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Political Connections of Top Entrepreneurs: Approaches to Measuring and Evidence in Contemporary Russia

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Abstract. The article considers political connections of top entrepreneurs as a special resource that guarantees privileged access to the means of production and provides competitive advantages on the economic markets. They accumulate political connections both in the countries with developed economies as well as in the countries with emerging markets. In the latter case, entrepreneurs exploit this resource directly for the purpose to design institutional environment favorable for firms' performance. Different approaches are identified those allow measuring the magnitude of political connections. Their advantages and disadvantages are revealed. An approach is proposed that involves the use of measure of political connection that is unique for contemporary Russia. This approach is associated with the presence of personal sanctions imposed on the Russian entrepreneurs in 2014 and 2022. The motivation for the imposition of sanctions was due to the fact that they were introduced against entrepreneurs of the "inner circle" who could impact the political decision-making process. In this sense, the presence of personal sanctions can be seen as a proxy for the political connections. The analysis showed that top entrepreneurs who were sanctioned in 2014 are statistically significantly different from entrepreneurs who were included in the sanction lists in 2022. The first group of entrepreneurs was very narrow and it included "confidant persons" of the ruling group. The second group of entrepreneurs was characterized by a combination of personal ties with political leadership and significant investments in establishing links with the political and economic elites of the Western countries. This combination provided the highest return on the exploitation of political connections.

Keywords: political connections, economic markets, top entrepreneurs, approaches to measuring political connections, quantification of political connections.

Research area: social structure, social institutions and processes (socio-logical sciences); regional and sectoral economy.

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Политические связи крупных предпринимателей: подходы к измерению и специфика современной России

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Аннотация. В статье рассматриваются политические связи крупных предпринимателей как особого рода ресурс, который гарантирует привилегированный доступ к факторам производства и обеспечивает конкурентные преимущества на экономических рынках. Показано, что крупные предприниматели накапливают политические связи как в странах с развитыми экономиками, так и в странах с развивающимися рынками. В последнем случае они используют данный ресурс непосредственно с целью формирования институциональной среды, благоприятной для функционирования фирм. На основе анализа экономической литературы выделены подходы, позволяющие измерить величину политических связей, выявлены их преимущества и недостатки. Предложен подход, который подразумевает использование уникальной для современной России меры политических связей, связанной с наличием персональных санкций, наложенных на крупных российских предпринимателей в 2014 и 2022 гг. Мотивация наложения санкций была связана с тем, что они были введены против предпринимателей «ближнего круга», которые могли оказывать влияние на процесс принятия политических решений. В этом смысле наличие персональных санкций можно рассматривать в качестве прокси политических связей крупных предпринимателей. Проведенный анализ показал, что крупные предприниматели, попавшие под санкции в 2014 г. статистически значительно отличаются от предпринимателей, включенных в санкционные списки в 2022 г. Первая группа является очень узкой по составу, и в нее входили «доверенные лица» правящей группы. Вторая группа предпринимателей характеризовалась сочетанием личных связей с высшим политическим руководством страны и значительными вложениями в установление связей с политико-экономическими элитами западных стран. Данное сочетание обеспечивало для крупных предпринимателей наивысшую отдачу от использования политических связей.

Ключевые слова: политические связи, экономические рынки, крупные предприниматели, подходы к измерению политических связей, количественная оценка политических связей.

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Introduction

International experience demonstrates that political connections of big business play a key role in harvesting commercial benefits in developed economies as well as in the countries with emerging markets (Nee and Oppen, 2010). These connections provide competitive advantages on the economic markets and allow top entrepreneurs to obtain privileged access to economic resources. Interplay between top entrepreneurs and government officials can be analyzed as a part of industry lobbying (Olson, 1965), when firms form narrow groups with special interests to push their proposals through the political-bureaucratic process in the legislative bodies. Examples of industrialized democracies show that big business uses political connections indirectly and it exploits the failures of the government to seek and extract political rents (Monardi & Glantz, 1998; Moe, 2005; Gabel & Scott, 2011). At the same time, top entrepreneurs are directly involved in interacting with politicians and government officials to regulate conditions for doing business in emerging markets. They use political connections directly that to design institutional environment favorable for firms' performance (Li et al., 2006; Min, 2011).

Political connections between top entrepreneurs and government officials, as well as the benefits that individual companies and business groups derive from having special relationships with government officials, continue to attract considerable attention from researchers. This problem is especially relevant in the

context of Russia, a country characterized by a high degree of inequality (the share of the richest 1 % of Russians in total income is about 20 %, and in wealth – 43 %, see Novokmet et al., 2018), and high personalization of power. Previous study of the authors showed that entrepreneurs were to have political connections with representatives of regional and local authorities to do business as well as to generate innovations (Levin et al., 2017). High level of personalization and informality are the core features of political connections between the high-level government officials and top entrepreneurs in contemporary Russia. As S. Barsukova mentioned «under the slogans of legalizing the economy and fighting corruption, the administration found new informal ways to manage and control big business, assigning the «the kings of government contracts» to implement projects as a marker of loyalty to the President's administration and a precondition for continued business success» (Barsukova, 2019). For top entrepreneurs to be engaged in the government projects and programs realization means to be politically loyal and to get formal and informal privileges in the Russian economy.

At the same time, it is important to give not only a qualitative description of this phenomenon, but also to quantify how the investments of the top entrepreneurs in political connections allow them to achieve higher growth rates of their total assets. A feature of the implemented approach is the use of a measure of political connections that is unique for Russia,

i.e. the presence of personal sanctions imposed on the top entrepreneurs after the integration of Crimea in 2014, and after the start of special military operation in Ukraine in 2022. In the frame of the article, firstly, an analysis will be made of research literature published in the leading economic journals on the topic of measuring the political connections of business and the effect presence of political connections on the functioning of companies and business groups. Secondly, an empirical analysis of the influence of political connections on the growth rate of the wealth of the Russian top entrepreneurs will be presented. The analysis carried out will allow:

1. To highlight various approaches to define and measure political connections used in the economic literature.
2. To describe the specifics of top entrepreneurs' political connections in Russia.
3. To quantify the extent to which top entrepreneurs derive output from their political connections.

The conducted research will allow us to give a comprehensive quantitative and qualitative description of the activities of top entrepreneurs with political connections. At the same time, the relationship between the goals and limitations of representatives of both business and political decision-making actors will be considered through their political ties, when, on the one hand, the presence of political connections is the most important factor determining the competitiveness of top entrepreneurs on the economic markets, and, on the other hand, investments in they affect the motivation of all participants in political and economic interaction. As a result, not only politically influential top entrepreneurs, but also political decision-makers act as beneficiaries of political connections cultivation and exploitation.

1. Literature review

The relationship between political and economic systems has always attracted attention of researchers. There is an extensive theoretical literature on this topic (see: Bertrand et al., 2018; Prasetyo & Nasution, 2022). Empirical research on this topic faces significant challenges. Firstly, the political connections that

the largest firms and top entrepreneurs possess are inherently unobservable. It is necessary to search for proxy variables, i.e. observable characteristics correlated with unobservable political connections. Secondly, apparently, political connections take a different form depending on the political and institutional environment, respectively, and the proxy variables used to measure them are not universal, it is necessary to develop proxy variables applicable to the unique institutional context.

The most important work in the field of empirical study of the role of political connections was the article by R. Fishman (Fisman, 2001). The focus of the study is the question of the extent to which political connections determine the market value of a firm. R. Fishman notes that there are numerous evidences of specific cases of political connections between business and the state (the so-called anecdotal evidences), but the research, as a rule, did not go beyond the case study. In countries where political decisions are decentralized, defining political connections is a daunting task. The use of data from Indonesian firms has overcome these difficulties. Since this country is highly centralized and had a stable political structure (until the end of the Suharto era), this allowed the author to build a credible index of political connections. It is significant that the author took into account affiliation with business groups when compiling the index and building an econometric model, since the group as a whole, and not individual enterprises included in it, have political connections.

The essence of the study was an econometric analysis of how rumors about the deteriorating health of Indonesian President Suharto during his last year in office influenced the capitalization of firms with varying degrees of political ties. The analysis showed that in all cases the influence of rumors on the share price of politically influential firms was significantly higher than that of less dependent ones. Moreover, the magnitude of this effect was highly correlated with the change in Jakarta stock exchange indices. Apparently, according to the impact on the exchange index, investors assessed the seriousness of the rumors. In this way, the author demonstrated that in Indone-

sia of this period, political connections, rather than fundamentals such as productivity, were the main determinant of profitability, and this skewed investment decisions.

The work of R. Fishman was followed by a number of studies centered on a quantitative assessment of the role of political connections in the functioning of firms (in this case, the terms «political ties», «political influence», etc. were used in the literature). Thus, S. Johnson and T. Mitton (Johnson & Mitton, 2003) demonstrated that the impact of the Asian political crisis in Malaysia reduced the expected value of government subsidies to politically favored firms for 60 billion dollars. The paper uses data from Malaysia before and after the imposition of capital restrictions. The authors were able to show that capital control mechanisms can be used as an essential part of «relationship-based capitalism». Characteristic of this system is that politicians give informal instructions to banks to direct borrowing to approved firms. This policy is easier to implement when the economy is relatively isolated from international capital flows. As a result, firms with political connections: firstly, suffer more from macroeconomic shocks, as they reduce the government's ability to provide them with privileges and subsidies; secondly, benefit from the introduction of capital controls, because this allows them to receive higher levels of subsidies.

A. Khwaja and A. Mian (2005) analyzed the influence of political connections on the likelihood of obtaining credit in Pakistan, using data on loans made by more than 90,000 firms between 1996 and 2002. A firm was classified as «politically powerful» if its top managers ran as candidates in national or regional elections. The results showed that politically connected firms borrowed 45 % more and had 50 % higher default rates on those loans. At the same time, they received such a privileged attitude only from state-owned banks. In addition, the study showed a positive relationship between a firm's belonging to a business group and the likelihood of obtaining politically motivated lending, while the larger the business group, the greater the likelihood of obtaining loans.

In the works of M. Faccio (Faccio et al., 2006; Faccio, 2010), a company is considered

politically influential if at least one of its largest shareholders (controlling more than 10 % of shares) or top managers: 1) is a member of parliament, 2) is a minister or the head of state, or 3) closely associated with a senior official (primarily friendly or family ties). M. Faccio demonstrated that politically influential firms are much more likely to receive state support than firms that do not have political influence. In addition, politically powerful firms disproportionately receive government assistance if the International Monetary Fund or the World Bank provides financial support to a given country.

A significant part of the researches uses the existence of family or friendly connections between the owners or managers of the company and high-level government officials as indicators of the political influence of companies. This approach is perhaps the most objective, but its application faces obvious difficulties in collecting this kind of data. In addition, this approach is applicable only if the political system of the country under study is stable and highly centralized. As alternative approaches to identifying criteria for the political influence of companies, the following are used:

1. Analysis of the presence of state representatives in the board of directors of the company.

2. Study of the «political investments» of the company: spending on financing political parties and lobbying activities; party membership of managers and owners; participation of owners and top managers in political elections.

This type of investment can be characterized as transactional. Companies can make strategic donations, i.e. support politicians who are able to influence their economic well-being. At the same time, such donations can lead to an improvement in the operating activities of firms in industry clusters. The relationship between contributions and firm performance is strongest for poorly performing firms, firms closer to financial difficulties, and contributions in closed elections. The results show that individual political input is valuable to firms, especially in bad economic times (Ovtchinnikov & Pantaleoni, 2012).

A difficult research problem is the fact that «investment in politics» can often be seen not as a kind of «purchase» of competitive advantages, but as a duty, the result of coercion by the state. The situation when firms are forced to invest in politics, receiving no additional benefits from them, but only the absence of business problems, was called by F. McChesney «rent extraction» (McChesney, 1997) by political actors, in contrast to «rent seeking» on the part of economic entities within the framework of A. Krueger's (Krueger, 1974) approach, classical for the theory of public choice. It can be assumed that the acquisition of parliamentary status by owners and top managers is often not aimed at strengthening the lobbying potential, but at obtaining additional protection from persecution, and in this sense is also a forced «investment in politics».

A way around the difficulty of finding criteria for «political influence» is what might be called analysis in terms of political decision outcomes. An example of work built on this principle is the article by E. Slinko et al. (Slinko et al., 2004), in which the criterion for «political influence» was the number of regional laws adopted in the interests of specific firms. The analysis in terms of the results of political decision-making also encounters significant difficulties due to the fact that it is often impossible to unambiguously identify the main beneficiaries of specific political decisions, since the effects of these decisions are of a complex sectoral or regional nature. Thus, the choice of criteria for «political influence» is a non-trivial research task, which is solved differently by different researchers.

2. Statement of the problem

An analysis of the theoretical and empirical literature allows us to draw a number of problematic points. Firstly, political connections matter not only in relatively poor and highly corrupt countries. Moreover, even in the least corrupt countries in the world, such as Denmark, the importance of corporate rent seeking at the level of local governments, which account for almost half of total government spending, remains (Amore & Bennedsen, 2013). Political connections are not limited to

corruption. Personal connections with high-level government officials can go a long way even in a country with generally strong institutions, at least in times of sharp financial crisis and heightened political freedom of action.

Secondly, political connections take different forms in different countries. In democracies, donations to political campaigns are the most important form of political ties. In countries with personalized political regimes, personal connections with the highest political leadership play a key role. In countries where a significant proportion of public spending is at the local or subnational level, political connections at these levels are important. The more centralized the political system, the less important are political connections at the local or subnational level. Another possible classification of political connections is their division into relational (long-term personal ties) and transactional (exchange of services). In stable political systems, and especially personalized political systems, firms are most profitable to invest in relational political ties. In a situation of political uncertainty (for example, regular turnover of power), transactional political connections turn out to be more beneficial for the firm (Arifin et al., 2020).

Thirdly, the mechanisms through which politically connected firms benefit are varied. Political connections allow firms to receive privileged access to resources, primarily to capital, both to bank financing and to equity financing. In addition, political connections allow firms to receive preferential treatment when they participate in public procurement, as well as to be subject to less stringent regulation. Furthermore, politically connected firms are more tax-aggressive due to lower expected costs of tax compliance, better information about changes in tax laws and enforcement, less capital market pressure on transparency, and greater risk appetite caused by political factors.

Currently, high level of confrontation with the Western countries, which have imposed personal sanctions against Russian top entrepreneurs in response to a number of foreign policy actions held by Russian government, is a unique feature of Russia. These sanctions

were grounded by the existence of personal ties between these entrepreneurs and the country's top political leadership. The first wave of the sanctions was imposed after 2014 (Crimea integration), and the second one, that is significantly larger in size, was imposed in 2022 after the initiation of the special military operation. The motivation for the sanctions was that they were imposed against Putin's «inner circle», i.e. entrepreneurs who «had Putin's ear» and who were capable to influence the political decision-making process. Thus, the presence of personal sanctions can be seen as a proxy for the political connections of the Russian top entrepreneurs.

Research question is whether is it true that top entrepreneurs who were later sanctioned increased their fortunes faster before 2014 if compared them with other entrepreneurs? An analysis of the dynamics of wealth growth after 2014 is meaningless, because we cannot separate the two effects, i.e. the effect of political connections and the effect of personal sanctions. However, if we analyze the growth rate of wealth before 2014, this problem disappears because sanctions have not yet been imposed and their effect is absent.

3. Data and Models

Our data include information about assets of the wealthiest Russian top entrepreneurs for each year over the 2003–2009 period, compiled from the rankings published by a Russian business weekly Finance. On average, each yearly ranking includes 500 entrepreneurs. The rankings rely on expert assessment of the value of industrial assets and the real estate that the participants own. Data also include manually compiled information on entrepreneurs sanctioned by the EU, the USA or the UK, coded as a cat-

egorical variable with three distinct values: (a) not sanctioned, (b) sanctioned after 2013 but before 2022, and (c) sanctioned after 2022.

The final database has a panel nature. The unit of observation is a person-year, the objects of observation are entrepreneurs, and the time dimension is represented by years. Key variables include total asset value, industry affiliation of key assets, and a categorical variable reflecting whether an entrepreneur was sanctioned in 2014 and 2022 (Table 1).

The estimated models are the following:

$$\ln(Assets)_i = \beta_0 + \sum_{k=1}^K \beta_{1k}(Sanctions)_{ik} + \beta_2(Time)_i + \sum_{h=1}^H \beta_{3k}(Industry)_{ih} + \epsilon_i.$$

$$(Assets\ growth)_i = \beta_0 + \sum_{k=1}^K \beta_{1k}(Sanctions)_{ik} + \beta_2(Time)_i + \sum_{h=1}^H \beta_{3k}(Industry)_{ih} + \epsilon_i.$$

where assets are the total value of accumulated assets in million dollars; sanctions are a categorical variable that takes the value 0 if the entrepreneur was not sanctioned, 1 if he was sanctioned after 2014, 2 if he was sanctioned after February 24, 2022; Time is annual dummy, and Industry is a categorical variable reflecting industry affiliation.

4. Results and Discussion

Results of evaluation of models with random effects are presented in Table 2.

To simplify the perception of the evaluation results, we have presented them in graphical form in Fig. 1. The results show that the group of entrepreneurs sanctioned after the integration of Crimea in 2014 did not differ statistically from entrepreneurs who were not sanctioned either in the terms of level or growth of assets. At the same time, entrepreneurs sanctioned after the special military operation ini-

Table 1. Personal sanctions against Russian top entrepreneurs

	Quantity	Percent
Not sanctioned	979	95,23
Sanctioned after 2014	7	0,68
Sanctioned after 2022	42	4,09
Overall	1028	100,00

Table 2. Sanctions, assets, and asset growth: estimates from the GLS regression

	Asset level	Asset growth
Sanctioned after 2014	0,772 (0,446)	-0,118 (0,211)
Sanctioned after 2022	2,066*** (0,238)	0,131*** (0,041)

Note: 3,245 observations (person-years) and 1,028 persons for asset level; 2,075 observations (person-years) and 674 persons for asset growth. Standard errors in parentheses. Standard errors clustered on the level of persons. Results controlled for time effects and entrepreneur's industry. * $p < 0,05$, ** $p < 0,01$, *** $p < 0,001$

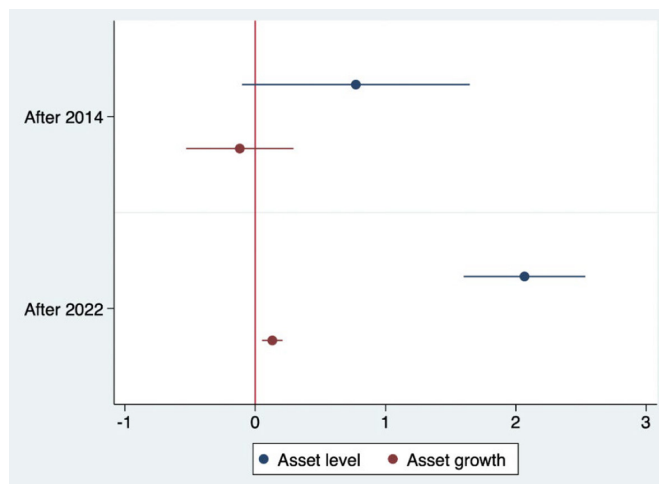


Fig. 1. Results of evaluation of entrepreneurs' asset level and asset growth after sanctions 2014 and 2022

tiation in 2022 are statistically different from both entrepreneurs who were not sanctioned and those who were sanctioned after 2014.

We can pay attention to the fact that entrepreneurs who were sanctioned after the integration of Crimea in 2014 differ significantly from entrepreneurs who were sanctioned after 2022. First group was distinguished by a high level of personal connections with the top political leadership. Second group was characterized by a combination of personal connections with top political leadership and significant investment in building links with political and economic elites in the Western countries. Apparently, this combination ensured the highest return rates on political connections for top entrepreneurs.

Previously, it was mentioned that the most important mechanism that allows firms to benefit from political connections is privileged access to bank and market financing. Financing

and newest technologies from Western countries played a crucial role in the development of Russian business in the period up to 2014. Foreign investors could provide privileged access to capital for entrepreneurs with political connections regarding them as a certain protection against country risk. A number of studies (Kalotay, 2008; Panibratov & Michailova, 2017; Fernández-Méndez et al., 2018) shows that the combination of internationalization of doing business strategy and exploitation of domestic political connections based on the state support leads to the high return rates and allows top entrepreneurs to scrape abundant political rent. In this case, one may say that second group of top entrepreneurs demonstrated dual loyalty and they were embedded into two types of networks (Levin & Sablin, 2022). The first network was Russian vertical of power structure, and second one was represented with global value chains (GVC).

5. Conclusion

Political connections allow top entrepreneurs to gain significant competitive advantages on markets of economic goods (services) and resources. Institutional organization of the economy and society, which determines the various forms and mechanisms of political connections exploitation, is of crucial importance. Top entrepreneurs actively use political connections in advance economies that is characterized with democracy and clear specification of property rights as well as in countries with emerging markets where there are blurred specification of property rights and personalized connections with top political leadership is the most reliable guarantees for doing business beneficially.

Currently, Russia is in unique and unprecedented situation, which is characterized by the imposition of comprehensive sanctions by Western countries. Sanctions were introduced in two waves. The first wave of sanctions was linked with the integration of Crimea, and af-

ected a small number of top entrepreneurs. We assume that they were the members of the «inner circle» of the President (his confidants). One may note that this «inner circle» does not have fixed number of its members and its borders are very flexible according to the various factors. Sanctions 2022 had comprehensive nature and they touched the Russian top entrepreneurs who performed dual functions and played the role of the «bridge» between the global markets (sources of the newest technologies and finances) and the Russian vertical of power structure.

Fulfilled research showed that entrepreneurs sanctioned after the special military operation initiation in 2022 were statistically different from both entrepreneurs who were not sanctioned and those who were sanctioned after 2014. This fact means that the most lucrative strategy to scrape political rent was to combine business internalization (and expansion) on the world markets with cultivation and exploitation of domestic political connections based on the state support.

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