

# PRIVATISATION OF INDUSTRIAL ENTERPRISES IN RUSSIA

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To my parents,

to their love and care and guidance,

I owe a debt which could never be repaid.

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The original inspiration to work on "Privatisation in Russia " came from the active suggestions of my previous supervisor - Late Prof. Jayashekar - who, unfortunately, could not see it in its complete form. He constantly guided my work till his untimely death did us part. May his soul rest in ~~an~~ eternal peace.

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SAROJ KUMAR ROUT

## **PREFACE**

Any change in the political sphere necessarily brings about changes in the economic and social spheres as well. With the collapse of communism and the demise of the all-powerful Communist Party in the erstwhile Soviet Union, the mighty commands were mercifully gone and so too inevitably, was the system of enterprise management, thus resulted in state enterprise facing a lack of clear incentives for restructuring as well as the challenges of significant dimension. At this crucial juncture, the Russian economy needed for internal restructuring to adopt to market forces, the establishment of independent profit centres in large enterprises, the introduction of incentive pay systems and so on.

Such a transition to market economy means looking for concrete market forms for the functioning of society as a whole as a socio-economic agent on a par with such agents as the individual and the collective, which, in turn, is possible only when the market is created as a system of relations based on a system of circulations and turnovers of social capital, the social product and consumer incomes. In conjunction with macro-economic stabilization, currency convertibility and rapid legal reforms introduced in Russia, a new and vibrant private



sector is growing with remarkable speed. This came as a corollary to the rapid privatization programme, introduced in the post-communist Russian economy.

This dissertation deals comprehensively but extensively with the process and progress of privatisation in Russia during its transition from a centralized administrative-command model to a self regulating market model of economic relations.

The first Chapter depicts a brief idea about the existence of autonomous sector in the erstwhile socialist economy of USSR and an overall idea about the coexistence of both public as well as private sector in the economy. This chapter puts in place the new institutional framework for transition to a market economy in the Soviet Union, and the sequencing of various reforms during the run-up to establish a market economy based on private property rights. Towards the end of this chapter the concept of privatization in general and in Russian context in particular, has been explained with clarity as well as precision.

The second chapter analyses the economic, social and political objectives of privatization. This chapter also tries to make an inter-relation between the

different objectives of privatization, in the context of a systemic analysis.

The third chapter of this dissertation broadly outlines the process of privatization and the legal bases laid down by successive legislative acts, including presidential decrees, to make the process irreversible.

The fourth chapter vividly explains the progress of privatisation. This chapter analysis the changes in the volume of production of and the allocation of investible resources in industrial enterprises, while implementing the privatisation program.

At last, the conclusion speaks a few words about the problems and prospects of privatisation of industrial enterprises in Russia.

## CHAPTER = 1

### INTRODUCTION AND THE BACKGROUND OF PRIVATISATION

Russia's move toward a 'civil society' involves two basic goals. One is the installation of a pluralistic society and swift advance towards implanting democracy as the basic principle of Russia's socio-political organisation. The second goal is the elimination of the centralized administrative-command economic system and envisaging a private market economy as the counterpart in the economic domain of democracy in the political sphere. In order to achieve the twin objectives, Russian economy needs not only decentralization in the arena of economic decision-making, but also the full recognition of private property rights and withdrawal of the state from its heavy involvement in the allocation of scarce sources.

Under the communist system, managers acted according to the commands of supervisory bureaucracies, whether in the government or the Communist Party apparatus. These commands were backed up by terror or, atleast, its threat. With the demise of the Communist Party, the commands are mercifully gone and so too, inevitably, is the system of enterprise management. In conjunction with macro economic stabilization, currency convertibility, and rapid legal reforms introduced by the post-communist governments, a new and vibrant private enterprise sector is growing with remarkable

speed.<sup>1</sup> However, for the large industrial enterprises that remain in the state sector, the collapse of the old system has been followed by mix of aimlessness, political rent-seeking, asset-stripping, and corruption and not by the clear motivation of wealth-maximization<sup>2</sup> that comes with private ownership.

\* \* \* \*

### **The Traditional Private Sector :**

The traditional private sector has had mixed fortunes over the years, depending on the dominant political trend and on the results achieved by the state sector. In spite of a limited amount of integration and cooperation with the state and cooperative sector,<sup>3</sup> the traditional private sector has generally been rather backward in character. Besides, the traditional private sector has been largely separate from, and often

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1. Sachs, Jeffrey D., "Privatization in Russia : Some Lessons from Eastern Europe", American Economic Review, 82(2), May 92, p.43.
  2. Ibid., p.43.
  3. Laky, T(1990), "The Reality and Potentials of Autonomous Entrepreneurship", paper presented to the IV World Congress for Soviet and East European Studies, Harrogate, 21-26 July.

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antagonistic to, the socialized sector.

Apart from a fairly limited number of cases, the traditional private sector consisted mainly of independent work, not of entrepreneurship. The common features of traditional private activities in both these cases were their small size and their reluctance to invest.

The fundamental causes of the underdevelopment of the private sector were the uncertainty caused by frequent changes in government policy and the lack of inputs, i.e., the dependence of the private sector on socialized firms for supplies. Besides, in a shortage economy, adequate incomes could be earned without innovation or risk but merely by relying on traditional, cheap, labour-intensive technology and good quality work.

Against this background the systemic change now under way in Russia is confronting and solving a three fold problem :

(i) how to develop the existing private sector, with an increase in the number of private firms and an expansion in their size;

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4. Morz, B.(1990), "Private sector and Economic Reform : The Case of Poland", paper presented to the IV World Congress for Soviet and East European Studies, Harrogate, 21-26 July.

(ii) how to privatise a large part of the state sector, in particular industrial enterprises and state farms; and

(iii) how to stabilize a difficult economic situation.<sup>5</sup>

### he Autonomous Sector:

It has been well recognised that in socialist systems there is an autonomous sector that grows in the shadow of the centrally planned system.<sup>6</sup> This raises the question of the relationship between the autonomous sector and the socialist sector existing in the erstwhile command-administrative economic system in the former U.S.S.R.

According to the conventional definition, the autonomous sector consists of all economic activities which are not directly controlled or commanded by the state. Going by this definition three different fields of economic activity may be distinguished :

- (i) the legal sector of the private economy,
- (ii) the underground economy, and
- (iii) household production as well as informal activities among various households.

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- 5. Dallago Bruno and Others (Ed., 1992), Privatisation and Entrepreneurship in Post-Socialist Countries pp.14-15
  - 6. Kornai, J. (1990), 'Preface to the Soviet Edition of Economics of Shortage', in J. Kornai, Vision and Reality, Market and State, New York, London : Harvester-Wheatsheaf, pp. 205-213

The legal private sector includes those activities that have been assigned to private producers by the socialist state. It consists mainly of somewhat limited agricultural production, small-scale business, trades and services. These activities are handed over to the private producers because they are technically difficult to integrate into the centrally planned economy, although there is a need for the products and services they provide. Moreover, within the process of recent economic reforms, growing shortages and the need for more economic efficiency have induced the Soviet government to allow some increase in such private activity.

The underground economy encompasses all those activities declared illegal by the state and conducted in pursuit of private gains. They may take place within the socialist sector or they may operate in parallel with it. Within the socialist sector we find such activities as barter trade among enterprises to achieve plan targets and crypto-private production, which enables managers and workers in socialist enterprises to produce for their own purposes under the shelter of a socialist enterprise. They may also be illegal, mainly redistributive activities involving the theft of time,

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7. Grossman, G. (1977), The 'Second' Economy of the USSR, Problems of Communism, p.31

of raw materials, of semi-finished and finished products; the deterioration of contracted quantities and qualities; bribery in order to obtain products needed; or, to a limited extent, tax evasion. In parallel with the socialist sector there is, for example, the underground production of goods in shortage or of illegal products; illicit labour by individuals supplying non-official services in trades, repairs and education; or simply black market activities.

Unlike the above activities, non-market household production is legal. It is not profit-oriented and varies according to location. Because of the availability of production facilities, it is more common in rural areas than in urban centres. Such non-market activity also comprises informal activities among households - for instance, taking care of children (baby sitting, etc.), neighbourhood help (shopping, cleaning, repairs) or assistance by charity organizations which provide free meals, fuel, clothes, and household work (washing, repairs, etc.).

Moreover, the autonomous sector offers ample scope for participation : legal activities in the non-market household economy and the official private sector or activities in the underground economy. Since the official private sector and the underground economy are profit-oriented, the decision whether or not to become active in the private sector or in the household and informal economy depends largely on the individual's



needs for subsistence, his orientation towards profit, and on his command over internal and/or external resources. It also depends on his assessment of the potential gain from such activities in the autonomous sector.

The autonomous sector appears to have overcome the production bottlenecks in socialist economies. Shortages are eased, the welfare of individuals increases, the population becomes more tolerant of economic crises and more receptive to politico-economic experiments aimed at reforming the system. The survival of the population seems to be guaranteed. To some extent, the failures of the planning mechanism are remedied and even inflation pressures may be alleviated. The autonomous sector seems to support and stabilize the socialist regime's public (purist) image.

Yet not all members of society may be able to operate in the autonomous sector; a sector, moreover, which produces goods and services which are often regarded as officially undesirable (alcohol, prostitution, and gambling). Such production also depletes the resources of labour and capital, raw materials, semi-finished and finished products.

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8. Altman, Y. (1989), Second Economy Activities in the USSR : Insights from the Southern Republics, in P. Ward (ed), "Corruption, Development and Inequality, London : Macmillan, pp.66-67.

Frequently, such resources are stolen from the socialist sector, and tax revenues decrease. A typical example is provided by the Soviet Union, where official alcohol sales dropped by more than 60 per cent between 1985 and 1988, increasing the budget deficit while consumption in general simultaneously seemed to stagnate. In addition, the autonomous sector does not generate major investments. However, the autonomous sector acted as a stabilizer of the society of shortage.

### The Shortage Economy :

Shortage in an economy can be defined as a situation in which certain products, inputs or services are unavailable; or as a situation in which enterprises, non-profit institutions or households are forced to resort to impoverished adaptation in order to cope with shortages. For instance, a scarce product or service is usually substituted by one which is inferior in quality or more expensive.

In the Soviet economy, shortage is seen as a general phenomenon which manifests itself in all important fields of the economy : the market for consumer goods and services, production, the labour market, investments, foreign trade and international

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9. Kornai, J. (1986), The Reproduction of Shortage, in J. Kornai, "Contradictions and Dilemmas - Studies on the Socialist Economy and Society", Cambridge, The M.I.T. Press, p.12

currencies. Moreover, the shortage phenomenon is chronic and ever-present. The system ensures the reproduction of shortages of great intensity which have a major impact on the behaviour of all members of the society. As a consequence, the manifestation of general, chronic, self-generating and intense shortage characterizes the Soviet system as a society of shortage or shortage economy.<sup>10</sup>

Within the command-administrative economy, political and ideological goals were given priority over other considerations. In view of the low level of its economic and technological development compared with that of democratic market-type economies, and since its aim was to build a communist society, such command economy focused exclusively on material growth. A peculiar interpretation of Marx's theory of reproduction has led to the establishment of a national accounting system. Material growth is most rapidly achieved by concentrating on the investment goods industry. This, however, entails neglecting the consumer goods and service industries, which are allocated smaller resources. Hence consumers suffer from shortages. At the same time, promotion of private production is considered to be ideologically inappropriate and unnecessary : resources for the private sector were

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10. Kornai, J., 1990, p.207

consequently reduced, production in the sector declined, and consumers continued to suffer from shortages.

Besides, hard budget constraints in the private sector (firms and households) rationed private demand while the socialist sector was simultaneously subjected to soft budget constraints which did not limit demand. The losses incurred by enterprises, because of their insufficient use of inputs and because of the structure of state-fixed prices, were usually covered by the state. Enterprise insolvencies or unemployment did not officially occur, since they are both unacceptable to, and incompatible with, the socialist command-administrative economy.

Moreover the system's inherent orientation towards material growth gave rise to a strong need for enterprise investment and was accompanied by a general expansion in the administration. This expansion brought further power, influence and higher salaries for the bureaucrats, who tend to enlarge their apparatus, while additional resources were absorbed by the socialist sector.

Furthermore, the central plan did not cover all entrepreneurial and individual decisions. It deliberately omitted certain decisions-for example, those concerning the purchase of goods or the choice of workplace by individuals. In addition, the planning system was static : it was not flexible enough to react

to unforeseen events (e.g. drought, natural catastrophies, embargoes, etc.). Incomplete and delayed planning generated bottlenecks and uncertainties in the supply of materials. Enterprises reacted by hoarding and stockpiling inputs. This confirmed "shortage breeds shortage"<sup>11</sup>. These shortages were further aggravated by the use of monetary prices which did not reflect scarcities, and by use of money which did not serve as a store of value and as a universal means of payment. The results of this economy of shortage bred an autonomous sector which has been discussed in the preceding pages.

#### **The Run-up to Economic Transition :**

The year 1990 saw a substantial increase in the number of legislative acts, including presidential decrees, designed to put in place the new institutional framework for transition to a market economy in the former Soviet Union. This had been made possible by a restructuring of the system of political representation which opened the way for wide-ranging public political and economic debate on a scale not experienced since the 1920s.

The first blueprint advocating a comprehensive dismantling of the previous system of economic management was offered by Deputy Prime Minister

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11. Kornai (1990), P.207

Academician L. I. Abalkin in November 1989. This radical programme was one of the sources used in the more cautious draft offered by the then Prime Minister N. I. Ryzhkov to the Second Congress of People's Deputies in December 1989 and in revised and more radical form to the Supreme Soviet in May of the following year. This, however, did not meet the approval of the Supreme Soviet. A more detailed variant of his own November programme was completed by Deputy Prime Minister Abalkin in August 1990 embodying the concept of a "regulated market economy". However, this was superseded by a joint inter-republican working group under the direction of Academician S. S. Shatalin which produced what came to be known as the "500 Days" programme in the same month.

The "500 Days" programme also failed to muster general support. Both the Shatalin and Abalkin plans were used in the drafting of a compromise programme by a team chaired by Academician Aganbegyan very shortly afterwards.<sup>12</sup>

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12. Stabilization, liberalization and devaluation : Assessment of the economic situation and reform process in the Soviet Union, Commission of the European Communities, 'European Economy', No.45, December, 1990, pp. 83-98.

The basic policy document for the transition to a market economy now in force was the "Main guidelines for Economic Stabilization and Transition to the Market", adopted for implementation with immediate effect by the USSR Supreme Soviet on 19 October 1990<sup>13</sup>. The immediate objectives were to improve government finances and control the money supply, restructure the banking system, regulate enterprise sector finances and raise interest rates to protect savings. Steps were taken to balance consumer incomes and expenditures including the provision of incentives for consumer goods production. All these were done in the first phase of the programme.

The second phase was dominated by a gradual transition to market prices for a broad range of technical and consumer goods, continued control of price rises by tough financial and credit policies and the maintenance of state prices for at least one third of all goods (fuel, raw materials and semi-finished goods), the monitoring and regulation of retail prices of consumer necessities, privatisation of small enterprises and reallocation of investment toward consumer goods production.

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13. Pravda, 18 October 1990; Izvestiya, 20 October 1990 (for the Supreme Soviet resolution on its adoption)

The prime objective during the third phase was full stabilization of the market for both consumer and producer goods on the basis of market forces and increased supplies. The restructuring of mutual relations between enterprises and local authorities and price liberalization were to be carried out further against the background of equilibrium prices, balanced government budgets and markets for goods and services, a modern banking system and a currency market.

With regard to the longer-term objectives following stabilization, the first paragraph of the "Guidelines" begins with the words, "There is no alternative to switching to a market". This is "dictated solely by people's interests and aims to create a socially oriented economy, gear all production to consumer needs, overcome the shortages, and the disgraceful queues, ensure citizens' real economic freedom and establish conditions for encouraging hard work, initiative and high productivity".

### The "500 Days" Programme

As the most radical of the transition blueprints, the "500 Days" programme was prepared under the joint responsibility of Presidents, Gorbachev of the USSR and Yeltsin of the RSFSR. The general objective of the "500 Days" programme was stated to be the implementation of measures in a short time to lay the foundations of a new economic system which, without extraordinary efforts on the part of the state will orient production towards the



satisfaction of private and social needs, create effective stimuli for work and entrepreneurship, guarantee the saturation of the market with all kinds of goods at stable prices and ensure prosperity for the country and its peoples of all the nationalities.

The programme was divided into four different stages : the first phase (the first 100 days, roughly the beginning of October 1990 to the beginning of 1991), the second phase (day 100 to day 250), the third phase (from the 250th to the 400th day) and the fourth and final stage of the programme (the 400th to the 500th days).

**Major differences between the two programmes :**

With regard to institutional factors, the most important was the setting of specific objectives and a tight time-table for the removal of state controls on prices and for privatisation in the "500 Days" programme. The "Guidelines" appeared to have advocated a more limited aspect of privatization, stressing the distribution of shares to workers in state enterprises. The "Guidelines" were also more circumspect than the "500 Days" programme with regard to the privatization of land, advocating the distribution of land use rights rather than outright sale of land as proposed in the latter.

The "500 Days" programme provided for emergency measures to achieve the virtual elimination of the budgetary deficit by the fourth quarter of 1990 while the "Guidelines" foresee its being maintained well into the 1991 and for the year as a whole. This programme also contrasts with the "Guidelines" and subsequent legislation in its summary rejection of administrative actions and penalties to maintain inter-enterprise delivery obligations beyond July 1991. Even in its early stages it stressed instead the role of free inter-enterprise trade on a contractual basis to preserve the momentum of the transition process. The "500 Days" programme also specifically rejected administered producer prices in 1991 (actually introduced at the beginning of 1991), advocating instead an extension of the new freedom to conclude free and contract pricing in inter-enterprise exchanges apart from those involving fuel, energy and certain raw materials.

However, one of the main weaknesses of both programmes is their treatment of the price problem. The "500 Days" programme did not directly discuss either the likelihood, the extent or the control of the inflationary pressures which have built up and are still rising in the Russian economy. But it makes the implicit assumption that the problem will be dealt with by a combination of increasing competition and cost reductions as enterprises raise their efficiency and cut their previously excessive use of materials. The

"Guidelines" did implicitly accept the need for higher prices though actual price policy, based on the programme relied on administered rather than market prices.

### The Concept of Privatization :

The word "Privatize" first appeared in a dictionary in 1983 and was defined narrowly as "to make private, especially to change (as a business or industry) from public to private control or ownership".<sup>14</sup> But the word has already acquired a broader meaning; it has come to symbolize a new way of looking at society's needs, and a rethinking of the role of government in fulfilling them. It means relying more on society's private institutions and less on government to satisfy the needs of the people. Thus, privatization is the act of reducing the role of government, or increasing the role of the private sector, in an activity or in the ownership of assets.

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14. Webster's New Collegiate Dictionary, 9th ed. (Springfield Mass. Merriam, 1983), 936. The earliest use appears to have been in Peter F. Drucker, in The Age of Discontinuity (New York : Harper & Row, 1969); he used the term "reprivatization". Robert W. Poole, Jr., shortened it to "privatization" and used it in the Reason Foundation newsletters (Santa Monica, Calif.) beginning in 1976.

Privatization appears in several forms. Contracting with private firms to finance, construct and operate waterworks or prisons, or to sweep the streets, prune trees, or repair ships, is a form of privatization. So is contracting with a not-for-profit agency to deliver "meals on wheels" to elderly shut-ins, or to operate a halfway house. Issuing food stamps and housing vouchers to the poor are examples of privatization that are far different from having government run farms and grocery stores and public housing projects. Urban dwellers practice privatization when they form neighbourhood security patrols and so do sub-urbanites who join volunteer fire departments. Selling off or denationalising a state-owned airline, factory, or coal mine is privatization, and it is privatization when government retires from the business of insuring home mortgages or running commuter buses and lets the market place provide those services.

#### **Privatization in Russian Context :**

In fact, some confusion has been caused by the different meanings attached to the term "privatization". Privatization can be seen as a process that takes the state (political bodies as well as government administration and 'nomenklatura') out of the decision making over the allocation of the returns from state-owned assets. In another sense, the term "privatization" is often implicitly restricted to the sale of state-owned enterprise assets.

In the first sense, privatization encompasses "corporatization" - the enterprise reform which alters the legal status of farms from state agents to corporations or joint-stock companies supervised by a state asset-management agency, and the nationally separate "commercialization" - the subjection of their management to the task of maximizing the value of assets subject to a hard budget constraint. The sale of assets is then regarded as the final stage in this process.

Asset sale in the transitional economy of Russia is generally separated into "small" (or "petty") privatization and "big" (or "real") privatization. Althoughn there is no hard and fast dividing line between them, petty privatization is essentially concerned with the sale to the general public of capital assets that should never have fallen under state control. On the other hand, big privatisation usually refers to the sale of the property rights to the large and monopolistic state-owned entgerprises.

**Major factors necessitating privatization in Russia :**

Privatization in Russia is quite different from that in the West. The main driving force behind privatization in the West is always explicitly political (such as reducing trade-union power or enhancing socio-political stability. But in the Russian context, the policy formulation on privatization has been largely a

reaction to the denial of private property rights under communism and, in turn, the desire to rectify the all-embracing power, including that over the state-owned capital assets, assumed by the entrenched bureaucracy.

Related motives were to enhance freedom and hence the democratic process. For that, some critical minimum of property rights reform and outright divestment had to be undertaken quickly, for a democracy without a solid market economy is unthinkable.

### Debate on Privatization :

The dominant theory today is that there can be no market without private property, which forms the agents of single circulation of parts of the gross social product and consumer income. Three avenues of transition to a market can be identified in scientific works, programs, and laws : the first advances the privatization of state property (economic property), free prices, and the social protection of the working people as basic prerequisites; the second envisages the destruction of the old socio-economic system through the total decentralization of the economy, with the state's only concern being consumer demand; the third is based on the economic advisability of multilevel regulation that has as its foundation the monetary regulation of

all reproductive proportions.

The first two variants view as a starting condition the privatization of state property with all destructive socio-economic consequences of the restructuring of reproductive circulations and turnovers. While the third variant affects the agents and forms of property only indirectly rather than directly.

On the contrary, R.V. Arkhipov, V.A. Volkonski, V.V. Mironov, I. In. Mironov, V.N. Rassadin and E.F. Saburov argued, "When we talk about the market, we usually have in mind a system of economic relations that may arise, if we liberalize current economic activity and the commodity market without eliminating the subordination of enterprises to the administrative-command hierarchy and without altering property relations.<sup>16</sup> Further, they argued that a necessary condition to the effective functioning of an economic system is the legislative differentiation and

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15. Gritsivk Grigori; "Privatization : Reality and Mirage of the Market", Problems of Economic Transition; 35(9); Jan'93; p.46.
16. Arkhipov, R.V.; "The Path to Privatization"; Problems of Economics; December 1991; p.23

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guaranteeing of the economic rights and responsibilities of specific agents of economic activity.

Notwithstanding the general perception that Soviet economy is allocationally inefficient, Robert S. Whitesell, citing the results obtained by Rosefielde, Danilin, Toda and Padma Desai and others, rightly argues that a number of econometric studies show the Soviet economy to be allocationally efficient.<sup>17</sup> He suggests that such results do not necessarily contradict the fact of poor performance. On the contrary, it may be that lack of technical progress, the slowness of change, helps to explain allocative efficiency.

Despite several allegations and counter-allegations on the question of privatization the Russian economy is still forging ahead with the programme of privatization in its various sectors.

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17. Whitesell, Robert S.; "Why does the Soviet Economy Appear to be Allocationally Efficient?", *Soviet Studies*; 42, 2, 1990, pp. 259-268.



## CHAPTER - 2

### OBJECTIVES OF PRIVATIZATION

Several major forces, or pressures, are behind the privatization movement in Russia : pragmatic, ideological, commercial, and populist. The goal of the pragmatists is better government, in the sense of a more cost-effective one. The goal of those who approach the matter ideologically is less government, one that plays a smaller role vis-s-vis private institutions. The goal of commercial interests is to get more business by having more of government's spending redirected toward them. And the goal of the populists is to achieve a better society by giving people of Russia greater power to satisfy their common needs, while diminishing that of large public and private bureaucracies.

The arguments put forward by the above forces, or pressures, are quite obvious. One, prudent privatization leads to more cost-effective public services. Two, government is too big; too powerful, too intrusive in people's lives and therefore is a danger to democracy. Government decisions are political, thus are inherently less trustworthy than free-market decisions. Three, government spending is a large part of the economy; more of it can and should be directed toward private firms. State-owned enterprises and

assets can be put to better use by the private sector. Last, people should have more choice in public services. They should be empowered to define and address common needs, and to establish a sense of community by relying more on family, neighbourhood, church, and ethnic and voluntary associations and less on distant bureaucratic structures.

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In fact, the basic objectives of privatization in Russia are social, economic and political.

I. **POLITICAL OBJECTIVES** :

To call a spade a spade, the attempt to introduce the mechanisms of privatization in Russia and economy has been largely a reaction to the denial of private property rights under communism, and, in turn, the general desire to rectify the all-embracing power, including that over the state-owned capital assets, hitherto assumed by the entrenched bureaucracy. Other motives are to enhance liberty of the individuals and hence the democratic process in Russia. In order to achieve these objectives, it was well recognised that the role of state has to be minimised so that the basic individual liberty is guaranteed and the true spirit is imbibed.

The above political objectives are in line with the main elements of the justifying theory of Western or liberal democracies, which rest on two maximizing claims - a claim to maximize individual utilities and a claim to maximize individual powers. Such importance of "freedom of choice" claims a sort of political consumers' sovereignty which ensures that the society will respond to changes in consumer preference, just as the market economy responds to changes in effective demand. Here the objective is to establish a free Russian society where the preference will be for individual freedom of choice of work and reward rather than authoritative allocation of work and reward. The assumption is that man's unlimited desire for consumption and his right of unlimited appropriation is needed as an incentive to increased productivity. And an incentive to increased productivity is needed to make possible the increase of wealth which the new enterprising class in Russia sees in prospect for themselves.

#### **State's Minimal Role :**

The preference for individual freedom of choice of work and reward rather than authoritative allocation of work and reward by the state aims at guaranteeing the Russians their rights and liberties. Article.2 of the Constitution of the Russian Federation (1993) states that "Human beings and their rights and liberties are the supreme values. The recognition, observance and

protection of human and civil rights and liberties is  
the obligation of the state.<sup>1</sup> Also libertarians  
emphasize that true liberty requires private ownership  
with the role of government in economic affairs  
restricted as much as possible to the enforcement of  
private property rights. They further stress that  
public goods should be provided by the state only when  
it has a comparative advantage over private goods.

Another objective of privatization was to  
establish the minimum institutions required for the  
system of capitalist enterprise. These are a legal  
contractual freedom to use one's person and property in  
the most gainful way one can see, and a system of  
markets in which labour, capital and land would  
continually find prices that would induce their  
proprietors to enter them in the productive process.

### **Strengthening Democracy And Social Stability**

In fact, a democracy without private property  
rights is hard to envisage. Private property rights are  
also held to be a condition for establishing market  
economy.

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1. The Text of the Draft Constitution published in  
The Current Digest, Vol. XLV, No.45 (1993), p.4

Russia's leading political forces have proclaimed a course toward destatising property and discontinuing the State's monopolistic position in the economic sphere.

Before the process of privatization began in the erstwhile USSR, ninety per cent of the country's productive fixed capital was the indivisible property of the state. It centralized in its hands about 80 per cent of the national income that was created and managed enterprises directly. As a result, the working people and their collectives had been alienated from ownership of the means of production and the product and from the management of economic affairs. The State was mediating all the processes. Motivation for effective labour and enterprise were eliminated. This brought the entire system to a crisis. In other words, to cling to the monopoly of state ownership means dooming the economy to total collapse. Hence guaranteeing private property rights to the Russian citizens was deemed to be a precondition for privatizing the state-owned enterprises.

Suffice it to say, establishing a democracy in a society without a middle-class required the quick divestment of a substantial part of state assets to make the political revolution irreversible and to provide a buttress for market-oriented economic transformations.

## Eradication of the "Nomenklatura"

The privatization program aims at taking the political and government bureaucracy out of the arena of decision-making over the allocation of capital assets and removing the 'politically appointed enterprise management' (nomenklatura). For this would help focus the behaviour of economic agents more sharply on economic matters.

Moreover, privatization would provide an opportunity for new owners to monitor management and hire labour according to market-based criteria.

## II. ECONOMIC OBJECTIVES :

The prime economic objectives of the privatization program in Russia have resembled those that have prompted privatization in other countries : to transform non-competitive and inefficient monopolies into streamlined, market oriented enterprises with greater freedom to increase investment or set realistic prices that finance their operations by profit rather than credit from a deficit-ridden state budget.

### Promotion of Economic Efficiency

In the erstwhile USSR, too large a public sector led to intolerable inefficiency in production resource

allocation and adaptation to structural change in the economy. The state had a huge monopolistic public sector dominating the entire Soviet economy in all its economic activities. In order to reverse the status quo, assets of the state-owned enterprises need to be entrusted to private owners or privately motivated managers, which should, in turn, promote economic efficiency in the adaptive, allocative and productive senses.

Besides, it was well recognised that the government was not a good manager of economic resources or a good monitor of the assets it entrusts to others. Its motive was not really profit maximisation. Therefore, to divest assets to economic agents through the process of privatisation would raise economic efficiency.

#### **Introduction of Shareholding Culture :**

As a means of privatization, divestment of assets of state-owned enterprises would formalise the Russian population with holding shares as part of their wealth portfolio. Divestment would also raise the degree of monitoring of management of enterprises and ensure proper management of investible resources.

#### **Change in the Volume of Budget Revenues And Expenditure**

Under the command economy, the state owned

enterprises were continuously provided with huge amount of budgetary support and the huge loss incurred by them were compensated by the state. By doing so, the State had to meet this staggering uneconomic expenditure from the revenue receipts.

Now the sale of assets will generate additional revenues for the state. This will also help reduce the large volume of outlays on public enterprises which are technically bankrupt and have been incurring huge losses. In addition, this will lessen the ever-widening budget gap, which, in turn, will check the inflationary spiral in the economy.

#### **Enhancing Economic Stabilization**

As it promises radically to change the prevalent patterns of micro-economic behaviour of firms that exert an inflationary bias, privatisation can help with stabilizing the Russian economy in a flow sense. By soaking up money in circulation, privatization, it was aimed, could also facilitate stabilization in the stock sense.

#### **Providing Social Safety Net. etc.**

One notable aim of privatization in Russia is to obtain budget revenues which would be used for social protection of population, the implementation of ecological remedies, and the development of engineering



infrastructure of towns and regional territories. Also revenues are to be distributed to various purposes according to a predetermined modus.<sup>2</sup>

### III. SOCIAL OBJECTIVES

The social objectives of privatization includes abandoning the class struggle in an effort to reach a better-integrated society. Other social objectives are : coming to terms with co-determination of claims and maintaining coherence at the farm level.

It is held that being adhered to the doctrine of the class struggle, the former Russian society led to polarization (intelligentia versus workers, workers versus peasants, those in the nomenklatura versus the vast majority of the Russian people). Now, removing the repercussions of this approach throughout the society would bring about democratization and stabilization of the transitional economy of Russia.

The mechanism of privatization also holds that the property rights claimed by workers and management would be co-determined. The labour will not be the only stratum that bears the burden of adjustment. Through privatization, the expectations of the workers of having say in their enterprise will also be ensured.

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2. The privatization targets to be accompanied in 1992 have been laid down in great detail for each of the 20 Republics of the Russian Federation and each of the 57 administrative districts for ten economic sectors in an Ukar (No. 341) of 29 December, 1991.

~~Moreover,~~ privatization aims at reducing the role of labour intransigence. Privatization would remould the labour rewards according to performance. By doing so, it will break down the structures that support the high wage demands on the part of the civil servants. Privatization also aims at protecting labour from the potential abuses of capital. By weakening trade unions of the traditional mould or by eliminating the life-time job security system, the state would help rearrange the social contract. This, in turn, would lead to a more corporatist approach to reaching social consensus on the questions of income distribution and wages.

**LEGAL BASES AND PROCESS OF PRIVATIZATION**

Modern markets with their far-reaching division of labour and highly complex co-ordination tasks cannot function properly in the absence of a clear legal environment and institutions for the adjudication and enforcement of legal claims. This is obvious when it comes to ensuring property rights, for example, but wider civil and commercial legal codes are required to ensure that all agents, whether firms or private individuals, have enforceable rights. The necessary areas for legislation include company, anti-monopoly, contract, bankruptcy and foreign investment laws as well as financial-sector legislation. Besides, consistency across laws needs to be ensured and any new institutions need to be set up as quick as possible.

The adoption of clear laws and safeguards for various ownership categories, changes in the behaviour of enterprises, the introduction and use of market mechanisms, instruments and infrastructures and, as a precondition for the efficient functioning of any of these, price reform are the basic elements of transition to a market system.

It was well recognised that Russia's transformation from state socialism to a market economy could not be achieved without a fundamental reshaping of the existing legal regime. Change was to be effected through legislation and, when it proved inadequate or obsolete, through executive decrees. The Summer and Autumn of 1990 witnessed a number of legal and institutional changes in the status and internal operation of the Soviet enterprise designed to facilitate its adaptation to the market. A new law, "On Enterprises in the USSR", promulgated in June 1990, replaced the old State Enterprise law of 1987, and effectively did away with the limited experiments in enterprise self-management embodied in the Councils of Labour Collectives (STK) and the competitive election of enterprise managers. Besides, in October 1990 the Soviet government repealed its 1986 wage reform. In December 1990 there was a new law on investment. Several other laws and decrees on the question of privatization have been passed in successive years to make the process of privatization most effective.

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## The Evolution of Enterprise Self-financing

The 1986 wage reform<sup>1</sup> and the 1987 State Enterprise Law defined two methods by which enterprises could apply profit-and-loss accounting or "Khozraschet". On the first model, enterprises would be guaranteed basic funds for investment and wages, but bonuses and additional funds for social development (housing or childcare, for example) would have to be financed out of profits. Eventually, all enterprises would have to finance all expenditures out of revenues, including wages, replacement of fixed capital and net investment.

However, the introduction of such market criteria - in particular enterprise self-financing and the need for enterprises to earn their revenues through production and sales - has led to significant distortions in production and distribution, which in many ways have made the economy less viable than it was under the old bureaucratic command system. Ultimately, the emphasis on the state order is being reduced.

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1. The 1986 wage reform was imposed by a Decree of the Central Committee of the CPSU, the USSR Council of Ministers and the All-Union Central Council of Trade Unions (VTs SPs), 17 September 1986. It was repealed by a law, approved by the USSR Supreme Soviet, 19 October 1990.

Moreover, within this scheme, in 1986-87, enterprises began putting sub-units, ranging from shops down to individual bridges, on to self-financing arrangements. This was done primarily through the contract system (podryad), where work collectives contracted to fulfill specific production targets and would receive enhanced bonuses if all quantity and quality criteria were met. But unlike later leasing arrangements, these collectives on contract work did not manage their own wage funds or budgets. While the collectives had specific obligations to management, the latter did not have binding responsibilities to the contract brigades. The most serious impediment was the irregularity of supplies, which made it difficult for the management to guarantee collectives the materials they required to meet their contracts.

The contract system also aroused considerable hostility among both management and workers. The former was hostile because they did not always want to take on the extra work involved; the latter, because contract work involved a greater intensity of labour, which many workers were unwilling to accept. As a consequence, in early 1988 less than 5% of all brigades in industry were on contract arrangements.

Due to the limitations inherent in contract work, the regime began to place increasing emphasis on leasing arrangements ('arenda'). Under the leasing schemes, enterprise sub-divisions, or even entire enterprises

contract out of their parent organization (the enterprise or production association). They undertook to provide the parent body with a specified volume of goods or services, and are free to sell all output over and above this amount wherever they can find customers. They also controlled their own wage funds.

However, the experience of leasing has not been an unqualified success. The leasing collectives have found themselves confronted with the same problems as the old contract brigades. When collectives fail to meet their contracts they suffered heavy penalties, but management faced no sanctions for failure to provide equipment, supplies or raw materials. Besides, the contracts themselves were often poorly drawn up, or bureaucratically imposed by the top management. Also, leasing units have equally found themselves facing a number of financial difficulties.<sup>2</sup>

Finally, as the advance to the market progressed, some enterprises have been turned into joint stock companies, selling shares to their employees, other enterprises, or superior ministries. The showpiece of

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2. Izvestiya, 29 January, 1990

the joint stock companies to date has been the Kama River Motor Vehicle Factory (Kam AZ) in the Urals, a huge combine employing 140,000 people, which was turned into a joint stock company by a decision of the USSR Council of Ministers in June 1990.

From the above analysis, it is evident that the transformation of state enterprises and production associations into private companies is clearly the government's chosen path to full marketisation.

### **Basic Laws On Property And Land Rights :**

During the course of 1990 and early 1991, basic laws on property and land rights were adopted. The Law on property defines several forms of ownership right, which can be vested in individuals, collectives (leasing enterprises, enterprises sold to their workers, cooperatives, joint stock companies, joint associations of different types of enterprises engaged in economic activity and religious bodies) or the state (including republican and local governments). The Law makes no provision for the sale of productive assets other than the compensation of participants in a collective enterprise for their share of the property in the event of their withdrawal.



The provisions of the Law on property refer only to ownership of equipment, buildings and stocks of goods ( including farm animals )- not of land. This reflects the provisions of the Law on land. All land belongs to the state (the people); even collective farmers have no individual title to the land they work. Land use rights may be allocated to any individual or collective.

The "Basic Legislation on Land (28 February, 1990) and the "Law on Property " (6 March, 1990) were the two laws set out, for the first time since the 1920s, a legal framework for private ownership, guarantees of rights, protection against interference by the State and procedures for settling disputes. There had already been a sharp rise in employment in private enterprises which were set up following the adoption of the Law on Cooperatives on 8 June 1988. Over 7 million workers- over 5 percent of the labour force- were employed in co-operatives (other than collective farms but including the cultivation of private plots)<sup>3</sup>

### **The Law on Enterprises**

In terms of the practical agenda of enterprise

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3. Report of USSR Goskomstat, Ekonomika i zhizn. No.5, January 1991.

reform, the main legal instrument is the Law on Enterprises promulgated by the USSR Supreme Soviet on 12 June, 1990 to come into force on 1 January 1991. In comparison with the past, this law provides considerable potential for enterprise independence from interference by the State in its day-to-day operations, lays down the right to and conditions for private ownership, provides remedies against local authorities which refuse registration without good reason and specifies the principles for purchase of inputs and disposal of products by means of contracts with other enterprises without discrimination between private and state-owned firms. It also makes provision for raising finance from private sources, bank credits or the issuance of shares to the public. However, a considerable number of articles in the Law could be used to constrain the purely commercial activity of an enterprise and the regulatory role of the market-in particular, the stress placed on participation by representatives of the working collective in managerial question and a certain ambivalence with regard to the "main task" of the enterprise, which is apparently only secondarily to make profits.

The "main task" of the enterprise is stated to be "to satisfy public needs for its products, work and services, and, with the profit received, to satisfy the economic and social interests of the members of the work collective and the interests of the owner of the enterprise's property." (Article 1). Elsewhere it is

stated that "the administration of the enterprise.....shall be carried out on the basis of a combination of the principles of self-management of the work collective and the rights of the owner to economic use of its property." Profit itself is considered only as "the main generalising indicator of the financial results of economic activities" (Article 21.1) Moreover, although profit is said to be "completely at its (the enterprise's) disposal" the state may influence "the selection of uses for net profits..... through taxes, tax breaks and also economic sanctions" (Article 21.2)<sup>4</sup>

Article 14.1 of the above law states that "the owner shall exercise his rights to manage the enterprise directly or through a body authorized by him. The owner or his authorized body may delegate their rights to an enterprise council (board) or other body envisioned by the charter which represents the interests of the owner and the work collective".

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4. Economic Commission For Europe, Economic Survey of Europe, 1990-91, Box 4.6.2, p.179.

The Law also specifies that enterprises must sell their products at prices "established independently or on a contractual basis, and in cases envisaged by legislation of the USSR and union and autonomous republics, at state prices" (article 26.1). State regulation of prices is also envisaged in case of monopoly. There is also provision for "inspections and reviews, which should contribute to the effectiveness of management(article 35.3)<sup>5</sup>.

### **Principle of Leasing Legislation**

Article 7 of the 1989 Principle of Leasing Legislation of USSR gave the right to the managers and other employees in any unit ( for example, plant or workshop ) of an enterprise to lease its assets. The idea was that the leased assets would ultimately be bought by the collectives at once or by instalments after the lease period. Leasing was seen as an important prelude to privatisation in a sense that it was the main route to management buy-outs or auctions, by which the assets were controlled and owned by the managers or citizens. Leasing proved quite attractive and by the beginning of 1991 there were approximately

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5. Ibid. p. 179.

2,400 leased enterprises in the former USSR.<sup>6</sup>

**Bill on Privatization of State-run and Municipal-run Enterprises:**

In 1991 a bill on the privatisation of the state-run and municipal-run enterprises in the USSR was issued. Under this legislation, the employees of a state-run enterprise had the first priority for ownership over shares and assets upon privatisation. If no buyers were forthcoming from within the enterprise, the Soviet citizens were given priority over the overseas bidders of shares. However, the employees could not prevent the privatisation from taking place.

**Modification of the Existing Privatisation Laws:**

Soon after the disintegration of the USSR, the existing Laws on Privatisation were modified in June 1992, which established guidelines and procedures for privatising state and municipal enterprises throughout Russia.

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6. Igor Filatotchev, Trevor Buck and Mike Wright, Privatisation and Buy-outs in the USSR, Soviet Studies, Vol. 44, No.2, 1992, pp. 265-282.

Small enterprises seemed to have had the major influence on the emergence and functioning of a market infrastructure. Small enterprises were defined as those with less than 200 employees and a book value of less than one million roubles of fixed capital. It was estimated that there were around 150 to 200 thousand of these small enterprises in Russia.<sup>7</sup>

All the state enterprises employinmg upto 200 persons and with the property ( the residual cost of which is assessed on the basis of the first quarter of 1992) less than one million roubles one sold off either on a competative basis or through auctions. Enterprises employing more than 1,000 persons and with a property of more than 50 million roubles are privatised by transferring them into joint stock companies.<sup>8</sup>

#### Voucher-based Privatisation System:

With their "shock therapy" in 1992, the Gaidar Yelstin team turned their attention towards privatisation of large and medium state enterprises.

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7. V.V. Borodachev, Privatization in Russia : The Nizhny Novgorod Phenomenon, Economic Reform Today, Spring 1993, p.24.
  8. Grigory Shagalov, Russia on the way to Market Economy, in Transition Economics of the East, 1993, p.67.

In June 1992 another Privatisation Law was passed. The programme envisaged a form of mass privatisation of medium-sized and large enterprises which were to be converted into open joint-stock companies. These enterprises were to be sold primarily at auctions in competitive tenders to the highest or most qualified bidder. They were to use "vouchers" issued for this purpose—"voucher" system of mass privatisation, similar in many ways to the voucher model introduced earlier in Czechoslovakia.

The Privatisation Law of June, 1992 offered the medium and large scale enterprises two privatisation options :-

In the first option, enterprise workers were granted 25 p.c. of the enterprise shares free of charge but unlike the other shares they did not carry voting rights. The workers could also purchase another 10 p.c. (managers 8 p.c. ) of the shares at concessionary rates and the remaining 60 percent of the shares were to be made available to external purchases including citizens. The basic objective, however, was that this would enable the government to create investment funds in the country.

In the second option, managers and workers together were allowed to buy upto 51 p.c. of the (voting) shares of an enterprise but they are allowed to do so with substantially smaller price concessions and without access to credit from the Central Bank. The

selection of the second option required a favourable vote by two thirds of the workers (or their representatives ) failing which the first option was to be adopted.

In addition, in October 1992, the Russian government finally implemented the important decision of issuing the privatization vouchers with a face value of 10,000 roubles to every Russian citizen to speed up privatization programme.

By mid-December, more than 30,000 facilities in Russia that were subject to "small-scale privatisation" had been transferred to collective or private ownership. The process of conversion to joint-stock companies was being completed at approximately 5,000 large and medium-sized industrial enterprises. At almost 2,000 other enterprises that were not even stated to be privatised under the present state program, the employees had begun preparations for conversion to joint-stock companies on their own initiative.<sup>9</sup>

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9. Izvestia, Dec. 18, 1992, p.2



With regard to strengthening the position of the voucher, an important role was to be played by the recently adopted documents and the new guidelines and formats for working with the "checks" that were slated to be included in the State Privatisation Program for 1993. The first voucher-based auctions and calculations by specialists have shown that there might not be enough checks at enterprises with a high level of fixed assets per worker in cases where privatisation takes place through a closed subscription to one's share of stock. Therefore, by an order of the State Property Committee, enterprises have now been given permission to buy vouchers using money from privatisation funds credited to the personal accounts of workers in the collective, and to use those vouchers exclusively to purchase facilities subject to privatisation.

Moreover, the 1993 State Program intended to make voucher-based auctions the main means of privatisation : Shares in even the largest enterprises was to be sold exclusively for checks. It was easy to see how high this would raise the prestige of the voucher, the activeness and authority of investment funds, and interest in checks on the part of exchanges and other commercial structures.<sup>10</sup>

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10. Izvestia, Dec.10, p.2

President's Decree "On State Guarantees of Citizen's Right to Participate in Privatisation" :

The President's decree, signed May 8, 1993, "On State Guarantees of Citizen's Right to Participate in Privatization" protects Russian citizens' rights to acquire state and municipal property and stock in enterprises in exchange for privatisation checks. It establishes that from now on, 29% of the stock of all enterprises and the amount of their capital stock are to be determined without considering the revaluation of their fixed assets that was conducted in accordance with the Russian government's resolution of Aug. 14, 1992. At the same time, the members of labour collectives that are converting their enterprises into joint-stock companies would still retain all the privileges established by law. Above all, these and certain other measures called for by the decree guarantee that Russian citizens will be able to use their vouchers - to exchange them for shares in the enterprise of their choice.

Decree "On Additional Measures to Protect the Right of Russia's Citizens to Participate in Privatization" :

The above decree almost entirely restores the whole system of measures set forth in the earlier decree, No.640, that was suspended by parliament, which, purely on the basis of technicalities, sent it to the

Constitutional Court for an examination of its constitutionality. The same deadlines for selling shares, the stipulation that 29% of stock must be offered for sale at voucher-based auctions, the same program of support for check-based privatization, strict timetables for conversion of enterprises to joint-stock companies, etc., have all been reaffirmed.<sup>11</sup> The President thereby rendered meaningless the Supreme Soviet resolution that had suspended his decree "On State Guarantees of the Right of Russia's Citizens to Participate in Privatization".

The key clauses of the Russian Federation President's July 26, 1993 decree were taken straight from the May 8 decree. Briefly, Boris Yelstin has "augmented" his edict with details intended to accelerate privatisation. Reaffirming the requirement that at least 29% of shares must be put up for sale at voucher-based auctions, the President has simultaneously reduced by a month the period between the completion of an enterprise's conversion to a joint-stock company and the beginning of the auction.

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11. Sevodnya, July 30, 1993, p.2 .

Besides, the July 26 decree sets forth new, strict requirements for the implementation of the privatization program. For example, it more clearly establishes that check investment funds are prohibited from using the vouchers they have collected from the public for anything other than purchasing stock in enterprises undergoing privatisation. The decree also includes a fundamentally new provision that could greatly enhance the voucher's role- payment must be made in vouchers for not less than 80% of the shares being offered or of the total value of the facility that is being privatised.<sup>12</sup>

**President's approval of Oleg Lobov's Proposals:**

With his order of Aug. 30, 1993, the President approved the proposals made by Oleg Lobov, first Deputy Prime Minister of the Russian Government, and supported by Moscow Mayor Yury Luzhkov. The radical changes in the privatisation program as prescribed by the Lobov-Luzhkov plan made their appearance in late August of Yeltsin's order indexing the value of privatisation checks and adjusting the book value of fixed assets.<sup>13</sup>

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12. Nezavisimaya gazeta, July 29, 1993, p.2

13. Izvestia, Sept. 14, 1993, pp.1-2

Oleg Lobov's privatisation concept has the following features :-

\* Adjust the book value of the fixed assets of enterprises slated for privatisation, multiplying it by a factor of 100 to 150.

\* Adjust the value of privatisation checks (vouchers by a factor of 25

\* Reduce the share of state and municipal property that is transferred free of charge in exchange for privatisation checks from 80% to 30%

\* Privatisise approximately 70% of state and municipal property for money that would then go partly into investments in those enterprises and partly into the state budget ( which would reduce the budget deficit)

#### Privatisation-Check Auction :

The public's doubts and skepticism about privatisation by means of vouchers stemmed mainly from the fact that people had never received anything from the state for free. In order to overcome this situation, it was thought that transferring the bulk of the property free of charge, so that not only labour collectives but the whole population receives its shares, would have been impossible without checks. Of course, the State Property Committee also did an

adequate job of organising efforts to explain the privatisation checks.

A person was to receive his check together with an explanation of where and how he could invest it in the most profitable manner. He must unquestionably have a list of enterprises that are being sold. He has to know the procedures for auctions and the order in which they will be held, to have a sort of time-table of privatisation. Moreover, with the publication of that information in the major newspapers and broadcast on the radio and television, it will change people's attitude towards privatization immediately and drastically.

Moscow's first privatisation-check auction has opened in the exhibit hall of the Expo Centre on Krasnaya Presnya Embankment : Application to purchase shares in the Bolshevik confectionary factory began to be submitted there on Dec. 9, 1992. In the first type of application, the check-holder had to indicate only the amount of checks with which he intended to buy shares, and all of them were to be accepted on a mandatory basis. In the second type of application, the check holder indicates the maximum price that he is willing to pay for a share. But, of course, no matter what the case, the shares were to be sold to absolutely everyone at an identical price.<sup>14</sup>

By the end of 1992, some 40,000 enterprises - approximately 17%-18% of the total number in Russia - have been privatised. More than 5,000 major industrial enterprises were being converted to joint-stock companies, and when the period for closed subscriptions was over, 17 million of their employees were stockholders.

The second wave of privatisation, involving medium-sized enterprises with capital stock of upto 50 million rubbles, had also begun by 1992. They form the majority of Russian industry, numbering in tens of thousands. Thus, the system of voucher-based auctions or "popular privatisation" was being developed.

**An Alternative Law on Privatization : A "Fourth Benefit Option" :**

The privatisation program for 1993 made several proposals including an alternative Law on Privatisation, a "fourth benefit option" (for the employees of enterprises being privatised) and the idea of giving

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14. Izvestiya, Dec.9, 1992, pp. 1-2.

priority to labour collectives and transferring the assets to their possession and control (but not legal ownership)

The main idea underlying the so-called "fourth option" for converting state enterprises into joint-stock companies was vividly explained by Anatoly Chubais, the Deputy Prime Minister and Chairman of the State Property Committee. The idea is that enterprises would be bought out at their residual value (which is some 93%-95% lower than the current market price), without the use of vouchers, using money paid out of current profits in installments over five years.<sup>15</sup> He included in this category pensioners, disabled people, students, doctors, teachers, in general everyone paid from the state budget including police officers, state security personnel and people in the military.

In Chubais's opinion, "the main goal of the drafters of the fourth option, who under the cover of economic pseudoscience intend to torpedo the process of privatization," is to destabilize the social and political situation in the country. Of course, implementation of the "fourth option" would mercilessly

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15. Nezevisimaya gazeta, Feb. 18, 1993, p.1



rob officers, who are somewhat cut off from mass voucherization even now, the privatization minister emphasised.<sup>16</sup> Besides, a Large Group of Russian Cultural Figures in a letter to the President, the People's Deputies and the Government, claimed that the "fourth option" for privatisation infringes on the rights of the majority of Russia's citizens. The group suggested for the establishment of compensatory privileges in the privatisation process for all those who are not employed in material production, by expanding their rights a voucher-based auctions.

**State Privatisation Programme for 1993 :**

On Dec. 17, the Presidium of the Council of Ministers approved, on the whole, the program for privatising Russia's state and municipal enterprises. State Property Committee Chairman, Anatoly Chubais, who spoke at the session, said that "the halfway point in privatisation has now been passed". He cited the following data : 65.5% of all small enterprises subject to privatisation have been converted into joint-stock companies, with 55 million of the country's citizens holding stock in them. The general public, after

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16. ibid, p.1

receiving 160 million vouchers, has used 115 million of them in various ways, entrusting a sizable portion of them to 600 voucher investment funds.<sup>17</sup>

Moreover, vouchers and voucher-based auctions were the main instruments of privatisation in 1993. The Law on Privatisation Checks and the State program were presented to the Supreme Soviet for discussion at the same time; the key goal of the latter was the broad implementation of "popular privatisation", the sale of shares for vouchers at voucher-based auctions. Several new sections of the program were devoted to the mechanism of privatisation without payment based on the use of vouchers, the organisation of voucher-based auctions, the development of a stock market, procedures for using foreign investments at voucher-based auctions, etc.

#### **First Nation-wide Voucher-based Auction :**

The sale of stock in the Moscow I.A. Likhachov Plant Joint-Stock Company began on March 15 at the Exhibition Complex on the Krasnaya Presnaya Embarkment, where the capital's inter-regional auction is located.

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17. Sevodnya, Dec.21, 1992, p.3

There and in eight other Russian provinces and seven Russian cities, the Federal and Moscow Property Funds and the Moscow Likhachov Joint-stock Company were putting up more than a million 1,000-ruble shares to be sold for privatisation checks.

The auction was held from March 15 through April 20 in Vladimir, Sverdlovsk, Leningrad, Novosibirsk, Omsk, Perm and Smolensk Provinces, Krasnodar Territory, and the cities of Izhevsk, Maikop, Moscow, Orel, Penza, Ryazan and Chelyabinsk. The auction marked a new stage of the process, as it was the start of truly large-scale popular privatisation.

#### **The Association of Private Enterprises And Enterprises Undergoing Privatisation :**

This organisation's main goals are to protect the interests and rights of private owners, to improve the State Privatisation Program and to promote processes of interaction between Russia's private sector, on the one hand, and economic structures, enterprises and organisations in the CIS States and other countries, on the other.

The founding congress of the Association was held on April 2 and 3 in Moscow. By the opening day of the founding congress, 60,000 small enterprises in Russia had been privatised, and 5,000 large enterprises were being turned into joint-stock companies, including the

famous Magnitogorsk Metallurgical Combine, as well as plants and factories in Moscow, Volgograd, Yekaterinburg, Omsk and other cities.

### Voucher-based Auctions in 1993

In industry, the main instrument for privatisation in 1993 had been voucher-based auctions. Such auctions were being held in 72 regions covering almost all of the country. The "blank spots" were in the republics of the Northern Caucasus, Tatarstan, Bashkortostan, and Arkhangelsk, Lipetsk and Tula Provinces.

Russia currently has 17 privatisation centres that are organizing nation-wide auctions. By May 15, 1993, the property of the Moscow Likhachov Automotive Plant was sold at the first one; the results of the second, at which shares in the Urals Heavy Machinery Plant and the Urals Pipe Plant were sold, were being summed up; and the third had begun.<sup>18</sup> Such nationwide auctions were held continuously.

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18. Izvestia, May 25, 1993, p.1

The increase in the number of enterprises that have been transferred from state to private ownership indicates that the conveyor belt of voucher-based auctions is steadily picking up speed. Whereas in December 1992, there were fewer than 20 of them and in January 1993, there were just over 100, in February there were 200, in March 400, and in April-584 enterprises.

Residents of the capital are now able to invest their checks with the greatest benefit for themselves through investment funds that are being created in the city. The bulk of the state share of stocks in Moscow's Likhachov Automatic Plant, Lenin Komsotmol Automotive Plant and several other major enterprises were sold to the general public specifically for vouchers. Such prestigious facilities as TsVM (Central Department Store) and GVM (State Department Store), the network of hotels and restaurants, etc, were also stated to be sold at auctions, mainly for privatisation checks.

Besides, a special sub-division is being set up in the capital's property Fund to handle the disposal of plots of land on which to build production facilities. The program also specifies that the main emphasise will be on selling the right to take out a long-term lease.

An analysis of practical legal support for privatisation programme shows that amendments and additions to the existing normative acts, instructions, and rules of ministries and departments so as to bring them into line with the basic objectives of privatisation in Russia. The laws and government decrees drafted so far are not always well coordinated with one another, which results in serious shortcomings when the adopted decisions are implemented.

However, the development of a mechanism for creating the legal environment necessary for the successful implementation of privatisation programme was essential. This presupposes continuous improvement of the legislative and normative base on a unified conceptual foundation that excludes contradictory decisions and presupposes a certain consistency in their formulation.

PROGRESS IN PRIVATISATION

One of the more striking paradoxes of the Russian reform process is that its most emblematic phenomenon, the privatization of production and distribution enterprises, has surged ahead in a persistently anomalous context, characterised by high inflation, declining levels of output, taxes and exports, fiscal imbalances, great foreign indebtedness and a massive flight of capital. Even though all this threatened to kill privatization dead on its feet, it has, nonetheless, advanced because of its pivotal significance in the gamut of macro-economic stabilization measures attempted since January 1992.

Among the priority problems in the sphere of institutional transformations is the privatization of state and municipal property, conversion of enterprises into joint-stock ownership, and the transfer into private ownership of a number of means of production. However, the transformation of forms of ownership and the formation of a competitive environment is accelerating, albeit slowly. By the beginning of October, 1993, over 24,000 enterprises in various sectors

of national economy were converted to private ownership<sup>1</sup>. This is 1.5 - fold more than during last year's corresponding period. Of the 24,000 enterprises, more than 60 per cent are municipal property; 22 per cent - the property of the republics within Russia; and approximately 16 per cent - federal property installations.<sup>2</sup>

Regarding the progress of privatization, the Chairman, the Russian Federal Property Fund, F. Tabeyev, in a press conference, quipped, "A new stage has now begun in privatization. Its tempos have grown and it is being conducted in a more organized and purposeful manner. We consider the fact that we have managed to reach an agreement on all aspects of privatization with the republics and other regional formations to be one of the important circumstances<sup>3</sup>."

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1. Data taken from Foreign Broadcast Information Service Report: Central Eurasia, 10 March 1993.
  2. EKONOMIKA I ZHIZN, No. 35, August 93, p.14.
  3. ibid, No.35, August 93, p.14



## Privatization and the Volume of Industrial Production.

In the first quarter of 1993, Russian industry produced Rs. 12.2 trillion worth of goods at existing prices.

As compared with the corresponding period last year, the index of the physical volume of industrial output in the 1st quarter constituted 80.7 per cent, including 78.2 per cent in March<sup>4</sup>. The intensification of the production slump was therefore halted in the 1st quarter of 1993. Its overall volume virtually remained at the level of the 4th quarter of last year, and, considering the elimination of the differences in the regulation fund of work time and seasonal fluctuations, exceeded it by approximately 2 per cent.

As a result of the slump, which began in 1990, the country rolled back many years with respect to the output of many years with respect to the output of many very important types of products. For example, in the

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4. These data are taken from the table depicting data on the dynamics of Industrial production by quarters of 1992 and 1993, given in FBIS-USR-93-103, 11 August, 1993, p.22.

1st quarter of 1993, the average daily production of metal-cutting machine tools, forging and pressing machines and freight cars virtually corresponded to the level of the 1950's; of coal, tractors and whole-milk products - the 1960's; of petroleum rolled ferrous metals, steel pipes, mineral fertilizers, chemical fibres and filaments and hosiery items - the 1970's; and of meat and animal oil - the beginning of the 1980's.

The production slump in the first quarter of 1993, as compared with the corresponding period of the preceding year, is characteristic of all sectors, but its scale varies. While in the fuel-raw material sectors, the output of goods was reduced by 14 per cent, in the processing sectors it fell by 20 per cent, including by 26 per cent in the light and food industries.

The production of goods was cut back in larger amounts than as a whole for Russian industry, as compared with the corresponding period last year (1992) in every second region in the country. In every fourth region the production recession constituted 25 percent or more.

However, the reduction in industrial production in many ways stems from the breakdown in economic ties. According to the data of a random survey at 9,200

enterprises, conducted by Russia's Goskomstat according to the condition on 22 March 1993, 62.7 per cent of the year's production program outlined by the enterprises was formalized by contracts to supply products to the consumers, but only 49.8 percent to obtain raw materials, materials and completing items (on 22 February 1993, 57.1 per cent and 43.3 per cent respectively).

In fact, the high level of industry monopolisation in Russia has an adverse effect on production development. Russia's Goskomstat correlated report data for January 1993 on 467 industrial monopoly enterprises on the republic level.

The greatest degree of production monopoly is in the enterprises of the light industry: eight enterprises (0.3 per cent of the enterprises in the sector) produce 39 percent of all enterprises in the second products.

The level of profitability was higher at the monopoly enterprises surveyed than on the average for corresponding sectors, and this is in many ways the result of utilizing the monopoly situation when prices are established for its products.

In the 1st quarter of 1993, the Russian Federation Committee for Price Policy made a check of 111 monopoly

enterprises. The check established that 72 enterprises violated price-setting. Sanctions were applied against 40 enterprises. At the same time, Rs. 182.2 million was confiscated for the budget income. Ten enterprises exceeded the established profitability level, which led to the confiscation of Rs.80 million.

In 1992, the extraction of coal dropped by 16 million tonnes, or by 5 percent, as against 1991. This was due to the recession in the coal industry.

In ferrous metallurgy, steel production in 1992 was cut back by 10 million tonnes, or by 13 percent, as compared with 1991.

In the first quarter of 1993, the steel output was reduced by 10 percent with the corresponding period last year, the output of finished rolled metal- by 8 percent and of steel pipe-by 15 per cent. At the same time, the production of rolled metal with thermal hardening treatment was reduced by one-third, of assorted cold-drawn steel and roll-formed steel section by almost one-half, and of rolled-metal made of stainless steel - by a factor of three. The daily output of the basic types of goods in metallurgical production in the 1st quarter of this year lagged 1-2 per cent behind the level of the 4th quarter of 1992 and in pipe production- 11 per cent behind.<sup>5</sup>

In machine-building industries, the trend towards a reduction in the production of basic types of goods is long-term in nature. On average for the year in 1986-1990, the output of metal-cutting machine tools dropped by 5 per cent, and in 1991-92 their production was reduced by 18 per cent. The Novocherkassk Machine Tool Plant (Rostov Oblast), Dmitriyevka Milling Machine Plant (Moscow Oblast) and Samara Machine-Tool Building Association did not produce a single digitally controlled machine tool in March. The output of these machine tools was considerably reduced at the Moscow Krasnyy Proletary Association. By August 1993, the production of forging and pressing machines dropped by over half, of casting machines-by 43 per cent and of woodworking machine tools by over one-third.

The locomotive and rail car building industries also suffered reduction in production. In the 1st quarter of this year, the Kolomenskiy Zavod Production Association, the only manufacturer of mainline diesel locomotives in Russia, reduced production of these machines by one-third, while a considerable number of locomotives in the diesel locomotive fleet are being

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5. ibid, No.35, 11 August 1993, p.24.

operated with an engine life that has already been worked out. The Ural-Vagonzavod Production Association, which produces about two-thirds of all the railcars, has not reached last year's level with respect to production of mainline freight cars (70 per cent), and this has entailed a reduction in the output for Russia as a whole.

Crisis phenomena are gripping the enterprises of the chemical and petrochemical industry to an increasingly great extent as their stable work depends on supplies of imported raw material.

In January-March of 1993, as compared with the first quarter of last year, the output of a number of the most important raw material products was reduced: synthetic ammonia, sulfuric acid, caustic soda (by 8-24 per cent). The drop in production of high efficiency types of products: polyethylene (by 4 percent), poly-propylene (by 3 per cent), polystyrol (by 13 per cent) and poly vinyl chloride (by 27 percent), led to the breakdown in the work of the subcontracting production facilities and above all caused a reduction by one-half in the output of pipes and pipeline parts made from thermoplastics, and a reduction by one-third in polyvinyl chloride plastics.

The industry of the Russian Federation produced 3.9 trillion<sup>6</sup> worth of ruble in January-March 1993, which is 12 percent below the same period last year. In the light industry, under the conditions of a certain improvement in raw material provision for the textile enterprises, the daily output of yarn, woolen, silk, linen and hemp-jute fabrics rose in the 1st quarter of last year. At the same time, the production of hosiery and knitwear items, footwear and a number of readymade items was reduced.

**Privatization and the volume of Investment in Industries :**

According to the surveys of Russian industrial enterprises' business activity which are conducted regularly by the Economic Conditions Centre attached to the Russian Federation Council of Ministers show that the volume of investment in industries has been increased in the first half of 1993. The survey show that the situation is better in ferrous metallurgy (26 per cent), the fuel industry (31 per cent), and the milling and grinding and mixed feed industry and non-ferrous metallurgy (33% each)<sup>7</sup>.

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6. Source of the above data : Goskomimushchestvo.

At the same time, 46 percent of enterprises in the chemical industry and 40 percent of enterprises in machine building and metal working reported to a decline in investments for the enterprises as a whole, where this indicator's average for the industry was 27 per cent.

A similar situation applies to investment in equipment. Most non-ferrous metallurgy enterprises (37 per cent) and enterprises in milling and grinding and mixed feed industry (33 percent) reported an increase in investment in the first half of 1993.

According to the surveys, managers in the fuel and chemical industry (42 per cent each) and machine building and metal working (44 per cent) reported more of a decrease in capital investments in equipment than in industry as a whole (28 per cent). However managers of non-state enterprises, in particular 23 percent of the

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7. The surveys of Russian industrial enterprises' business activity which are conducted regularly by the Economic Conditions Centre attached to the Russian Federation Council of Ministers.



closed-type joint-stock companies, reported more of an increase in investments in the enterprise as a whole, where as 21 per cent reported more of an increase in investments in equipment, than the average for the sampling (taken in the survey); these figures were 21 per cent and 20 per cent, respectively, for limited partnerships.

The trend of less investment in their production predominatis in large enterprises (35 per cent of enterprises with 1,001 to 5,000 employees and 44 percent of enterprises with more than 5,000 employes).

By the end of 1993, more than one-fourth of all the enterprises polled believe the volume of investments will remain at the same level as in the first half of 1993.

The survey results show that the trend toward reduced stocks of raw material and materials is typical for most of the enterprises.

At the end of 1992, 26 percent of the enterprises reported an increase in their stocks, while 18 percent of the enterprises responding reported this in the first half of 1993. The largest reduction of stocks of raw material and materials are reported by managers of enterprises in the light industry (66 percent), ferrous metallurgy (66 percent), and machine building and

metalworking (64 percent)<sup>8</sup>. The actual estimates of a reduction in raw material stocks are almost twice the figures forecast in machinebuilding, the building materials industry, light industry, and ferrous metallurgy.<sup>9</sup>

In the first half of 1993, 36 percent of the enterprises surveyed reported a decrease in their stocks of finished products. In the second half of the year, 44 percent of the enterprise managers intend to maintain their stocks at the level of the first 6 months, and 32 percent plan to reduce them.

#### **The Financing Structure of Industrial Enterprises**

According to the survey, industrial enterprises' own funds continue to be the basic source of financing. The use of budgetary funds, which predominated before, is being cut back. And the proportion of credit and loans being used by enterprises is increasing.

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8. ibid.

9. DELOVOY MIR, 8-14 Nov. 1993, p.11

In particular, in the first half of 1993, 42 percent of the respondents reported a decrease in their own funds, and two-thirds of the enterprise managers do not plan to increase them in the second half of the year. More than 70 percent of the enterprises surveyed had no budgetary financing in the first half of 1993 and do not plan to use it by the end of the year. Some 39 percent of the industrial enterprises surveyed made more active use of credit and loans, and about half of those polled are not planning to reduce the volume of financing with funds that have been attracted by the end of the year.

In analysing the situation by sector, it must be noted that 75 per cent of enterprises in non-ferrous metallurgy, 65 percent of those in ferrous metallurgy, and over 60 percent of enterprises in the food industry and the building materials industry have not cut back the use of their own funds for production development. Six out of 10 enterprises in the chemical industry, 55 percent of those in light industry have begun to use less of their own funds while increasing the proportion of credit resources as sources for their financing.<sup>10</sup> However, an analysis of the situation at enterprises

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10. ibid, 8-14 Nov. 1993, p. 11.

with a different level of production concentration shows that at large enterprises (those with over 1,000 employees)<sup>11</sup>, the extent to which they are using their own funds has decreased significantly, while the use of credit and loans has increased.

### Privatisation and Prices of Industrial Products.

In fact all the participants in the survey mentioned the rise in prices to obtain raw material and materials for their enterprises over the last 6 months, and 98 percent expect them to increase before the end of 1993.

However, the higher prices for raw material and materials have been determined to a large extent by their further increase throughout the entire technological chain of industrial production. Practically, none of the respondents reported a reduction in price for their enterprise's output over the past 6 months. On the contrary, 96 percent of them noted an increase in price.

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11. ibid, 8-14 Nov. 1993, pp. 11-14.

Managers of fuel industry enterprises reported more often that the previous price level for their output was maintained in the first half of the year. A price rise at all the enterprises surveyed was noted in the non-ferrous metallurgy, the milling and grinding, and the printing sectors. All the enterprises in the fuel industry and ferrous metallurgy intended to raise their prices for output before the end of 1993.

Be as it may, substantial differences are not being observed in the price dynamics at enterprises with different forms of ownership. With an overall rise in prices for output, 4 percent of the limited partnerships maintained the previous prices for their commodities in the first half of 1993. The managers of enterprises with all forms of ownership differ little in their predictions of price movement before the end of 1993. Closed-type joint-stock companies intend to hold prices at the level of the first 6 month period to a greater degree.

### Industrial Enterprises and the use of Production Capacities

Various surveys of Russian industrial enterprises' business activity conducted so far show that the use of production capacities varies from enterprise to enterprise. Only 11 per cent of the managers reported that the level at which their production capacities are

being utilized at the time of the survey was over 90 per cent; 57 per cent of the respondents said that 51 to 90 percent of their capacity was being utilized; 31 per cent gave an estimate under the 50-per cent mark, and 8 percent said utilization was below 30 per cent. In another survey, the corresponding figures were 11, 67, 21 and 4 per cent, respectively.

Use of capacities above the 90-per cent level was mentioned most often by managers of fuel industry enterprises. Managers of enterprises in the ferrous metallurgy, machine-building, chemical, and timber industries mentioned this level of capacity utilization least often. At the same time, less than half of the capacities were put into use at 40 per cent of the enterprises in the chemical and milling and grinding industries and over one-third of the enterprises in the machinebuilding, food and building materials industries. As a whole, the most intensive utilization of production capacities was reported by managers of enterprises in the printing and fuel industries, while the least intensive use of capacities was cited by managers of chemical industry enterprises.

According to the survey, capacities at state and leased enterprises were put into use on a smaller scale in comparison with other forms of ownership. The best indicators of production capacity use at the time of the survey were revealed by closed-type joint-stock companies.

## Demand for Industrial Products :

Under the conditions of strict credit-monetary and budget policy, enterprises encountered restriction of overall demand for the products being turned out (reduced demand was observed at six out of 10 Russian enterprises). In fact, many industrial enterprises decreased their production volumes. Under the conditions of reduced demand and inflationary expectations, nearly 70 per cent of the enterprises increased their stocks of finished products in warehouses. Only 37 per cent of the enterprises were able to take advantage of the benefits of price liberalization and increase their own financial resources.<sup>12</sup>

In the circumstances, the industrialists began to realise that the old methods of economic operation and

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12. Report by Tatyana Kubanina and Nina Zhukova, Economic Conditions Centre attached to the Russian Federation Council of Ministers : The Business Activity of Russian Industrial Enterprises.

often candid opposition to the economic reforms would not bring any substantial advantages to production. They began changing their way of thinking by reorienting themselves to market controls. Thus, the problem of demand for their products, which did not concern enterprise managers much before, became one of their primary interests.

Various surveys show that managers in ferrous and non-ferrous metallurgy, as well as light industry predict the most stable situation in the market for their products. They did not forecast a decrease in demand.

The managers of large enterprises (1,001-5,000 employees) and the largest enterprises (over 5,000 employees) reported the lowest increase in demand for their products while the highest increase in demand was reported by the managers of medium-sized enterprises (202 to 1,000 employees).

The managers of privatised enterprises-joint stock companies and limited partnerships- reported an increase in demand less frequently. They also reported a decrease in demand less frequently. However, closed-type joint-stock companies reported the most substantial increase in demand.



## C O N C L U S I O N

Although the mechanism of privatisation is gaining momentum in Russia, the negative phenomena accompanying it are increasingly manifesting themselves. The initial objectives for which privatisation was undertaken have receded into the shadows. The goals of fostering stabilization of the financial situation, of the social protection of the population using monies from privatization, etc., are dropping out of the field of vision.

The process of privatization in industry is lagging considerably behind the schedule envisaged by the State Program, thus slowing down the formation of the class of proprietors and a competitive environment in the economy. The industrial enterprises are facing unstable financial situation and the uncertainty in industrial policy. As a consequence, commercial structures are not providing the effective demand for large-scale privatization installations and their shares. Besides, the plans for privatization still do not take the interests of private capital into account adequately, thus transforming a substantial amount of the assets held by businessmen into productive capital. Moreover, the goal of the appearance of an 'efficient owner' has not been achieved so far.

In addition, the maturing of the privatization process is also hampered by the fact that the rate at which the state-owned assets of public undertakings have been transferred to private ownership has outstripped the emergence of financial institutions that are necessary to regulate this new capital market.

It was well recognised that Russia's transformation from state socialism to a market economy could not be achieved without a fundamental reshaping of the existing legal regime. However, there is no complete legally codified set of documents for conducting check auctions. It is not clear where the money to pay for them is to be obtained, or how to deposit checks, make non-cash payments, or monitor, inventory and cancel vouchers. Nor is there any mechanism for transferring checks and shares throughout the territory of Russia.

The existing situation can be changed by creating an effective mechanism for the representation of entrepreneur's interests and expert evaluation of draft documents. In order to achieve this end, Russian economy needs economic stabilisation, control over hyper-inflationary trend, the establishment of economic institutions particularly in respect of banking and finance, proper development of a capital market. For

these are all necessary for the success of privatization in Russia. The prospects in this regard, however, depend upon the extent to which overall political and economic conditions are improved in the country.

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