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## RUSSIA'S TRANSITION TO CAPITALISM. MYTH OR REALITY?

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**Abstract:**

*There is no perfect economic system, but capitalism stood the test of time and proved to be the most efficient one from an economic, social and technological perspective. The countries which adopted a different type of system during history, discovered its limitations and started to embrace capitalistic elements. Russia is a relevant example: the communist system which was meant to bring liberty, equality and progress, generated control, terror and inefficiency. Russia's transition to liberal capitalism is a necessity but also a lasting process, for the state is not yet prepared to reduce its major influence in the economy.*

**Key words:** *communism, oligarchic capitalism, state capitalism, entrepreneurial capitalism, liberalism*

### 1. History's lessons

Almost a century ago, the first communist state emerged: The Soviet Union. Two revolutions were necessary in 1917, for the Russian monarchy to be forgotten, and the Bolshevik party, led by Vladimir Ilici Lenin to grab the power. Lenin believed that the best social system, from an economic, political and social way is the communist system. However, history proved him wrong.

Lenin tried to fulfill the communist dream of a society without classes, based on collective property of the means of production, where there is no unemployment and people are equal. In his book "State and Revolution", published for the first time in 1918, Lenin stated the importance of the revolutionary actions of the working class and the freeing of the masses from the capitalist tyranny. Inspired by Karl Marx's and Friedrich Engels' beliefs, he shared their views regarding the class struggle between the proletarians and the capitalists. The State, seen as the instrument of oppression and exploitation needed to be replaced: "it is clear that the liberation of the oppressed class is impossible not only without a violent revolution, but also without the destruction of the apparatus of state power which was created by the ruling class and which is the embodiment of this "alienation""(Lenin,5). Lenin's dream was the birth of a socialist

revolution, by which the proletariat will remove the bourgeoisie state, because only after the State's removal, the classes and the oppression will disappear. His beliefs were similar to his mentor's: "The immediate aim of the Communists is the same as that of all other proletarian parties: the formation of the proletariat into a class, the overthrowing of the bourgeois supremacy, the conquest of political power by the proletariat... the theory of the Communists may be summed up in a single sentence: abolition of private property" (Marx,22). Lenin thought that thanks to this revolution, the unfair and abusive capitalist system will be replaced by the communist system. The capitalist democracy will be firstly replaced by the proletariat's dictatorship –necessary for the transition to the communist society-, which "imposes a series of restrictions on the freedom of the oppressors, the exploiters, the capitalists" (Lenin,51). In the end, the proletariat dictatorship will vacant its place to a more complete form of democracy – democracy of the people.

Although he tried to justify his actions and personal ambitions quoting from Marx's writings, Lenin, distanced himself from his mentor's theory regarding the changing of the social order. Firstly, Marx sustained that the process of transition to socialism, should take place in the advanced capitalist societies, where the industry reaches a high degree of development, and the proletariat class is mature and in a continuing growing. These prerequisites were lacking in Russia, which in 1917 was an agrarian country, with an incipient industry and a reduced proletariat. Secondly, Marx sustained that the replacement of the capitalist system with the socialist one, will be caused by objective economic laws, resulted by the capitalist system's limitations. The Bolshevik revolution changed the social order through military and political actions. Thus, the objective economic laws have been replaced by the subjective laws of an almighty political class, that made the socialist economy register much lower performances than the capitalist economy it wanted to surpass. The effects of the revolution, were not the ones Lenin promised; the tsarist absolutism was replaced by the soviet absolutism, and the cult of personality was passed from the tsar, to Lenin and then to Stalin.

After securing power, Lenin started to nationalise the industry, inheriting many factories, railways and steelworks dating from the First World War and before. In the agricultural sector, collectivisation was very risky, because The Soviet Union was an agrarian economy, and the population in the rural area was very numerous. Thereby, in 1921 Lenin established the New Economic Policy, by which he allowed the private enterprises in the agricultural sector and the private commerce. This way, Lenin made the transition less abrupt, not giving up to a major pylon of capitalism – private property. Once Stalin came to power in 1928, it took place a major process of the agriculture collectivisation and rapid industrialisation. Even though the process of collectivisation was very difficult, on a long term the measures proved to be beneficial: the productive capacity of the industry grew. Now, what Marx, Engels and Lenin dreamed, happened – communism in its pure form was installed, but this did not bring performance: the products made by USSR were technologically inferior to the ones produced in the capitalist countries.

USSR isolated from the capitalist countries, refusing to take part in the IMF and World Bank in 1944, trying on the other hand to create other Marxist countries, and make them function according to the Moscow's rules. USA, England and France, tried to spread the free market, and held democratic elections all over the world, seriously worried about the power the Marxist parties started to gain. The Marshall plan in 1947 and the North Atlantic Treaty Organisation signed in 1949, divided Europe in two areas of influence: the capitalist and the communist one. While the communist system developed in the East side of the globe, in USA the liberal literature intensified and the voices of Milton Friedman and Friedrich Hayek crossed the Atlantic. They both raised a warning signal regarding the possible effects of the communist system: "Wherever the State undertakes to control in detail the economic activities of its citizens, wherever detailed central economic planning reigns, there ordinary citizens are in political fetters, have a low standard of living, and have little power to control their own destiny" (Friedman, 55); "It is undeniable that as far as individuals are concerned, the effect of collectivism was almost completely destructive" (Hayek, 234). What system will prove better? Each side believed that its own system will emerge victorious.

The rise of the Berlin Wall in 1961, by Nikita Khrushchev, revealed the communist tyranny, and also the fact that the soviet leadership was no match for the economic attraction of the West. Even though in the 70's the USSR tried to keep up with the USA –having a comparable level of nuclear weapons, and sending people into space- in the country, the population was humiliated and frustrated lining up in long queues for basic food. Lack of private property and of big financial rewards, inhibited innovation and progress. In a centralized system, based on planning, where free initiative is repressed, employees become less involved and motivated, and the managers are more concerned about the quantity they produce rather than the quality. The centralized planning of the communist system proved its limits in comparison to the free market of the capitalist system. In the economies where the state chooses the winners, owns the means of production, makes the prices and salaries, the consumers suffer the most. The state is not focused on their needs, the diversity of products is limited and the quality of the products is lower in comparison to the developed capitalist countries. The autocratic and bureaucratic policy, the international isolation, and also the privileges offered on political criteria, rather than on efficiency, made the USSR incapable of reaching the West's level of development.

Once Gorbachev came to power, he started to reform the communist system, using the well known words: "glasnost" and "perestroika". A change was absolutely necessary to revitalise the system, and to make it more competitive. He adopted a series of policies in order to create a greater social transparency, tried to reduce corruption and political abuse, and allowed new parties to exist. In stark contrast to his intention, these inside reforms caused the entire communist system collapse. Reality proved that communism is incompatible with freedom, liberty, and democracy. The breakdown of the economic and political soviet system, led to the collapse of all the

other centralised regimes from Eastern Europe; the fall of the Berlin Wall in 1989, marked the end of communism as a viable idea.

## **2. Transition to capitalism**

The Russian Federation, the new name the USSR was given in 1991 by president Eltin, entered in a vast process of transition, from planned economy to market economy, from communism to capitalism. The communist system proved its limits, the only possibility of progress for Russia, seemed to be the transition to capitalism. Russians were thrown into the deep pool of market economy, in order to learn faster to “swim”, but unfortunately many of them “drowned”. This kind of change was difficult because a great battle needed to be waged with people’s mentality. In a communist system the State guarantees its citizens a job, and so they have a strong feeling of stability. Once state companies were privatised, Russians had to take care of themselves and find a job.

After 1992, a massive process of privatization took place. A great percentage of the country’s productive resources came into the hands of a small number of people who started to dominate the economic and political life. This way, the communist system was replaced by an oligarchic system, “a system where the governmental policies promote the interest of a small group of people (usually very rich)” (Baumol W. J., Litan R. E., Schramm C.J, 65). In this new system, economic growth was a marginal goal, the leading class was more preoccupied to accumulate state capital, and prevent population from rebelling. Economic growth is generated by private investments and human capital’s growth, but in Russia under this system, corruption has grown, and investors were discouraged. Facing a great danger, starting in 2007, Russia began nationalising the economic sectors which had a great strategic importance. So, the oligarchic capitalism was transformed into state capitalism – a system where the state dominates the market’s activity. Forms of state capitalism are seen in many other countries: like Brazil, India, China. These countries, member of the BRIC group along with Russia, overcame the 2008 financial crises, in an unexpected manner. “Despite a large drop in real GDP in 2009 (-7.8 percent), an acute liquidity crisis, and a sharp increase in unemployment, the crisis was managed without systemic bank failures, and the economic and labour market conditions began to improve during 2009 in line with the rise in oil prices and the recovery in domestic demand and credit. (World Bank, 2011)

People believed that the trend will continue and these countries will become some of the most dominant economies by the year 2050. However, starting with 2010, the economic growth of BRIC group diminished, state capitalism proved its limits.

**Table 1: GDP growth rate 2010 – 2012:**

<b>Country/Year</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>
<b>Brazil</b>	7.5	2.7	0.9
<b>Russia</b>	4.5	4.3	3.4

<b>India</b>	10.5	6.3	3.2
<b>China</b>	10.4	9.3	7.8

Source: World Bank

A system based on state capitalism in not a dynamic and innovative one, it is a system were the winners are chosen by the state, according to political favouritism. It is a system that risks becoming highly corrupt. Although Russia seems to be aware of these limitations, and its officials declare that they want to make the transition to liberal capitalism and create an open market, it lacks a coherent economic strategy in this direction. State companies own approximately 60% of the stock market, and state banks own 50% of the entire market. The influence on the Government in key sectors is indirect but significant, a lot of big companies' CEOs, are Kremlin's men. Although it seems that the companies activate in a liberal environment, the strict control of the state contradicts this impression.

Russia came back into the world's attention thanks to its enormous natural resources: natural gas and oil. Lukoil and Gazprom expanded their activity in Europe, taking advantage of Europe's energetic dependency, and the absence of a unique energetic policy. Gazprom identified with Russia, influenced the state's external policy. An economy that depends in such a great proportion on the natural resources, can be defined as an unstable economy, because it depends on the price fluctuation. The price of the oil barrel grew constantly since 2009, from 60\$/barrel to 100\$/barrel in 2013. This situation proved to be a great advantage to Russia, but the perspectives are not as optimistic. USA's production and exportation of oil and natural gasses risk to: diminish the prices of natural gas, reduce the exports, depreciate the ruble, create inflation and finally diminish Russia's economic growth.

Russia should evolve from an economy based on resources, to an economy based on technology, and so, it must find a way to transit from state capitalism to entrepreneurial capitalism. Step by step the state's influence in the economy should diminish, and SMEs should be encouraged to raise the efficiency and the innovation the business sector. Russia should improve its legislation, its legal system, privatise the national banks in order to facilitate access to capital, develop the infrastructure, diminish corruption and bureaucracy, privatise the state's companies and last but not least, educate the population in order to develop an entrepreneurial spirit.

In the table below I have presented the main indexes that show the easiness and desire of people to start a business in Russia, Romania, European Union and United States of America in 2013. Unfortunately Russia registers one of the worse data in the charts, proving once again the negative effect of state capitalist on the entrepreneurial sector.

**Table 2: Main indexes that show the easiness and desire of people to start a business in 2013**

	Russia	Romania	European Union	USA
<b>Start-up procedures to register a business (number)</b>	7	5	5.3	6
<b>Time required to start a business (days)*</b>	15	8.5	12.9	5
<b>Ease of doing business index (1-most business-friendly regulations)*</b>	92	73	41.8	4
<b>Cost of business start-up procedures (% of GNI per capita)*</b>	1.3	2.4	4.4	1.5
<b>Corruption of the public sector (0 - highly corrupt, 100 - very clean)**</b>	28	43	-	73
<b>Starting a Business rank (1-very easy, 189 - extremely difficult)***</b>	100	65	-	11

Source: World Bank\*, Transparency\*\*, Doing Business\*\*\*

Transition to capitalism requires the transition to a free market, and so, in August 22, 2012, after 19 years of negotiation, Russia made a huge step in this direction, becoming the 156<sup>th</sup> country member of the World Trade Organization (WTO). A country who becomes part of this organization, needs to take a couple of commitments and has a couple of obligations: to reduce the taxes on the agriculture and manufactured products imported, eliminate the protectionist measures and reduce the state's influence in the economy. This step seemed to be a major one for Russia and its commercial partners, but after only 11 month as a WTO member, it was accused by the European Union and Japan of disloyal practices - superior taxes on the vehicles imported, except the ones imported from Kazakhstan and Belarus, and the ones produced inside the Russian borders. On the 6th of January 2014, Russia accused the European Union of unjustified anti-dumping actions, imposed by the European Union on several products imported from Russia, including ammonium nitrate and steel products. No other WTO member reached a conflict with the other members so quickly after it joined the international organization, this shows how unprepared Russia is, to align to the market economy rules.

The political tensions in Ukraine risk to affect Russia's international commercial relations and also diminish the investors' trust that the country is walking down a road that leads to market economy and liberal capitalism. Is a new Cold War about to emerge? Didn't Russia learn anything from the history's lessons? Russia's transition to liberal capitalism is a necessity but also a lasing process, for the state is not yet prepared to reduce its major influence in the economy.

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