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Monopolistic behaviour, corruption and rent seeking in Russia : the institutional foundations of an economic “pathology”

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Why putting together such different economic objects as monopoly, oligarchy and corruption ? To be sure, many facts seem to link together them in Russia. One of them is that they are all, in a sense, an illustration of “rent seeking”.

Rent seeking : classical definition

In its classical definition, a rent is an undue taxation imposed by an economic agent to others, thanks to a position of monopoly. The author who most contributed to the popularisation of the concept of rent seeking in Russia is Anders Aslund (Aslund, 1995). He rightly pointed out this problem as one of the biggest “pathologies” of the Russian economy. Natural monopolies are abundant in the Russian economy, oligarchy has been playing a prominent role in the recent political and economical evolution of the country, and the list of cases of distorted competition, *blat* and other forms of corruption is almost endless.

Before studying the implications of rent seeking in the Russian economy, it is necessary to distinguish between rent and profit. Following the ricardian definitions, many economists assume that profit is generated by the efficient use of capital and labour in a competitive context, while rent would be the product of an ex-ante favourable endowment with means of production or legal privileges. All rents are not avoidable, nor perverse from an economic and social point of view ; some rents can be efficiently used in order to benefit to a large part of the population. The distortions that rents can introduce into the distribution of earnings can and should be controlled. They also need to be corrected to the extent that they are harmful to the economy.

The Russian case can be used to address some theoretical and practical questions about rent seeking : What are the conditions favourable to a development of rent seeking ? In which sense can a rent be seen as inappropriate ? How should it be used properly ? What are the means to ensure the right distribution of a rent ?

The limit of Anders Aslund’s analysis as applied to Russia is that it only grasps the efficiency dimension of rent seeking. Rent seeking is seen as an opportunity cost supported by the community. But the Russian case itself shows how much this account is incomplete. Corruption, rent seeking and monopolistic behaviours are economically significant not only because they involve a inefficient use of resources, but because of their institutional dimension.

The institutional dimension of rent seeking

The Nobel Price winner Douglas North (1991) defined institutions as “rules of the game” in the economy. These sets of rules provide guidelines for individual behaviours. In that sense, they shape the competitive context in which economic actors make their decisions. But

institutions, as human devices, are themselves subject to evolution and competition : their development is interdependent with technological, demographic and socio-political changes affecting the society.

In order to survive and develop, any institution has to ensure a form of superiority vis-à-vis individuals : its influence upon a given individual must be superior to the influence (s)he can exert on it. If this asymmetrical relationship is broken, then the rules provided by the institution are no longer effective. In this light, rent seeking and its manifestations (corruption, oligarchic behaviours, etc.) become a much more larger phenomenon than in the classical presentation : whenever a private actor can impose its own set of rules to others, it raises new opportunities for rent extraction. In this sense, corruption is a monetary illustration of rent seeking, and rent seeking is an economic illustration of the ineffectiveness of certain public institutions.

The role of the State in fighting rent seeking

Following this, what could be the role of public institutions in fighting corruption ? Quite often, corruption is associated with the size of the State in the economy. There is some kind of naïve equation built up by certain observers, according to which the bigger is the State, the bigger is the amount of money you can make in corrupting civil servants, and the bigger must be the corruption phenomenon.

This conception is not well informed, neither theoretically nor empirically. A consistent adverse theoretical point of view should be that the strongest is the State, the weakest is the corruption, since resources used to fight rent seeking are greater. Empirical support to this thesis can be found in the countries ranking of Transparency International : the less corrupted countries (namely, Scandinavian countries) are not those in which the State is playing the weakest role. Conversely, a majority of weak state institutions (in terms of perimeter and resources) can be found in the most corrupted countries.

But what is exactly a “strong state”, from an economic point of view ? The institutional analysis shows that it is not merely a matter of percentage of GDP absorbed by its budget, even though a State with poor resources will face many difficulties in building public institutions able to compete efficiently with corruption or rent seeking. By “strong State”, we do not mean either a State that has built up strong capacities of controlling the activities of the society ; we rather have in mind some qualitative aspects of the functioning of the public institutions, such as :

- Stability : the role of the State is to provide a stable environment for individual decisions. During the 1990's, Russia has experienced a period of legal and political turmoil that fuelled the general sentiment of urgency. During the first half of this decade, institutional stability has improved ; still, a lot is to be done in this field, especially at the regional and local levels. Reducing uncertainty concerning the future is of utmost importance for the long-term growth rate of private investment and consumption throughout the Russian territory.
- Simplicity : institution building must look for simplicity, in order to provide rules that can be understood by the whole society. In Russia, at a time when President Eltsine was signing several thousands Presidential decrees a year, complexity contributed to the general weakness of public rules. The current set of the legal framework surrounding economic activities still needs an enormous work of cleaning in order to make it more

readable for both those who are supposed to adhere to it and those who are supposed to guarantee its enforcement.

- Coherence : without stability nor simplicity, institutions cannot be coherent. The Russian case is a telling example of inconsistency of reforms. Along with simplification, the quest for coherence in a single policy should be a top priority in order to facilitate the enforcement of the regulations and to raise their economic and social efficiency.
- Collective character : every institution has to be the result of some kind of consensus among the society. As the Russian case shows, the ability of the authorities to obtain the support of a large part of the population during the process of reforms is one of the keys for the success. In Russia, as time goes on, the democratic process should be scrupulously observed in the process of institutional consolidation.

These observations explain why privatisation, which was sometimes presented in Russia as the panacea in the struggle against corruption, is hardly convincing. During its recent history, Russia provided numerous examples of the way in which privatisation, conducted without appropriated institutions, can fuel corruption, monopolistic behaviours and rent seeking much more efficiently than any public management.

Rent seeking and the management of public sector in Russia

Rent seeking is an almost universal individual behaviour, that could be interpreted in evolutionary terms as the quest of a “ecological niche”. To ensure that this behaviour will not be too detrimental to the distribution of earnings in Russia and that it will not generate too many negative externalities throughout the whole society, the role of Russian State is determinant. Moreover, since State institutions are targets of rent seeking, some precautions should be taken by the authorities in order to immunise them against this form of pathology. Some of them could be rapidly implemented in Russia :

- to define a reasonable (not maximal) level of public earnings in percentage of the GDP, in order to secure the balance of economic power between public and private institutions ;
- to ensure good working conditions (among which decent salaries) to civil servants, so as to make public careers attractive and allow a selection between candidates ;
- to impose and enforce the principle of accountability of any civil servant or political representative, with appropriate sanctions when the principle is violated ;
- to maintain a mechanism of “checks and balances” at any level of public responsibility, in order to guarantee that any decision made by a civil servant or a public representative is oriented toward the public good.