get a prompt reply
- Use connections
- Write a letter to the head office
- Do what you want without a permit
- Nothing can be done

2. How often do you think bribe-taking and corruption occurs in the federal government?

3. What do you think, in comparison with Soviet times, is the extent of bribe-taking and corruption in the central powers?

- Increased a lot
- Increased a little
- Has remained much the same
- Decreased a little
- Decreased a lot

4. How about public officials in this city? How often do you think bribe-taking and corruption occurs?

5. By comparison with Soviet times, would you say that in this city the level of bribe-taking and corruption has:

- Increased a lot
- Increased a little
- Has remained much the same
- Decreased a little
- Decreased a lot

6. It is sometimes said that there is no need to pay taxes if you don't want to; the government will never find out about it. Do you:

- Strongly agree
- Agree
- Disagree
- Strongly disagree

7. It is said that even if the government found out a person wasn't paying taxes, he or she could always give a "present" to an official who would help him find a way around paying taxes. Do you:

- Strongly agree
- Agree
- Disagree
- Strongly disagree

8. Some people say that nowadays to get anything done by a public agency you need to pay money on the side. Do you:

- Strongly agree
- Agree
- Disagree
- Strongly disagree

9. In the past year, have you or a family member had to obtain any official documents from the state?

9a. Were you successful in getting the documents?

9b. Did you have to pay extra money at any point to receive them?

J. SUBJECTIVE WELL-BEING

1. All things considered, how satisfied are you with your life today?

2. People have different opinions about the most important problems that need to be fixed to make life better. Tell about your problems and order them by degree of importance.

3. In your opinion, what do you see happening in the future in Russia?

4. Do you think that your quality of life will improve or decline in the coming years and why?

5. In what way has your life changed the most because of the regime change?

6. What is the best thing that has happened since 1991 as a result of the regime change?
7. What is the worst thing that has happened since 1991 as a result of the regime change?
8. Do you think that Russia will be a market economy?
9. How would you define a market economy?
10. Do you talk about the political changes with your family and friends?
 often
 sometimes
 seldom
 never
11. What is your opinion of President Putin?

APPENDIX B: LETTER OF INTRODUCTION

Hello,

My name is Laura Taylor. I am a student in the Economics department of Colorado State University in the U.S. I have come to Krasnodar in order to complete the research for my dissertation. The purpose of my research is to study the impact of the transition to the market economy on the well-being of Russian citizens.

For my research, I would like to speak with you about your experiences. Our conversation will be of an anthropological character and will consist of answering several questions regarding work, family and your financial position.

Your answers will be kept confidential. Also, your name will not be associated with any of your answers. You have the right to not answer any questions that you choose.

The conversation will take approximately two hours. If you would like to take part in this, please call me at 39-46-85.

Thank you in advance. Respectfully yours,

Laura Taylor

APPENDIX C: MAP OF RUSSIA



APPENDIX D: CONSENT FORM

COLORADO STATE UNIVERSITY INFORMED CONSENT TO PARTICIPATE IN A RESEARCH PROJECT

TITLE OF PROJECT: Organized Chaos: How Ordinary Russian Citizens are Managing the Transition from Plan to Market

NAME OF PRINCIPAL INVESTIGATOR: Kathleen A. Pickering, Ph.D.

NAME OF CO-INVESTIGATOR: Laura J. Taylor, Graduate Student

CONTACT NAME AND PHONE NUMBER FOR QUESTIONS/PROBLEMS: Laura J. Taylor (39-46-85)

PURPOSE OF THE RESEARCH: The purpose of the interviews are to examine the way in which you and your family have managed the market transition following the demise of communism and how your daily lives have been affected by the change.

PROCEDURES/METHODS TO BE USED: You will be asked several questions concerning your job, your family and your financial position. Some examples of these questions are:

- *Would you say that to get a house or flat in this neighborhood, most people had to have connections?*
- *Does your household have a plot of land where you grow food?*
- *If there was a problem that affected the entire neighborhood (i.e., crime, graffiti) who do you think would work together to deal with the situation?*
- *Suppose you suddenly had to go away for a day or two, who could you count on to take care of your children?*
- *Are you or is someone in your household a member of any groups, organizations or associations?*
- *Compared to before perestroika, has the time people at your place of work spend producing things for the enterprise changed?*
- *How would you compare your family's economic situation with what it was before perestroika?*

The interview should take approximately one to two hours. I will be audiotaping the interview. These audiotapes will be kept for a period of ten years.

RISKS INHERENT IN THE PROCEDURES: You will be assigned a participant number so that your name is not associated with any of your responses. However, the data that you provide will be stored on the same computer as the list of names and their associated participant numbers. Some of the questions that will be asked concern "under the table" activity that may be regarded as unlawful. Be assured that your responses will remain confidential. In addition, you have the right to refuse to answer any questions.

It is not possible to identify all potential risks in research procedures, but the researcher(s) have taken reasonable safeguards to minimize any known and potential, but unknown, risks.

BENEFITS: Although you may not personally realize any benefits from participating in this study, your participation is invaluable and will greatly help individuals that are studying the Russian transition to a market economy identify how this period of change has affected the daily lives and well-being of Russian citizens.

CONFIDENTIALITY: As stated above, all participants will be assigned a random number so that individual names are not associated with individual surveys. The identity of participants will be protected through storage on a computer in a locked office that requires entry of a username and password in order to access the data.

LIABILITY: The Colorado Governmental Immunity Act determines and may limit Colorado State University's legal responsibility if an injury happens because of this study. Claims against the University must be filed within 180 days of the injury. Questions about participants' rights may be directed to Celia S. Walker at (970) 491-1563.

PARTICIPATION: Your participation in this research is voluntary. If you decide to participate in the study, you may withdraw your consent and stop participating at any time without penalty or loss of benefits to which you are otherwise entitled.

Your signature acknowledges that you have read the information stated and willingly sign this consent form. Your signature also acknowledges that you have received, on the date signed, a copy of this document containing 2 pages.

Participant name (printed)

Participant signature

Date

Witness to signature (project staff)

Date