

The Future That AvtoVAZ Needs

By Konstantin Sonin



The fate of AvtoVAZ was finally settled last week. According to the latest information, a controlling stake in the auto giant, held by the company itself and managed by its top executives, has been acquired by state-owned arms exporter Rosoboronexport. There is little doubt that the removal of Vladimir Kadannikov, whose undistinguished 20-year tenure as head of AvtoVAZ ended late last month, and the search for a new owner were orchestrated in the Kremlin. From this point on, in line with current Kremlin policy, AvtoVAZ will operate under direct state control.

This is the wrong way to proceed. The main motive behind the changes at AvtoVAZ was not the banal greed of individual members of the Kremlin leadership, although this catch-all explanation has become increasingly popular with political commentators. The changes more likely resulted from the government's unwillingness and inability to pursue a sound economic policy. The notion that the state ought to take charge of companies like AvtoVAZ is also based on the belief that individuals control the economy, when in fact it is controlled by incentives.

I have no doubt whatsoever that the new state-appointed executives at AvtoVAZ will succeed in restoring order to the company by sorting out relations with its distributors, for example. But I am equally certain that once they have put AvtoVAZ's house in order, the new execs will shy away from the pressing task not just of modernizing production, but of replacing AvtoVAZ with a new, up-to-date automobile production facility. They won't back down from this challenge because it's more than they can handle. They'll simply realize before too long that designing and building cars is not the most profitable approach.

Even the most market-minded MBA, installed as the general director of AvtoVAZ and made responsible for the well-being of the nearly 750,000 residents of Tolyatti, the company town where AvtoVAZ is based, would opt to invest his time and money not in production but in lobbying the government for protective tariffs and other forms of state support. Incentives drive the economy, and for AvtoVAZ lobbying brings in far more revenue than making and selling cars. Rosoboronexport's considerable clout and connections will only increase the profit to be made from lobbying, which will, of course, further decrease the incentive to invest in production.

Assuming that the change of ownership at AvtoVAZ was ordered by the Kremlin, what could be done to make it work? First off, the government should sell the company to a private investor without worrying too much about the price. That's not the most important thing, however. If the government wants to make AvtoVAZ a going concern, it should free the new owners from the burden of providing for the good people of Tolyatti. This would also remove the company's trump card in its requests for state subsidies and boost incentive to invest in the modernization and development of the company itself.

This would be an enormous and very expensive task involving the retraining of the work force, the relocation of residents and the diversification of the city's economy. And no one but the government is ever going to take it on. In recent years, the authorities have developed the habit of leaving social problems to the oligarchs. But at some point the government has to tackle the big problems facing the Russian state.

Liberal economists usually oppose state intervention in the economy. In this case, however, the state has to get involved -- in the right way.

Konstantin Sonin is a professor at the New Economic School/CEFIR and a columnist for Vedomosti.