SALE OF THE CENTURY

RUSSIA'S WILD RIDE FROM COMMUNISM TO CAPITALISM

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CROWN
BUSINESS
NEW YORK

Published by Crown Publishers, New York, New York.
Member of the Crown Publishing Group.

Random House, Inc., New York, Toronto, London, Sydney, Auckland
www.randomhouse.com

Printed in the United States of America

Design by Joseph Rutt

Library of Congress Cataloging-in-Publication Data is available.

ISBN 0-8129-3215-3

10 9 8 7 6 5 4 3 2

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WHO GETS THE LOOT?

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For the first few years, Russia's second revolution was about ideas. But once the young reformers had set their revolution in motion from above, a whole new struggle began. Russia's transformation was no longer just an ideological battle, a clash between dissident intellectuals and Communist hard-liners. Instead, it became a fight over what all revolutions are ultimately about: Who gets the loot? Who would own the stuff—the rust-belt manufacturers, the Siberian oil fields, the Arctic diamonds—that the Russian state no longer had the will or the power to control?

In most revolutions, the answer to that question is simple: the revolutionaries confiscate the loot from their opponents and give it to their friends. The Jacobins beheaded the old French nobles and handed their estates over to the rising bourgeoisie. The Bolsheviks executed and exiled the tsarist aristocrats and merchants and transferred their property to the state. Iran's ayatollahs expelled the Shah and his ruling class and nationalized their assets.

But Russia's capitalist revolutionaries were a bit different. They quickly identified who their friends and enemies were: a new breed of aggressive, ostentatious entrepreneurs, eventually dubbed the New Russians, were the reformers' natural allies, and the old Soviet industrial bosses, known as the red directors, were their instinctive adversaries. Ideally, the reformers would have liked instantly to force out the Communist industrial elite and usher in a new capitalist one. But if that wasn't possible, it didn't worry them too much. The main thing was to create a capitalist system: it didn't really matter who the capitalists were.

For them, transforming Russia was sort of like writing a computer program. As long as they got the program right—as long as they created the proper, capitalist incentive structure—everything else would automatically fall into place.

So the young reformers wrote their program—they set mass privatization in motion—and then stepped back and let Russia's 147 million citizens fight it out. Most of the time, the struggle was between the red directors and the New Russians. Occasionally, foreign investors tried to get involved, too. Always, the battle was about more than one specific plant somewhere out in the southern steppes or a single remote oil field in the Arctic tundra. Each fight was a fight for dominance of the new Russia. Here are a few stories from the front line.

THE SMARTEST RED DIRECTORS OF ALL

The canniest players in the fight for the loot, and the most enduring ones, were the *gazoviki* and the *neftyaniki,* the natural gas and oil executives who managed the vast reserves of fossil fuels with which Russia is endowed. By nature and by experience, they did not seem particularly well adapted to the fledgling market economy. They were red directors, crimson-cheeked, heavy-drinking, fist-thumping princes of the Soviet Union's industrial *nomenklatura.* Yet, somehow, once the dust had settled, the old-school *gazoviki* and *neftyaniki* had emerged as the most successful combatants in the struggle for economic dominance in the new era.

The secret of their phenomenal success was that they had the audacity to apply the basic privatization principles that had been designed for a worthless industrial base to Russia's precious natural resources. The whole idea behind Chubais's privatization drive was that it didn't really matter if Russia's factories were given away—the important thing was to transfer them to private owners. Where the Soviet rust belt was concerned, that philosophy made some sense. But there was a world of difference between being given shares in an antiquated steel mill and shares in a vast natural gas field. That difference was what made the *gazoviki* and *neftyaniki* the most powerful of Russia's new capitalists.

The mightiest of all were the unlikely capitalist duo of Viktor Chernomyrdin and Rem Vyakhirev, two middle-aged former Soviet gas engineers. A heavyset man with a shaky grasp of Russian syntax and a plodding manner, Chernomyrdin was swiftly dismissed as a nonentity by the quick-witted Moscow intelligentsia when the parliament appointed him prime minister in late 1992, as a compromise replacement for the increasingly unpopular Gaidar. Yet it was the stolid Chernomyrdin who had masterminded the creation of Gazprom, capitalist Russia's dominant company. As the Soviet cabinet minister for the oil and gas sector in the mid-1980s, he was one of the first industrial apparatchiks to spot how Gorbachev's perestroika might one day transform the country's entire economy. What other red directors saw as a threat, Chernomyrdin turned into an opportunity. In 1989, he brought the whole gas industry into a single company, then still state owned, and became its chairman.

The beauty of Chernomyrdin's strategy became clear after the young reformers' privatization drive began to reshape Russian industry. A walloping 15 percent of Gazprom was sold to the company's employees and management at a nominal rate. Ten percent was retained by the company itself, 35 percent sold to domestic investors (generally at closed auctions held in the remote Siberian regions where most natural gas is produced), and a golden 40 percent stake was retained by the government. The Gazprom executives' power was further enhanced by a trust agreement between the cabinet, led by Chernomyrdin, and Vyakhirev, his former deputy and successor as head of Gazprom. The deal gave the Gazprom boss the right to manage the state stake and vote on the government's behalf at shareholder meetings. A further, secret agreement, which was later revoked by the state, gave the Gazprom management the option to buy additional shares far below their market value. Vyakhirev also had tremendous authority over the private shareholdings in his company: the Gazprom charter granted the company's management the right to veto all private transactions in the firm's shares.

As the first, fuzzy outlines of Russia's post-Communist economic landscape began to emerge, Gazprom towered over every other business in the land. It had 360,000 employees and, counting pensioners, family members, and subcontractors, supported an additional 6 million people.

Gazprom controlled 30 percent of the world's known natural gas reserves; it was Russia's single biggest hard-currency earner; and it accounted for about 8 percent of the country's gross domestic product. In 1996, when a leading Russian financial journal polled the country's top entrepreneurs and economists to determine the nation's most powerful businessmen, there was no contest: Vyakhirev of Gazprom was at the top.

Although the *gazoviki* were probably Russia's most successful capitalists, they were also among the most old-fashioned. Gazprom's biggest nod to the paternalistic traditions of the USSR was the subsidized prices—usually less than a tenth of the world level—at which it sold gas on the domestic market, and its tolerance of huge levels of nonpayment by its Russian customers. On the face of it, Gazprom's support for state-controlled, artificially low gas prices seemed bizarre. But in a country where gas was a major source of heating, the chief source of cooking, and an important fuel for electricity production, the subsidies gave Gazprom the right to claim, as Vyakhirev did in a conversation with me, that "we heat and feed all of Russia."

The political and financial advantages of playing such a role were inestimable. Gazprom was granted a number of generous tax concessions, including tax breaks to build up a special internal stabilization fund. Although gas exports were regulated by licenses and quotas, Gazprom itself was exempt from export tax, some import tarriffs, and VAT. According to Anders Aslund, a Swedish economist who is one of the company's most informed critics, Gazprom's package of tax breaks amounted to billions of dollars in lost state revenues every year.

These tax concessions and Gazprom's close relationship with Chernomyrdin's cabinet prompted many of the young reformers to attack the company as one of the biggest obstacles to the emergence of a liberal, transparent market economy. Western critics were even more virulent. Jeffrey Sachs, the Harvard economist who was one of the intellectual fathers of shock therapy, argued that Gazprom had been "stolen" from the Russian people. Coming from one of the world's premier market reformers, his proposed solution was shocking: renationalization, followed by a more equitable privatization of the company.

Unsurprisingly, Vyakhirev turned even more beet colored than usual when I put these charges to him. What was good for Gazprom, he insisted heatedly, was good for Russia; the government was absolutely justified in taking special care of its flagship—indeed, it would be folly to do otherwise. This argument, backed by Gazprom's tremendous economic and political muscle, worked. Gazprom shrugged off the young reformers' repeated attempts to curb its power and trim its privileges as languidly as Vyakhirev stubbed out the cigarettes he chain-smoked.

Vyakhirev was confident Gazprom would endure no matter who Russia's political merry-go-round would spin into the Kremlin next. "No matter who is in power, they won't start dividing the pipelines or give them to some collective farm," he told me. "The system cannot be disturbed. Without Gazprom, there is no Russia."

It was the sort of ponderous comment that made Vyakhirev and the old-school Gazprom executives seem so out of place in the increasingly Westernized, fast-moving, and sophisticated business culture of the new Russia. But two and a half years later, when the new Russian economy came crashing down to earth, I would remember Vyakhirev's words as more than a little bit prescient. Russia's looming economic collapse would take down many of its newfangled highflyers. But the apparatchiks at Gazprom, who had kept one foot firmly planted in the Soviet past and used their old-school connections to milk the state more effectively than the most resourceful entrepreneur, were left standing. Rem was right: warts and all, Gazprom really was Russia.

THE NEW RUSSIANS WIN: SHOWDOWN IN THE ARCTIC CIRCLE

On a clear blue morning in the middle of February 1996, with the slam of a door that would not quite shut and the whirr of helicopter blades, I was on my way to Gaz-Sala, a remote settlement of two thousand people north of the Arctic Circle. The only reason people lived this close to the North Pole was to search for more of Russia's abundant natural gas and oil reserves, and in Gaz-Sala the company that did that was Zapolarneftegazgeologia (ZNGG), a small seismic exploration and drilling enterprise.

For savvy New Russians, companies like ZNGG, known as *geologias*, were a potential Klondike. The main work they did—geological exploration on contract to the larger companies—was not particularly lucrative. But, thanks to a loophole in Russian legislation, in theory, the *geologias* also had the right to obtain production licenses for any oil and gas they discovered on the territory they were chartered to explore. That made *geologias* a back door into the Russian oil and gas industry. For the investors smart enough to realize it, *geologias* were a way of buying access to potentially millions of dollars' worth of fossil fuels for mere kopecks.

Naturally, like the Communist-era managers of all Soviet companies, the directors of the *geologias* were not keen to surrender their enterprises to outsiders. The remoteness of the Arctic magnified the power every Soviet director enjoyed, making the heads of *geologias* more like feudal lords than mere managers. A lifetime spent enduring the hardships of the far north also sharpened their resentment of outsiders who sought to use the privatization process to win control of companies the directors had come to think of as "theirs."

Just getting to Gaz-Sala was a major expedition. I traveled the final leg of my three-day journey with vodka rubbed on my face by anxious fellow travelers to ward off frostbite and wrapped up in newspapers like a piñata to provide an extra layer of insulation under my coat and boots. When we finally arrived, I was astonished, and not just because I had survived the trip: it was one of those absolutely still northern days that are the coldest, but also the most beautiful. The silent and seductive landscape was a world away from the metropolitan grime and big-city politics of Moscow. But, even here, at the edge of civilization, Russia's capitalist revolution was making itself felt.

I began to learn the story of the battle for ZNGG a few hundred meters away from the helicopter landing pad, in the two-story headquarters of the company, perched on stilts above the treacherous permafrost. The ramshackle building dominated the sad little street that passed as Gaz-Sala's downtown and had the thrown-together, almost intentionally ugly look of most settlements in the far north. Inside, I met Joseph Piradashvili, the acting director of ZNGG and the local representative of

Kakha Bendukidze, the sharp Moscow-based New Russian entrepreneur who had launched the battle for the company.

A small, energetic man with thick black hair, chocolate brown eyes, soft hands, and the elaborately courteous manners of his native Georgia, Piradashvili was not the sort of person I had expected to encounter at the edge of the world, at the eye of a corporate war. In what Russians called their "past life"—meaning life before the collapse of the USSR—Piradashvili had been a theoretical physicist in Tbilisi, an ancient, elegant city of cobblestoned streets and sidewalk cafés. But the disintegration of the Soviet Union had thrust Georgia into civil war and desperate poverty. Piradashvili, in his late thirties with two children, needed a new job.

In late December 1994, he phoned Bendukidze, a fellow Georgian and old university buddy, who had hustled his way into business in Moscow, starting with producing chemicals for laboratories then quickly expanding into everything from trading cigarettes to refining oil. Three days later, Piradashvili was putting up posters around Gaz-Sala, part of a team trying to buy enough shares in ZNGG to give Bendukidze majority control.

Oleg Kudrin, the company's pugnacious, hard-drinking red director, put up a powerful defense. He stoked the suspicions of the already skeptical locals, warning that the outsiders were dangerous Georgian mafiosi. Helicopter operators, part of the Soviet industrial establishment in which Kudrin was an influential figure, would not allow Bendukidze's employees to fly with them. When the group chartered their own helicopters, they were refused permission to land. When they finally managed physically to arrive in the town, the two local hotels, both controlled by ZNGG, would not rent them rooms. The best they could do was persuade one sympathetic resident to rent them a three-room apartment—a tight squeeze for ten men living in isolation for nearly half a year.

By June 1995, the team's tenacity and deep pockets had paid off. Bendukidze's group had bought up over 54 percent of the enterprise, paying more than 100 times the initial price for the last few vital shares. Legally, Bendukidze now owned ZNGG. But the fight did not end there. Accustomed by long years of Soviet experience to treating the enterprise he managed as effectively his personal property, Kudrin, like thousands of other red directors, refused to hand over control to an outsider whose only claim to ZNGG was that he had bought it.

One of the most popular and most effective ways of keeping the new owners out was the one Kudrin used against Bendukidze—he refused to enter the outsiders' holdings in the shareholder register. It was a widespread tactic, and before long, fund managers in New York and London were complaining about managerial tampering with shareholder registers, warning that the lack of safeguards for investor rights would dissuade many outsiders from bringing their capital to Russia.

Like many Western investors, Bendukidze responded by taking Kudrin to court. Bendukidze won. But, back in Gaz-Sala, the court's ruling had no effect. In a symptom of the weakening of the Russian state, which was felt in thousands of similar cases across the country, the government lacked the muscle to enforce its laws on the ground.

So Piradashvili took matters into his own hands. When Kudrin was out of town on July 20, one of those endless northern summer days, Piradashvili and his team, feeling a bit ridiculous, "like actors in a western," walked into the ZNGG headquarters and took over the company by force.

These commando-style tactics were the beginning of a surreal, three-month standoff that Piradashvili described as "like something out of Gogol." The Bendukidze group held their ground in the managers' office and began to issue a stream of orders. Meanwhile, the old management continued to occupy the rest of the building and issue their own edicts. In practice, the old management still ruled the roost, but they couldn't evict the capitalist cuckoo, either.

Like any military siege, the stalemate was both mind-numbingly tense and excruciatingly boring. At one point, Kudrin threatened to shoot the interlopers to force them out of town. To keep themselves amused, the occupiers played computer games. Throughout, Piradashvili and his team knew all of their telephone conversations with Bendukidze were being bugged. They were on the verge of buying a scrambler, when the two men realized it would be cheaper and easier simply to revert to Georgian, their mother tongue.

The conflict did not end until October, when the brief, riotous blooming of the tundra and the midnight sun had already given way to three-foot snowbanks and lengthening nights. Neither the dueling cowboys in Gaz-Sala nor the ineffectual local courts managed to resolve the struggle. As with so many things in Russia, it was settled only when the power brokers in Moscow made a deal.

After months of negotiating, Bendukidze reached an agreement with the Moscow financial group that had been backing the red director. The opposition on the ground in Gaz-Sala evaporated. Bendukidze was now the uncontested owner of what he hoped was an embryonic oil company, and Piradashvili was appointed the enterprise's new manager.

It seemed like a victory for Russia's market revolution. Not only had ZNGG been privatized, but ownership had been transferred to the sort of aggressive entrepreneurs that Chubais hoped would eventually acquire most of Russia's assets. With progressive, Westernized owners and managers like Bendukidze and Piradashvili—men driven by the profit motive, not the Party diktat—in charge, the young reformers in Moscow were confident the Russian economy would emerge from terminal decline into robust growth.

But up in frozen Gaz-Sala, Piradashvili discovered it was not quite as simple as that. For one thing, during the era of dual power, while the rival directors had duked it out from neighboring offices, the company had been "paralyzed" and its financial health had deteriorated precipitously. ZNGG's difficulties were also exacerbated by bizarre decisions Kudrin had taken in his effort to adapt to the strange new economic rules being imposed by the reformers in Moscow. For example, Kudrin had decided to use ZNGG'S slender financial reserves to play the stock market. Like so many of Russia's enthusiastic but inexperienced investors, he had been ripped off. Piradashvili and ZNGG were left with his losses.

Another problem for Piradashvili, and the thousands of other New Russian managers across the country, was the corrosive legacy of the Soviet past. Like every enterprise in the Soviet Union, ZNGG had been created and run to suit the needs of the centrally planned economy. These were usually wildly at odds with the market conditions that were gradually coming to predominate. Restructuring ZNGG—and indeed the entire Russian economy—would ultimately prove far harder than privatizing it.

For Piradashvili, the hardest thing to do was sacking the hundreds of superfluous workers the Communist system had given managers implicit incentives to employ. "People come to me with tears in their eyes and beg for their wages and their jobs and I must be hard and refuse," he told me. "I have become like a caricature of the evil capitalists I used to read about in school as a child."

What made the layoffs particularly traumatic was the country's paternalistic tradition. Life in the Soviet Union was oppressed and uncomfortable, but the workers' state was true to its Communist credo at least insofar as it offered almost all of its citizens the right to a job, however unpleasant or poorly paid. Within a few months, Yeltsin's capitalist revolution had swept away those guarantees and dissolved the savings that might have cushioned people's transitions.

The economic deformities of the Soviet era were not Piradashvili's only problem. Russia's new economy, still floating in a limbo between communism and capitalism, imposed its own distortions. The most crippling of them, and the one that would prove the most difficult to unravel, was the web of interenterprise debt.

Russia's hulking monopolies, partially privatized behemoths that controlled energy and transport and had no incentive to adapt fully to the market economy, were at the center of the arrears web. These monopolists, a group that included Gazprom, allowed other enterprises to accumulate huge, unpaid arrears to them. Burdened by massive debts, these smaller enterprises were unable to pay one another, the government, or their workers. That made it difficult for the government to pay its own bills to everyone ranging from pensioners to arms factories and energy suppliers. The energy and transport monopolists in turn amassed huge debts to the government and to their own suppliers.

For many people, the arrears crisis was a financial bonanza. It served as a smoke screen, obscuring the significance of transactions in what was supposed to be a market economy. Behind the veil of arrears, managers could steal from their own companies, pay one another kickbacks, defraud the state, and bribe bureaucrats.

But for progressive managers like Piradashvili, the arrears web was a tremendous obstacle in the effort to create profitable, financially transparent companies. When Piradashvili finally took over ZNGG in the fall of 1995, the company owed 42 billion rubles in back taxes. But it was owed almost three quarters as much by the government and Gazprom, for which ZNGG worked as a contractor. Because the arrears crisis was as much a political creature as it was an economic one, these debts had a chimerical nature that made them particularly difficult to manage. As Piradashvili put it: "It's a strange sort of debt that can get larger or smaller all by itself. Yeltsin says one thing, or signs some decree in Moscow, and the debt changes."

For the ordinary people of settlements like Gaz-Sala, Russia's bizarre, metastasizing web of debt had one very practical consequence: wage arrears, which meant that salaries were paid months, and in some places years, late. When I traveled to Gaz-Sala I was accompanied by three armed bodyguards carrying a suitcase stuffed with a third of a million dollars' worth of rubles. The injection of cash was part of Piradashvili's effort to reduce ZNGG's wage debt from the 9-billion-ruble level he inherited, down to 4 billion rubles.

After a happy day doling out the money from Moscow, Piradashvili invited me to join him and Vladimir Semianiv, the local policeman, for supper at one of the town's three private restaurants. Stepping into Svetlana's Place was one of the most encouraging moments of my visit. Warm, clean, and cheerfully decorated, with the hearty atmosphere of a mom and pop's truck stop somewhere in the Midwest, Svetlana's Place was an exception to the general gloom of Gaz-Sala. If someone in such a remote town had been enterprising enough to open a restaurant like this, I thought as we sat down, then the outlook for Russian capitalism must be pretty bright.

My optimism did not last for long. Within a few moments vodka and its traditional accompaniments—rye bread, pickles, and marinated mushrooms—had arrived, and Vladimir launched into the ritualized lament about the new Russia, which I had heard dozens of times over the past few years. "People here have worked hard all their lives, freezing and finding oil," Vladimir, a tall, lanky Afghan war veteran with a perky mustache and two gold teeth, declaimed. "Now, they have all lost their savings overnight. Worst of all, now some people have become very rich, while others have become very poor. I'm surprised we haven't had a public revolt."

After a second shot of vodka, Vladimir became more poetic and began to embroider on a rhetorical question that was a sort of popular chorus for the people of the far north: "What I can't understand is how the Arabs in the desert could create for themselves a paradise on earth, while we live in hell. We live on top of a fortune, but we live like beggars."

It got worse: soon Vladimir was telling me that half the townspeople were alcoholics, that freezing to death in the five-foot snowbanks after a particularly nasty bender was one of the most common causes of death, and that the settlement's pensioners, who had expected a comfortable retirement on "the earth" (as the people of the Arctic called anywhere south of the permafrost line), had instead become "prisoners of the north," trapped because their life savings had been devalued by Gaidar's price liberalization.

To my relief, this pessimistic litany was interrupted by the arrival of our first course: a pinkish slab of a northern fish called *shchokur.* Rich in vitamins and tasty, *shchokur* was eaten in raw, half-frozen slices dipped into a spicy sauce; it was, Vladimir and Joseph told me, "the ice cream of the Arctic."

Introducing a foreigner to a strange local delicacy seemed to lighten the mood, and by the time we got to our fourth shot of vodka, Joseph and Vladimir grew more optimistic. They regaled me with stories of northern hardships fought and mastered. How thick the mosquitoes were in the summer, but also how rich the tundra was, for a few precious days, in berries and wildlife. How, in the winter, the snowy landscape and ivory horizon grew so indistinguishable that driving was impossible. But also how, as I would learn when I left the settlement before dawn the next morning, driving by night, with powerful headlights, was a way to outmaneuver nature's whiteout.

"You can see the people here as prisoners of the north, but that is not the only way to see them," Joseph said. "The people here are men who take masculine pride in the brave and difficult work they do. They are women who want to live with their menfolk. It is not just the rejects who are here, but good, hardworking people, people who deserve a better life than bad managers have given them. We are here to further our corporate interests, of course, but we also hope that our efforts will lead to an improvement in their lives."

They were also people, Joseph said, who, like the rest of their countrymen, were taking their first few breaths of freedom. Liberty was unaccustomed, and difficult to adapt to, but it was exhilarating. "Last year, this town faced a real and difficult choice," Joseph explained. "You had to work with us, or with Kudrin, the old manager. People here, and in Russia as a whole, are not accustomed to making choices. The whole idea of making choices is difficult, but it is also exciting. This is the victory of Russian democracy. Even here, in a town that appears on no maps, it is being felt and that's why I think democracy has a great future in our country."

Vladimir agreed: "Let us have choices, even bad choices, because that is better than no choice at all."

And, with that, Joseph proposed our fifth and final toast: "I perfectly understand its defects but, all the same, let's drink to Russia's new democracy. To freedom!"

THE FOREIGNERS WIN: CATS, RATS, AND BEER

A few weeks after joining Joseph in his toast, I was drinking to Russia's future with another group of enterprising company directors, in another remote province. The hopes and fears expressed around that heavily laden table were much the same but these were toasts with one important difference. Our tipple of choice was beer, rather than the more traditional vodka, because the enterprise whose prospects we were rooting for was the Perm Brewery, in the eponymous city in Russia's geographical heartland.

Perm Brewery's initiation into capitalism was a world apart from the physical struggle that raged in Gaz-Sala. For a start, the factory's transition from state control to outside proprietors was a gentle, conciliatory process. And the brewery's new owners didn't just fly in from distant Moscow—they came from New Delhi.

Russia has an ancient and volatile relationship with foreign entrepreneurs. The first eastern Slavic state—Kievan Rus, based in what is now Ukraine—was founded by Scandinavian merchant princes. Some of the younger scions of the trading clan were sent up north, eventually forming what became the first Russian city-states and the country's royal dynasty. The Mongols, bitterly resented for imposing what Russian historians dubbed the Tatar yoke on medieval Russia, introduced a business relationship with the outside world of a different sort: for two centuries, the Mongol overlords exacted heavy tributes from the Russian princes, constraining the region's social and economic development, but also opening up trade routes to the east.

Imperial Russia continued this love-hate relationship with businesses and business ideas from abroad. Peter the Great spent a year as a lowly apprentice in Dutch and English shipyards and imported foreign tradesmen en masse. Yet he also introduced Russia's first comprehensive protective tariff and treated the country's fledgling industrialists, both foreign and native, as vassals, utterly subservient to the will of the tsar. Subsequent Russian rulers, including the Bolsheviks, continued this schizophrenic pattern, seeking to acquire foreign know-how but often rejecting the foreigners themselves.

Boris Yeltsin's Russia exhibited the same ambivalence. On the one hand, the capitalist revolution and its chief architects, the young reformers, were strongly in favor of foreign investment. They knew the moribund Soviet economy needed external capital and know-how to be rebuilt. But, in practice, the new Russian economy was often hostile to foreign investors. A business culture that relied far more on personal ties than on the rule of law tended to automatically discriminate against outsiders. Where "strategic" sectors of the economy were concerned (such as the defense industry or natural resources), the bias became overt, with official restrictions on foreign participation.

These barriers and the lingering failure of market reforms to deliver economic growth kept direct foreign investment far below the Russian government's hopes—and below the international norm. Indeed, in 1997, the year of the country's strongest economic performance since the collapse of communism, little-league Peru attracted more direct foreign investment than the former Soviet superpower.

But a few adventurous outsiders were undeterred. For these buccaneers, Russia's mass privatization drive represented, in the words of one American businessman, "the sale of the century," and they were determined to get in while the bargains lasted. One of them was Shiv Khemka. Like many of the first wave of foreign investors, his family had been doing business with the USSR since the 1950s, when the special relationship between nonaligned India and the Soviet Union was at its apogee. When Russia launched its market revolution, the Khemkas suddenly had an opportunity to build their Soviet-era connections into big business.

Shiv, the eldest son, was delegated to spearhead the family's new Russian campaign. A teetotaling vegetarian with a coffee complexion, a hooked, patrician nose, and the plummy accent and almost painful good manners of his Eton education, Shiv, who was in his midtwenties when I met him in 1992, seemed disastrously ill suited for the vodka-slurping, meat-chomping, earthy masculinity of Russia's nascent business culture. But in the spring of 1996, when I joined Shiv on a visit to the Perm Brewery, I discovered a foreign investment that, ever so slowly, seemed to be starting to work.

From the moment in the early 1990s when they decided to focus on the beer business—by 1996 the family owned several Russian breweries and a separate distribution company—the Khemkas owed their survival in Russia's rough young marketplace to two basic tenets: a sensitivity to the political constraints on foreign investment and a boundless faith in the country's economic prospects.

It was thanks to the first principle that the family chose the humble world of beer, rather than sexier sectors like oil and gas. Like most outside investors, the Khemkas were initially attracted to the country's wildly undervalued and easily exportable natural resources. But the old apparatchik friends of Shiv's father, many of them powerful figures in the conservative defense industry, warned that foreign investors in such high-profile areas risked becoming the targets of overt nationalist political attacks or more subtle backroom maneuvering.

Their second principle, an adamantine confidence in the coming Russian economic boom, narrowed the choice down to beer. Beer has a marginal role in the life of the Russian drinker. With its wimpish 3 or 4 percent alcohol content, it is treated, as it was in medieval Europe, as a soft drink, rather than a genuine alcoholic beverage. The peak daily consumption of beer is between 6 and 8 A.M., at breakfast time, and in stores it is sold next to the mineral water and Coca-Cola.

By contrast, vodka has pride of place as a "real" drink. Russian drinkers guzzle 83 percent of the world's vodka, Shiv informed me during our flight to Perm, with the average Russian drinking 2.5 times as much vodka as the total hard-liquor consumption of the average American. Consumer trend specialists have predicted that if Russians were to become richer, they would adopt Western drinking patterns, switching from vodka to the gentler pleasures of beer. For the optimistic Khemkas, that made beer the perfect choice: it was like buying an option in Russia's future prosperity.

Picking a sector turned out to be the easy part. As the Khemkas started to try to acquire majority stakes in newly privatized Russian breweries, like Kakha Bendukidze, they began to clash with entrenched red directors. At one brewery, the director used his majority control of the enterprise to dilute the Khemkas' 20 percent stake to just 3 percent, a legerdemain that foreign investors in all branches of the economy would suffer. At another brewery, a factory director who initially had welcomed the Khemkas' interest and offered to assist them in buying his brewery decided at the last minute to buy a 51 percent stake himself.

For Shiv, each of these setbacks was a lesson in the evolving art of Russian capitalism. The Perm Brewery, which the Khemkas acquired in 1992, was a crucial part of the learning process. Although it was the first brewery the Khemkas bought, the Perm Brewery was not an obvious choice. Perm was one of the engine rooms of the Soviet Union's colossal cold war arms buildup. Until 1989, the city was closed to foreigners and a whopping 70 percent of the local economy was devoted to military production. The legacy of that period was still visible when Shiv and I visited in 1996, in the dramatic designs that MiG jets based in the city traced across the skyline every night.

Nevertheless, in typical Soviet pattern, heavy spending on the defense sector left few resources for producing consumer goods, including beer. When Shiv first toured the Perm Brewery in 1991, he was horrified: "It was the biggest disaster I'd ever seen. There were rats running around. There were cats to kill the rats. There was mold hanging from the ceiling like vines. No one was smiling, everyone looked depressed. You needed galoshes to walk around. There were no lights on. It was only operating at 20 percent capacity, and the beer was undrinkable."

Not surprisingly, Shiv crossed the brewery off his list. But his technical team urged him to take a second look. Beneath the mold, the experts said, there was a functional factory. So, the Khemkas began to woo Sergei Mitirev, the Soviet-era director, and the Perm regional government. By June 1993, their efforts paid off, and the Khemkas acquired a 75 percent stake in the Perm Brewery.

Three years later, the brewery's capitalist transformation was well on its way. The walls and floors gleamed with fresh coats of brightly colored paint and plants adorned the corridors. Profits and production standards had improved, too. Production was up by more than 30 percent; the shelf life of Viking, the brewery's beer, had been extended from five days to ninety days; the company was in the black.

A key factor in the brewery's metamorphosis was Mitirev's enthusiastic participation. Having been outwitted and double-crossed by red directors at other enterprises, at Perm the Khemkas set out to co-opt their potential antagonist. Even after their takeover, Mitirev, a jovial, red-faced, barrel-chested manager of the old school, still enjoyed all the pomp and circumstance of the old industrial class. He retained his title, his long, narrow office the size of some pre-revolutionary ballroom, and an antechamber staffed with two heavily made up, bored-looking secretaries, whose chief occupations seemed to be watching soap operas and humiliating unimportant visitors.

Better still, life with the Khemkas had brought Mitirev a whole new set of perks. He had been taken on tours of state-of-the-art breweries in the West. He and the four other Soviet-era managers of the Khemka breweries were sent on company-sponsored group vacations to the tropics. And Mitirev had been given shadow stock options—bonuses linked to the company's performance—which would probably make him a very wealthy man.

"We honor them, we make sure they are well off, we give them performance-based bonuses," Shiv explained. "All of our directors should become millionaires in dollar terms."

But what the Khemkas were careful not to do was give the old directors unchecked financial authority. A few doors down from Mitirev's status-symbol office was a cramped room, full of foreign men in suits perched over notebook computers. There were no dragon-secretaries guarding the entrance to this room and it lacked the long, rectangular dark-wood power-meeting table, which no self-respecting Soviet manager can do without. Yet it was here, with the Khemka group's handpicked team of foreign accountants, that the real power resided.

"We have unchecked control of the finances of the company—earlier, there was leakage," was Shiv's tactful explanation.

Perry Moi, the chief accountant, was less oblique. One example of the "leakage" the brewery suffered before tight external financial control was imposed was Mitirev's plan to reface the outside of the plant with granite. It seemed like an absurd gesture—extravagant and impractical—until Moi discovered that the supplier of the overpriced granite was one of old management's best friends.

Instances like this are why the Khemkas, like most foreign investors in Russia, quickly learned to distance Soviet-era managers from the money side of their businesses. But they did so as tactfully as possible. For one thing, Mitirev's technical expertise and knowledge of the company's workforce helped to keep the plant ticking. More crucially, as a former member of the regional *nomenklatura,* Mitirev was plugged in to the local establishment. For the Khemkas, his connections were vital, especially when it came to the all-important issue of taxation. Taxes and their cousins, a thicket of government regulations, often determined whether a company turned a profit or suffered a loss. But the level at which taxes were levied, and the rigor with which regulations were imposed, was more a question of politics than economics.

It was, as Shiv put it, "a very interactive process." And in this process of interaction, Mitirev's cooperation was a huge advantage, ensuring that the brewery was still seen as part of the local power structure, rather than as a foreign cash cow to be milked for all the money the provincial authorities could extract.

Mitirev's local contacts proved useful in another respect. Perm's bloated, underemployed defense plants hugely complicated the region's efforts to adapt to the market economy. But they became a useful local resource for the brewery. Mitirev and the Khemkas persuaded a Perm factory that used to produce shells to turn its expertise to building brewing equipment. The results were excellent, and at just one fifth of the price of imported machinery.

The Khemkas hoped to do more than harness the expertise of Perm's arms manufacturers. The key to reviving their decrepit brewery—and the Russian economy as a whole—was, Shiv believed, to recapture the vigorous, sweating enthusiasm that had powered Russia's transformation from European hinterland to cold war superpower. "What we have to do is turn the cold war drive to succeed into a business drive," he told me. "When you come out to factories like this, and see the change which has been accomplished in just two or three years, you can see that that is beginning to happen. To me, it gives me the feeling that market reforms will work."

We concluded our visit to the brewery with the obligatory feast, including vegetarian dishes especially prepared for Shiv. Mitirev made the final toast, in the effusive Russian tradition: "We used to be one of the worst breweries in Russia, and all the defense factories looked down on us. But now we pay our wages on time and when we go to trade fairs we are respected, even feared. Everyone knows Viking beer and everyone knows it comes from Perm. Soon, Russia will get richer and people will drink more Viking."

We all raised our glasses of the reddish Viking brew—except for Shiv, who toasted the plant's success with mineral water.

THE RED DIRECTOR WINS: THE TSAR AND GOD VERSUS THE $100-MILLION-DOLLAR JOURNALIST

The Perm Brewery and ZNGG were the sort of local dramas Gaidar and Chubais had hoped to catalyze when they launched their capitalist revolution. But a far more typical story was one that was played out in Novosibirsk, the gateway to the Siberian steppes, which was dubbed the Russian Chicago when it was founded just over a century ago.

One of the city's chief enterprises was the Novosibirsk Tin Factory, Russia's only tin producer. With thirteen hundred employees and a product that could be readily exported for hard currency, the tin factory was one of Novosibirsk's most attractive companies.

But at the Novosibirsk Tin Factory, the capitalist revolution did not bring in the money and know-how of a foreign investor or a New Russian entrepreneur. Instead, privatization entrenched the position of Aleksandr Dugelny, the factory's Soviet-era red director, transforming him from Party comrade to independent capitalist.

Dugelny was not alone. In a survey of two thousand Russian enterprises, Joseph Blasi, a Rutgers University professor who was part of the team of Western economists advising Chubais and the GKI, concluded that two thirds of medium- and large-sized Russian companies had ended up in the control of their old managers after privatization. This was the great irony at the heart of Russia's capitalist revolution: thanks to the political compromises Chubais had made to push through privatization, the red directors, the aristocrats of the old order, became the biggest beneficiaries of its collapse.

Even though the young reformers had already loaded the legal dice in their favor, many red directors could not resist taking extra liberties, manipulating the power they had enjoyed in the old system to give themselves an even greater stake in the companies they managed. For a few months, the Novosibirsk Tin Factory became a national symbol of this sleazier side of *nomenklatura* privatization. It owed this fleeting notoriety to the efforts of one crusader—Sasha Bekker. A small, thin man, with desperately nerdy Soviet-style glasses, an Old Testament beard, and the neurotic energy of a Russian Woody Allen, Bekker was a Novosibirsk native who had moved to Moscow in 1983 and become one of the country's leading economic journalists and advocates of market reform. He was also a rottweiler of a reporter.

In the spring of 1994, Dugelny and his bureaucratic backers had the misfortune to pass onto the radar screen of this reporting fanatic. The injustice at the Novosibirsk Tin Factory became Bekker's personal campaign, and, within a few months, the factory and its manner of privatization became a national cause célèbre. "I saw Dugelny as an insult to my ideas of honor, of decency, of patriotism," Bekker told me. "He represented all of the people who were preventing us from building a normal economy."

In 1995, Bekker persuaded me to join him on a trip to Novosibirsk to see for myself how the red directors were taking over the new Russia. Our first encounter was with Anna Gumerova, the former head of the factory's securities department. A pretty thirty-five-year-old brunette, Gumerova was as passionate about the sins of the Novosibirsk Tin Factory as Bekker was. As I struggled to stay awake after our red-eye flight from Moscow, the two crusaders explained what Dugelny had done and how they had tried to stop him.

Just thirty-four years old when he was appointed director of the tin factory in 1987, Dugelny had been something of a wunderkind. He was popular with the "workers collective" and was an influential member of the regional establishment: as Gumerova put it, using a Russian colloquialism for the well-connected, he could go to any office in Novosibirsk and "open the door with his foot."

He was progressive, too. While other Soviet factory directors were fighting Gorbachev's tentative efforts to introduce market reforms, Dugelny threw himself and his plant into the transformation. Even before the collapse of the Soviet Union, he was chafing to go further. In 1989, he wrote an article in a Novosibirsk magazine complaining that the market transition was not moving swiftly enough. Why were the *kooperators,* the small private businessmen allowed to set up firms in the late 1980s, the only people who were getting rich? Surely the managers of the country's largest factories, like Dugelny himself, should be getting a piece of the action.

Then the Soviet Union fell apart and Dugelny got his chance. He was such an enthusiastic supporter of the privatization drive that his plant became one of the first in the vast Novosibirsk region to be sold off. From the point of view of the young reformers in Moscow, that made Dugelny one of the rare good guys, a Soviet director who couldn't wait for his factory to be transferred to private hands. "Dugelny wanted to buy state property as quickly and cheaply as he could," said Gumerova, who at the time was Dugelny's economic advisor.

There was just one problem. Dugelny was so determined to sell his plant off quickly, and to make sure that he was its new private owner, that he wasn't about to let mere laws slow him down. He systematically undervalued the factory's assets, making it easier to buy it up, and he manipulated an "investment tender," through which part of the plant was sold off, ensuring the stake went to a company to which he was closely connected. Troubled that these measures might be illegal, Gumerova, who was now running the factory's securities program, began to ask a few awkward questions. But she was young, unconnected, and female. No one, least of all Dugelny, took her seriously.

Then Dugelny launched a new campaign to increase his stake in the factory, and Gumerova's criticisms became impossible to ignore. As we have seen, Russia's mass privatization program granted a generous stake in privatized companies to the rank-and-file laborers who worked there. Dugelny wanted those shares—all together, more than 50 percent of the company—for himself. To get them, he set up a system of carrots and sticks to cajole workers into selling their shares back to a company fund, which he controlled. At the heart of the scheme was a pool of consumer goods, ranging from television sets to stockings, which Dugelny bought using company revenues. Workers were encouraged to trade in their shares for these consumer goods.

Beyond Dugelny's use of company money to increase his own control over the plant, what really infuriated Gumerova were his underhanded tactics. These included not paying factory workers their regular wages, so they had no alternative but to sell their shares to survive. Gumerova began explaining to the factory workers that selling their shares to the company was not their only option. ("To make people real owners, it's not enough just to give them shares; you have to educate them as well," she believed.) But most of Gumerova's fellow employees were still too scared to defy their boss.

"Dugelny had a powerful instrument. He decides who keeps his job and this is especially important in a city like Novosibirsk, when people at so many factories are being fired," she said. "At the Novosibirsk Tin Factory, Dugelny was like a tsar and a god."

By the time I met Gumerova in the spring of 1995, she had been forced out of her job: Dugelny had simply stopped paying her wages until she had had no choice but to leave; she had received anonymous death threats late at night over the telephone; young thugs (she suspected they were sent by Dugelny, but had no proof) had warned her to drop her campaign—or else. . . . But still, Gumerova carried on. Like Bekker, she had begun to see the Novosibirsk Tin Factory as a metaphor for everything that was wrong with Russia's capitalist transformation. With two colleagues, Gumerova found Bekker and tipped him off to the story: "Once he wrote his first article, the state machine began to notice."

Yana Rogozhina, a Novosibirsk prosecutor, began to pursue Dugelny through the civil courts, ignoring pressure from his friends in the local government and condemnation from market reformers in the media, who worried that the furor threatened to block the development of the new economy. At the same time, the organized crime unit of the local police department started to try to build a criminal case against Dugelny; they suspected he had embezzled profits from the export of the plant's tin. Sergei Afanasiev, a twenty-nine-year-old police detective, was in charge of that investigation and his office was our next stop.

The room Afanasiev shared with his partner was on the second floor of a dilapidated fire station. It had all the usual markings of a post-Soviet bureaucrat's habitat—a dusting of paint drifting off the walls, lots of wooden desks crowded into a small space, bulky, ancient telephones—but with a cops-and-robbers' edge: a few pistols, resting casually in their holsters, lay on one desk, and a topless pinup girl giggled into the room from a poster in the corner.

Afanasiev matched his slightly louche environment perfectly. He was tall and dark with the razor-sharp cheekbones and brooding look of the Russian steppe. When he wasn't sucking on a vile, locally made cigarette, he was playing with his lighter—a bright-red bit of plastic adorned with a drawing of a busty brunette and the word "Lolita."

By tracing the trail of metal leaving the Novosibirsk Tin Factory, Afanasiev had found several firms that, he alleged, Dugelny was using as dummy companies to conceal his profits abroad: one in Liechtenstein, one in Singapore, and one in the United Kingdom. Since 1990, when the factory became a leased enterprise and was allowed greater room for maneuver, Afanasiev alleged Dugelny had skimmed off more than $2 million.

Afanasiev wasn't surprised by the sordid turn privatization seemed to have taken. "The ideas were good on paper, but when they began to be applied in real life they took the Russian path, and we know what that means—Russians steal." But he was worried by it. His biggest fear was that the current injustices would lay gunpowder trails for future social protests, and that is why he was so committed to righting what wrongs he could now.

"My job is necessary to prevent a new social revolt," Afanasiev told me. "Already, some nationalist politicians are saying to the people—look boys, you were robbed. It is very sad that our New Russians do not understand this."

Predictably enough, Afanasiev's bosses in the regional government and in Moscow did not share his zeal. But he was undeterred: "The time has passed when all it took was a telephone call to stop our work. Look, our country is in an absurd position. We are begging for $6 billion from the IMF, when twice that amount of money, from places like the tin factory, leaves the country as capital flight every year."

The next day, I went to see the man Afanasiev was trying to stop: Dugelny. After a day of denunciations, it had been hard to imagine Dugelny as anything but an ogre. Yet, in the flesh, he was charm itself. A vigorous forty-two-year-old with a thatch of graying hair, Dugelny looked modern, but not too modern. His sharp suit and mobile telephone distinguished him from those hard-core red directors who still clung to the personal accessories of the Soviet era. But he wasn't suspiciously flashy, either, at least not by the over-the-top standards of the New Russians.

His spiel matched his look. Dugelny saw himself as a forward-thinking, reform-minded manager, one who had had the courage and the insight to support privatization from the outset. He may have bent a few rules along the way, but so did everyone else. The campaign against him, he believed, was motivated by nothing more noble than envy. "For other directors, privatization was a tragedy; for me it was an opportunity," he told me proudly. "I made only one mistake—I lived in euphoria about the change in our country, the new developments. I didn't count on the fact that the old mentality of envying and opposing those people who achieve more remains and that my success would attract enemies."

Now that those envious enemies had materialized, Dugelny was fighting back. His strongest argument against the policemen, prosecutors, and journalists accusing him of privatizing the plant illegally was the one that, sotto voce, was being made by some of the young reformers in Moscow. All right, Dugelny said, even if, for the sake of argument, I admit to having broken a few laws, what difference does that make now? The privatization process is finished and to begin questioning its legality is to open a Pandora's box of legal and political problems.

"What is the point of all of these court hearings?" Dugelny asked me. "The factory has been privatized. How would the state benefit if it were renationalized? To do that would be against the interests of society, against the interests of the shareholders, and against the interests of the whole new market economy we are trying to create. Since the beginning of all of this I've asked, 'What is our goal? To abide by the letter of the law or to create a prosperous market economy?' I ask myself, 'Why did I work so hard, when now they are threatening to take it all away from me?' Maybe I should just immigrate to the West."

I listened to Dugelny's arguments with a growing sense of unease. He was probably the greedy bully his opponents had described, but I had a queasy feeling that he might have a point. Enriching red directors like Dugelny had been the political price the young reformers had paid, part of the social compact they had struck with the old Soviet elite. Dugelny was acting within the confines of that unofficial deal. His sins had been venal and, in a country that lost billions of dollars a year in capital flight, if he had pilfered, it had been on a relatively petty scale. Dugelny was a rather sordid poster boy for Russia's capitalist revolution—but he was probably an appropriate one.

Eventually, the legal case provoked by Bekker's articles made it up to the highest stage in the Russian appeal process. When it got there, the courts and the procuracy finally balked. Dugelny and the management of the plant were found guilty of violating several laws, but the federal authorities decided it was too late to do anything about it. The factory management paid a token fine—whittled down to almost nothing by raging inflation—and Dugelny kept his majority stake.

"He is now more entrenched at the plant than ever," Bekker told me after the final decision. "He fought like a lion for his property and he won."

After Bekker's years of fanatical obsession with the factory, I assumed he would be depressed. The red director and his backers had triumphed. It seemed to be a personal defeat for Bekker and a bleak omen for the fate of Russia's market reforms as a whole. To my surprise, Bekker saw the whole episode as a source of hope: "It proved to me that Russia is not a lost country. That if a journalist writes an article, it can force the most powerful state institutions, like the regional property committee, the procuracy, the civil courts, the Ministry of the Interior, into action. We turned on the legal machine. It was only at the final stage that we lost."

Bekker's optimistic spin astonished me. Privatization had triumphed, but it was increasingly moving out of the control of the young reformers and becoming the province of the old elites. And it had become disconnected from the liberal political revolution—the rule of law, antimonopoly regulations, shareholder rights—that was vital if the change in ownership was to create a functioning, prospering economy.

Before long, Russia's two huge transformations seemed destined to clash. Once ordinary Russians realized that the promised market revolution had effectively been a transfer of assets to the hated apparatchiks, and that those apparatchiks did not seem particularly good at running their new property, how would they vent their ire? Would they use their new political freedoms—the vote and a freer press—to back the young reformers in a push for a second wave of market liberalization? Or would they turn their backs on liberal reforms, both economic and political? The moment of truth was not far off—parliamentary elections were scheduled for December 1995, and there would be a presidential race in 1996—and both the Kremlin and the young reformers were beginning to worry that Russia's political revolution would devour its capitalist one.

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THE OLIGARCHS: THE OUTSIDER, THE APPARATCHIK, AND THE BLUE BLOOD

Nowadays, in the West, the biggest money is nerdy, so cerebral you can hardly see it. It wears Gap clothes, operates from a featureless cubicle, and is so busy working 24/7 on the latest internet IPO it has very little time left for conspicuous consumption. The seven Russian businessmen known as the oligarchs are a different proposition altogether. To understand them you have to go back to the 1980s, to Reaganomics, greed-is-good, and the Masters of the Universe, to a decade in which bigger was always better, no bonus was ever obscenely large enough, and the best CEO was the one who could be persuaded to bet everything on an absurdly leveraged management buyout.

The Russians have the same machismo, the same killer instinct. They think—in fact, they know!—they are smarter, ballsier, luckier than anyone else. They have the same swagger, the same if-you've-got-it-flaunt-it mentality. The oligarchs wear $100,000 wristwatches and their wives wear $100,000 fur coats. They travel in motorcades of armored Mercedes and Jeeps, employ small armies of bodyguards, and maintain a collection of homes. They spend $1 million on a birthday gift for a helpful politician as casually as you or I would send a card to a friend.

Many of Wall Street's Big Swinging Dicks or Silicon Valley's Micro-Midases are richer and exert greater global influence than the oligarchs, but the Russians are tougher and, in a perverse way, more impressive.

The thing about the oligarchs, what makes them so cocky and so cruel, is that they are the victors of gladiators' capitalism. In the West, capitalism is a game played with a safety net. Would-be entrepreneurs who never quite make it rarely suffer anything bleaker than life in the lower middle class. Successful businessmen who break the law, cross the wrong rival, or go bankrupt might, in the worst-case scenario, do a little bit of time in a country-club prison.

But in post-Communist Russia, trying to become a capitalist was more like being trapped in *Logan's Run.* Like the deadly society in the 1976 science fiction movie, capitalism in the new Russia was a contest everyone in the country was forced to enter. In the film, the losers die. In Russia, they were usually left alive but condemned to a life of grinding poverty. And even the lucky few who made it really big and became oligarchs still always felt at risk: Maybe the Communists would storm back into power and execute or imprison the wealthiest businessmen, as the Bolsheviks had done in the 1920s. Maybe a political enemy would take over the Kremlin and arrange for the arrest—and perhaps a jail-cell heart attack?—of an oligarch he hated. Or maybe a rival businessman would have better luck with that car bomb, which, last time, killed the chauffeur and totaled the Mercedes but left the targeted oligarch unscathed. The rich have always been different from you and me, but in Russia the biggest difference was that they were more scared. They were always looking for the emergency exits. As I got to know a few of the oligarchs, the question they asked me most often was whether it was easier to immigrate to Canada or the United States. No amount of money and no number of musclemen was ever enough to make them feel safe.

Maybe that perpetual sense of insecurity was behind the biggest difference between the oligarchs and their Western counterparts: the oligarchs weren't just businessmen; eventually, they also became politicians. At times their influence was so great it would not be an exaggeration to call them a sort of unofficial capitalist politburo. Usually, their power was malign. The oligarchs, and the intimate links between their corporate interests and their political ones, became a metaphor for all of the corruption and insider deals that deformed Russia's young capitalism. And they themselves organized the biggest, most distorted, insider deal of all.

This chapter, and the next one, tell the stories of the five most important oligarchs during their early years, before they became oligarchs.

THE OUTSIDER—MIKHAIL FRIEDMAN

Most of the oligarchs are the business equivalents of Bill Clinton, men born believing they were destined to lead and determined, from the very earliest age, to do whatever it took to make that prophecy come true. Mikhail Friedman is an exception. A stocky man with a sallow complexion, a square-jawed, slightly pudgy face boyish enough to belong to a twelve-year-old, and an impish grin, Friedman grew up a long way from power and he thought that was where he would stay.

Born in 1964, Friedman was raised in Lviv, the beautiful but decaying western Ukrainian city that was forced into the Soviet Union only in 1945 and spent the next five decades desperately trying to pretend the USSR didn't exist. Ukrainian fighters prowled the local forests taking potshots at the Soviets until well into the fifties, and western Ukrainians accounted for nearly a quarter of the USSR's political prisoners. Poland, with its freer speech and relatively vibrant civil society, was only forty miles away.

In an environment like that, feeling like an outsider within the larger Soviet system was the norm. Friedman grew up listening to Radio Liberty broadcasts in the family kitchen and with an almost instinctive awareness of the absurdities of the Communist system. People like him naturally gravitated toward the sciences, which demanded less mouthing of political orthodoxies than other disciplines. Luckily, Friedman loved math and physics and was very good at both.

But he was too much of an outsider to get into the MIT of the Soviet Union, the Moscow Physical-Technical Institute (MPTI). For one thing, he was Jewish, and in Friedman's experience Soviet anti-Semitism "was absolutely obvious—no one announced it to your face, but no one ever really bothered to hide it, either." He was also a nobody, the son of obscure provincial engineers without enough *blat,* or connections, to overcome the blackball of his Jewish origins. When his second application to MPTI was rejected, he settled on another, less prestigious Moscow school, the Institute of Steel and Alloys, to avoid being drafted.

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Russians call the early 1980s the years of stagnation and that is a pretty fair description of Friedman's quality of life as an out-of-town student in the Soviet capital. His dormitory was squalid; his student grant enough "not to starve," but inadequate to buy new clothes regularly; and the height of glamour was a VCR smuggled into the country by the well-connected papa of a fellow student. The Soviet regime was too senile to be properly totalitarian, but it still had a few repressive teeth left: one of Friedman's classmates was arrested and imprisoned for possessing anti-Soviet literature.

Yet, at least for the intelligentsia, life in the fin de siècle USSR had its compensations. No one had very much money, but no one had to do very much work, either. The result was a whole society that acted as if it had never left college: intense, emotional, time-consuming friendships; endless hours spent drinking tea or vodka and discussing the meaning of life; the avid pursuit of esoteric spiritual or creative interests. If middle-class Russians sometimes seem perversely nostalgic for the Soviet Union, one reason is that the collapse of communism forced them horribly and abruptly to grow up. Even Friedman, one of the biggest winners in the capitalist casino, sometimes can't help but regret the end of those languid years.

"My life was very carefree, just as life was for everyone in the Soviet Union," Friedman told me. "Materially, of course, people did not live very well, but no one had to worry about anything. The main thing, what was really intense, was friends, spiritual interests, books. The relations between people were far more open. People did not compete. There was not the same disproportion or envy. People today are far more stressed."

But even as Friedman enjoyed the mellow life of the late USSR he was one of the people who, inadvertently, began to undermine it. With all the free time that the late Communist state granted to the intelligentsia, Friedman needed something to do alongside his studies. Almost by accident, he found himself running a quasi-clandestine student business. Thanks in part to the pressure of thousands of small, secretive business schemes like Friedman's, in just a few years the slacker lifestyle of the Soviet intelligentsia would be gone.

His first venture was joining the "theater mafia." The basic principle was simple: with their abundant free time, Moscow university students queued to buy theater tickets, then bartered them for whatever they wanted on the black market. The theater mafia had been around long before Friedman's arrival, but he was the first to organize it into what was effectively a proper business. He imposed a clear management structure: every university department had a *komandir,* what Western managers would call a department head. Once a week, the *komandirs* met with Friedman—"I guess I was like the majority shareholder"—to review their business plans. The scheme even offered a sort of flex-time working schedule for its 150 scholar-employees: if they didn't want to wait in line overnight, students could come to take their places in the queue in the early morning and be paid a half salary.

Just as the Russian oligarchs would later do, the student entrepreneurs at various Moscow institutes coordinated their activities, creating a sort of theater ticket cartel. Each theater was assigned to a specific institute—Friedman had dibs on the popular Satyra, on Mayakovsky Square—and the *komandirs* were careful not to tread on one another's territory.

The theater mafia would prove to be a valuable training ground for Friedman. It was his first experience of organizing a business and taught him how to operate in the complicated world of barter deals, which still dominate much of Russia's fledgling market economy. It also brought Friedman together with most of the partners with whom he would eventually form the Alfa Group, the umbrella for his oil, industrial, trading, and financial conglomerate.

But in the 1980s, the most valuable result was that it allowed Friedman to buy his way out of forced exile to the dismal Russian hinterland. After graduation, he was assigned to a compulsory three-year industrial posting in an obscure corner of Ryazan, a province in central Russia he describes as "a cockroach-infested fog." With the barter points he had accumulated through the theater mafia business, Friedman was able to buy the favor of key officials at his institute: "For two years I supplied them with various foods, consumer goods, all sorts of things." Magically, his posting was switched from Ryazan to Elektrostal, a steel mill some thirty miles outside of Moscow.

By then, Friedman had caught the entrepreneurial bug. While nominally working at the mill, he and his friends set up a *kooperativ*, the name for the small, private businesses that were legalized in 1987 as part of Gorbachev's tentative embrace of market reforms. Friedman's business ventures were no longer just a student hobby; they were his full-time, adult job.

His parents and friends were horrified. Before long, Gorbachev's thaw, like every previous liberalization, was sure to end in a bloody crackdown, and Friedman would be executed or imprisoned. The irony of the situation was that while such misgivings were perfectly reasonable, the wise parents turned out to be wrong and the wild son turned out to be right. Starting a private business was risky, but in the topsy-turvy Soviet universe of the late 1980s, not starting one was even riskier. Everything about the Soviet experience had taught people to be cautious, to play it safe. But suddenly, playing it safe was about to become the most dangerous strategy of all.

"In those days, experience played a cruel joke on people," Friedman told me. "Life experience contradicted everything that was happening—and it is very difficult to fight with life experience. As a result, many people in those days reacted very passively. Just as they had always gone to their old jobs, so they continued going to them, right up until 1994, when they discovered that they had lost everything."

Friedman was one of the fortunate ones who, half by chance, half by instinct, chose to risk believing in market reforms. His young *kooperativ* tried everything: a courier service, an apartment rental agency, selling Siberian wool shawls, even breeding white mice for laboratories.

Their breakthrough was windows. One day on the metro, Friedman overheard two engineers complaining about the absurdities of central planning. Their institute had funds left over in its official spending allocation and they needed to use them up or risk having their budget slashed the next year. They also had something they would be happy to spend the money on: washing the accumulated winter grime from their institute's windows. The problem was that their funds were in non-cash rubles, a bizarre Soviet kind of psuedo-money that could be used only in official, business-to-business transactions, not on the street. Their institute didn't know of any such official business that washed windows.

Friedman's *kooperativ* stepped in. Soon business was so good that Friedman persuaded his workshop at the steel mill in Elektrostal to begin producing custom-built brushes for his student brigades of window washers. Within a few months, Friedman was earning ten thousand rubles a month, forty times the combined monthly salaries of his parents.

After that, Friedman and his partners became more ambitious. They moved into the hugely lucrative import trade, bringing in Western cigarettes, perfume, computers, and Xerox machines. Then they hit the big time, exporting oil, a tremendously profitable business given the huge discrepancy between domestic Soviet prices for oil and the going rate on the world market.

Western business schools tell their students the secret of success is to know your customers. In the late Soviet Union it was to know your apparatchiks. Friedman spent more and more of his time befriending bureaucrats. His favorite story is what happened when a shipment of his computers was "arrested" at Sheremetyevo Airport. It was missing a vital piece of paperwork—a document that offered assurances the computers were not being imported for resale. Of course, Friedman admits, that was exactly what his firm intended to do. Nonetheless, they duly supplied the appropriate "lying" document to the customs officials. Still, customs refused to release the computers.

Finally, Friedman drove out to the airport himself and found the head of the customs department. They spent five hours downing shots of vodka. By the end of the session, the apparatchik was so drunk he had to be carried out of the room, Friedman had heard dozens of stories about "the glorious victories of the customs service"—and he was free to take his computers.

The liters of vodka, battalions of charmed apparatchiks, and dozens of creative business ideas eventually bore fruit. By 1991, Friedman and his partners were dollar millionaires. Their business techniques were still primitive—as Friedman admitted, "we were absolute savages." But by the standards of their time and place, they had made it. Although the Soviet Union still existed, "we were already living in a market economy," Friedman said. "We bought at market prices, and we sold at market prices." They had started to live like capitalists in their personal lives, too, taking their holidays on warm, sunny islands abroad, usually Cyprus.

In fact, they were doing so well that when Gorbachev's Politburo appeared to swing back toward reactionary policies in 1991, violently cracking down on democratic protestors in Lithuania, Friedman and his colleagues moved part of their business to Prague as an insurance policy. But by the end of the year the Soviet Union no longer existed, Yeltsin was in power, and the young reformers had launched their market revolution.

Ideologically, Friedman sympathized with the new regime, but he was still an outsider. For him, the young reformers, many of them well-connected sons of the *nomenklatura,* were as distant as if they had been "citizens of the moon." In theory, that shouldn't have been a problem: the young reformers were supposed to be building a fair and equitable market economy. But, in practice, who you knew still mattered.

So, just as he had befriended the Sheremetyevo customs officer, Friedman looked for a way to get close to the new government. His path was bracingly direct—he simply brought in one of the prominent young reformers, an economist named Pyotr Aven, to an executive position within the Alfa Group. Aven was one of the first of the young reformers to cross the line and go into private business. His government connections, together with the shadow economy network Friedman had built up in the Gorbachev era, gave Alfa an entrée into the lucrative Loophole Economy of oil exports.

But even before Aven helped the Alfa team nose its way to the golden trough of government contracts, oil export licenses, and servicing state bank accounts, Friedman was the quickest of any of the oligarchs to spot the other great opportunity: mass privatization. He owed his head start to Alfa's detour into Prague in 1991, where the Czechs were pioneering a voucher-based mass privatization program. Thanks to his Czech experience, Friedman grasped the potential of the voucher scheme in Russia more quickly than many of his rivals.

Before long, Friedman acquired a second strategic advantage. When the bankers from Credit Suisse First Boston went to work for Chubais, organizing Russia's first voucher auction, they did some research for themselves on the side, preparing lists of companies that would be worthwhile investment targets. These lists proved invaluable, almost instantly boosting CSFB to the top of the Russian capital markets. But they also served as a precious blueprint for the Alfa Group, thanks to Mikhail Alexandrov, a young Russian who had worked with the initial CSFB shock troopers and then defected to Friedman's company.

"You have a bunch of multinationals coming to them [CSFB], letting them know what their plans are in Russian acquisitions," explained Charlie Ryan, the young American who set up his own investment bank in Moscow. "This is not a fact lost on little Michael Alexandrov. So Michael very cleverly takes the whole list of Western companies interested in making acquisitions in Russia, quits CSFB, and goes and joins an unknown group called Alfa Bank."

With his list in hand, Alexandrov persuaded Friedman to become the Russian pioneer in the art of "greenmail"—buying large stakes in the Russian firms he knew the big Western multinationals were interested in acquiring, and then selling them for a large profit. The small but growing band of Western bankers in Moscow—even the CSFB team whose research Alfa was using—was impressed by how quickly the Russian group had grasped the essential logic of the first stage of privatization.

Theoretically, aggressive investors like Alfa were supposed to be the workhorses of Russia's market transition, the force that would change how the economy actually functioned—restructuring companies at the shop-floor level, bringing in experienced strategic investors with the money and the know-how to turn the country around, factory by factory. But, in practice, Alfa had a hard time putting its classic idea to work. Most Russian plants were in such terrible shape, and the Russian economy was doing so badly overall, that it was often impossible to lure in the investment and the know-how required to turn factories around.

In the end, Alfa made a little bit of money from its early foray into corporate restructuring, and gained valuable experience. But they did it the hard way. Ironically, Alfa would have reaped greater profits, and needed to do a lot less work, had it simply invested its capital in Russia's grossly undervalued natural resources.

"It turned out that the way to make money was to be incredibly speculative and not to worry about restructuring," Stephen Jennings, then the cohead of CSFB's Russia team, told me. "If they had put that money into Lukoil or Gazprom, they would have earned a lot more money."

Before long, most Russian businessmen, including the oligarchs, would realize that the surest way to build fortunes was not to waste time and energy on the backbreakingly difficult job of changing the way factories were run. The real money spinner was to grab a piece of Russia's vast mineral wealth. That economic epiphany would guide the way Russia's greatest private fortunes were amassed. But for the country itself, it was a most unfortunate reality: with huge and relatively easy money to be made in acquiring Russia's natural resources, the best, most adventurous business talents were diverted from the crucial job of making the productive branches of the economy actually work.

THE APPARATCHIK—MIKHAIL KHODORKOVSKY

Most five-year-olds have crazy, impractical ambitions. They dream of becoming astronauts, rock singers, or ballerinas. Not Mikhail Khodorkovsky. As far back as he can remember, he always wanted to do just one thing—become the manager of a Soviet factory. He was so focused when young on that one goal that already in kindergarten the other children nicknamed him "director," the Soviet equivalent of referring to a kid as CEO.

Most of the oligarchs are flamboyant, larger-than-life alpha males. They dominate every conversation, become the focus of every room. You can imagine all of them chafing at the constraints of the regimented Soviet system, rebelling in big ways and in small ones, until finally the system collapsed and they were free to flex their willpower on a brave new world.

Khodorkovsky is different. He's in his midthirties now and one of the most powerful oligarchs, but meeting him you can still see traces of the obedient little teacher's pet whose wildest childhood dream was to become a Soviet red director. Khodorkovsky has mouse-brown hair, wide, naïve-looking mud-colored eyes, a large face, and geeky, oversized glasses. He has a surprisingly soft speaking voice, a slight stutter, and a smile that is so gentle it is almost wimpish. While most of the oligarchs flaunt their private jets and bejeweled mistresses, Khodorkovsky is determinedly, even boringly, bourgeois. He makes a point of dressing down, regularly wearing jeans to work and putting on a tie only under duress. His favorite restaurant is Maharaja, a Moscow curry house even Western graduate students can afford, and he scolds his wife when she spends too much money on clothes. He is unashamedly uninterested in high culture, preferring Abba and the Soviet crooners of his parents' generation to the Russian classical composers and Western pop stars his wife occasionally forces him to endure. In public with his wife, Khodorkovsky likes to act a bit kitten-whipped, complaining about the starvation diets she imposes on him and the cunning tricks she employs to manipulate him.

Khodorkovsky's emphatically ordinary persona is too consistent to be a façade, but it is deceiving nonetheless. This seemingly unprepossessing man is one of Russia's smartest and most ruthless businessmen. In a company he took over, he installed video cameras in every office to monitor his new employees—and fired more than a third of them when he decided they weren't working hard enough. In one Siberian oil town, some of his workers are too scared to criticize him on the record.

Born in 1963, the year before Friedman, Khodorkovsky comes from a very different background. Khodorkovsky is one of the insiders, a savvy young operator who flourished in the Soviet system and was smart enough to use his ancien régime connections to do even better under the new order. Like Friedman, Khodorkovsky is Jewish and his first effort to fulfill his childhood dream was thwarted by his ancestry. After receiving a degree in engineering from the Mendeleev Institute in Moscow, he had hoped to be assigned to work at a leading defense plant. It was not the most prestigious post on offer to students graduating in his year, but it was the one he wanted because it would bring him closer to his goal. As the top student in his class, the young Khodorkovsky thought he would be a shoo-in for the position. Yet Khodorkovsky's choice was refused: although no formal explanation was ever offered, he assumes that, as a Jew, he was deemed unsuitable for the high-security military plant.

Ironically, as in Friedman's case, anti-Semitism turned out to be a blessing in disguise. It locked Khodorkovsky out of the behemoths of the Soviet system—which were dying—and forced him into the quasi-private sector. Khodorkovsky set up a "center for the scientific-technical altamente multidisciplinar

creativity of young people," a characteristically ponderous Soviet moniker for one of the first officially permitted forms of business activity. Like all of the businessmen who survived the natural selection of that era, Khodorkovsky was a chameleon. His center, whose lumpy name was soon abbreviated to Menatep, became first a *kooperativ*, then a bank as the laws governing private business developed.

Its business activities were equally protean. Khodorkovsky and his group imported computers, a sector that yielded a sixfold profit for every invested ruble; they dabbled* in currency exchange; they sold specialized computer programs; they experimented with the construction business. Like Friedman's company, some of their fattest early profits came from a less obvious business—acting as intermediary for state enterprises, which wanted to convert their useless non-cash rubles into cash or a necessary service.

* meter o nariz

It was a typical pattern for a business started in the mid-1980s. But Khodorkovsky's entrepreneurial evolution was stimulated by one very important competitive advantage: from the outset he enjoyed the patronage and protection of senior Communist Party and government officials. The young Khodorkovsky was the Soviet equivalent of a corporate high-flyer. While studying for his engineering degree, he had diligently pursued a parallel career in the Komsomol, the Communist youth league and training ground for future *nomenklatura* bosses. By the time he graduated, he was the deputy head of his institute's powerful Komsomol committee. Had Khodorkovsky been an ethnic Russian, the next logical step would probably have been to begin climbing the ladder of the most powerful institution in the USSR, the Communist Party. But even though, as a Jew, that path was effectively closed to him, Khodorkovsky's prospects under the old regime were excellent. The Soviet party bosses "respected him, some of them even loved him," according to Leonid Nevzlin, one of Khodorkovsky's earliest business partners.

Even after the USSR collapsed, Khodorkovsky remained adept at winning the trust of older, Soviet-era government officials. While the other oligarchs soon started to swagger, bragging that they ruled Russia, Khodorkovsky was careful to act humble. When Yevgeny Primakov, a sixty-eight-year-old veteran KGB agent, became prime minister in 1998, Khodorkovsky was one of the only oligarchs to establish a working relationship with him. The two men, Khodorkovsky told me, represented alien epochs and outlooks—"we were like a cat and a dinosaur"—but the young oligarch smoothed over their differences with his tactful behavior. "With people of his age I always act respectful and for that reason they always treat me well," he explained.

In the late 1980s, when Khodorkovsky began his experimental ventures in the fledgling market economy, he did so with the blessing of the Communist regime. "To a certain extent, Khodorkovsky was sent by the Komsomol and the Party [into the private sector]," Nevzlin said. Having dispatched their hardworking protégé to build a capitalist beachhead, the Party establishment protected and supported him. The Menatep bank's links with the government were so close that in 1990, Khodorkovsky and Nevzlin were appointed economic advisors to Ivan Silaev, prime minister of the Russian Federation, while continuing to work in their own company. It was a terrific honor: in those days businessmen were marginal figures, barely a cut above muggers, and the Party still ruled supreme. It was also an immensely valuable experience, allowing Khodorkovsky and Nevzlin to acquire that most valuable of currencies: government contacts. A year later, when Gaidar launched his market revolution, Khodorkovsky was perfectly placed.

One of the unintended consequences of Gaidar's reforms was to rip up the old financial arteries that had connected businesses with one another and, under communism, with the government. The ex-Komsomolites at Menatep soon discovered that creating their own network—in effect, privatizing the flow of government money—was one of the most lucrative businesses in Russia's market economy.

Their business started with factories that were having a hard time extracting credits or payment from the collapsing Russian state. Like a check-cashing company, Menatep gave the enterprises their money up front, then collected the payment they were owed from the central government, taking a hefty cut in the process. Before long, Menatep began to perform the same service for regional governments waiting for rubles from Moscow. From there it was a short step to the real Klondike—handling the federal government's own finances, through a plethora of schemes ranging from servicing the fat bank accounts of government departments to becoming a conduit for money that needed to travel from one branch of the federal government to another.

The links between private business and the government that were struck up from almost the first day of market reforms would seem to be the antithesis of the young reformers' goals: cronyist, murky, and a dangerously fertile ground for corruption. But, at the time, things did not look quite that way. The reformers found themselves surrounded by a hostile, inefficient, and endemically corrupt apparat. What could be more natural than to hand over some of the apparat's former functions to the nation's plucky new band of capitalists, young men who belonged to the reformers' generation and shared their mind-set?

For Khodorkovsky, one benefit of these schemes was that they strengthened Menatep's already robust personal network. In each transaction, Menatep won the gratitude of another provincial factory director or the trust of another powerful regional government head, and improved its relationship with the Moscow ministries. The schemes were also hugely profitable. With double-digit monthly inflation, the men at the center of financial transactions could make huge windfalls just by holding up the transfer of money out of a government department's bank account for a few extra days, or delaying repayment of a debt for a few weeks. As one of Khodorkovsky's partners told me, "It was hard not to make money."

Inevitably, that money soon began to color the relationship between the future oligarchs and the state. The businessmen were already millionaires; their peers in government were scraping by on one hundred dollars a month. Before long, entire ministries would be supplementing their miserly state salaries with payoffs from Russia's private businessmen. But the new relationships were about much more than stuffed envelopes, and that was what made them so strong. They were about a whole new network of alliances, based on new friendships, clever arguments, and even ideology. A brand-new system of *blat*—the Soviet-era word for political influence and connections—was being created. Like communism, it was held together not just by greed, but also by its own system of beliefs—only this time, the article of faith was the market economy.

"The young reformers' team was not corrupt," Nevzlin said. "And, because of its intellectual strength, it was a serious barrier in the apparat's effort to make money. But, even then, without any corruption at all, people learned how to push the decisions which were convenient for them through the Gaidar government. Since they loved the market so much, all you had to do was explain to them how your project was so important for the development of a market economy."

The financial schemes Khodorkovsky and his team developed during the first few months of the Gaidar government exponentially increased their capital. Now they had to decide what to do with it. Chubais's voucher privatization gave them the answer. Some of Russia's biggest factories were on the auction block. For Khodorkovsky, it was a precious "chance to achieve my childhood ambition," with some bells and whistles attached: instead of becoming merely the director, now he could be the owner.

Menatep's drive to acquire a chunky industrial portfolio was boosted by cleverly taking advantage of one of the weaker rivets in Chubais's streamlined privatization machine. After the first stage of voucher auctions, the remaining state stakes in enterprises were sold off through a variety of means, including investment tenders. In theory, the investment tenders were designed to help remedy one of the shortcomings in the process: the failure of the first stage of privatization to bring much needed capital into the companies that were sold off. Investment tenders were supposed to fix that, by requiring that potential buyers pledge to make an investment in the company, as well as pay the government cash up front. But, in Russia's volatile market economy, handing over assets on the strength of a future promise was to invite sharp dealings. Rivals allege that Menatep was one of the most systematic, and the smartest, manipulators of the scheme.

"Menatep was very involved in the investment auctions," Friedman claimed. "They used to make very high investment pledges. Then they would back them with Menatep bank guarantees, which would then run out [before the investment had been made]. They had a whole system. They are, to this day, still fighting court cases over this. Gradually, they are losing some of the stakes they acquired [in this manner]. This is how property was grabbed up in our country." (In court, Menatep argued that it had failed to make some of its promised investments only because they no longer made economic sense.)

While Menatep's system for acquiring companies may have been carefully worked out, at least initially, its choice of assets was more haphazard. By the company executives' own admission, Menatep's mass privatization shopping spree was an eclectic, scattershot exercise—they bought everything from a titanium-magnesium plant near Moscow and textile factories to glass factories and food-processing companies. They chose companies because they had a good relationship with their directors, or because their undergraduate training as chemists gave them some expertise in the sector, or because the factories had played an important role in the Soviet economy and they believed they would continue to be significant. But mostly they bought, the way shoppers in any sale do, because prices were at bargain-basement levels, and they knew a deal this good couldn't last for long.

Some of their purchases, such as the food-processing companies, turned out to be complete duds. But, with high inflation washing away the group's mistakes like the forgiving tide sweeping clean a beach, bad buys weren't a serious problem. There was so much easy money in Russia, and the companies were so cheap, Khodorkovsky and his comrades felt the only way to learn whether a particular kind of business worked for them was to buy it.

Gradually, though, through trial and error, Menatep began to pull together what was starting to be called a financial-industrial group, a conglomerate of related industrial holdings and a bank able to provide the factories with financial services. Financial-industrial groups, known as FIGs, soon became the object of desire for every ambitious Russian entrepreneur. Although Western economists were almost immediately skeptical of the logic behind them, they had one obvious advantage: by closing financial operations behind the wall of a single owner, they became more opaque. That brought barter deals, strong-arm treatment of minority shareholders, and avoidance of taxes within the reach of relative newcomers like Khodorkovsky.

Better still, the FIGs, both in theory and in practice, soon acquired their own powerful political patron in the cabinet—Oleg Soskovets, the deputy prime minister and leader of the hard-line "party of war," the Kremlin faction that advocated a more authoritarian style of governance, including the ruthless suppression of breakaway Chechnya. With their emphasis on giganticism and their attempt to bring all the enterprises in a particular sector under the control of a group of cooperating owners, the FIGs reminded some observers unfavorably of the monopolism of the Soviet economy. For conservatives like Soskovets, that was precisely their appeal. Ironically enough, by 1995, just three years after Russia's market revolution started in earnest, the country's capitalist pioneers and its nostalgic political hard-liners began to make common cause.

But while the FIGs found favor with the Kremlin conservatives, the old guard on the factory floor found it difficult to adjust to the reign of the future oligarchs. For all his Komsomol connections, as far as the red directors were concerned, Khodorkovsky was an outsider. He had not climbed his way up the Soviet industrial apparat. Khodorkovsky began to clash with the old management: "We tried to reach agreements with the [old] directors, but eventually we had to fire them. We did not manage to keep a single one. They could not understand that they no longer worked for themselves."

The problem, Khodorkovsky said, was that like Aleksandr Dugelny of the Novosibirsk Tin Factory, the red directors were used to running their plants as their own property. Any extra revenues they could squeeze out, preferably out of sight of the tax man and their own infrequently paid workers, would trot along a well-trodden trail to their own offshore bank accounts. They did not take kindly to the idea that the money should go instead to Menatep: "We told them right away: 'Guys, let's make a deal. We are your partners, we pay your salaries, you will get a share. But you must work honestly.' No one did."

THE BLUE BLOOD—VLADIMIR POTANIN

In 1997, when Vladimir Potanin was at the height of his power—fresh from a job as deputy prime minister, about to announce a joint venture with British Petroleum, and with an empire controlling a purported 10 percent of Russia's GDP—*Euromoney* magazine described him as his country's J. P. Morgan, the Russian equivalent of Wall Street's aristocratic investment banker. The phrase did not quite capture the man Potanin was, but it definitely captured the man he desperately wanted to be.

All of the other oligarchs, even Khodorkovsky, still had a bit of the hustler in them, a bit of the guy who's sweet-talked his way up from the streets to the corner office and still can't quite believe his luck. Most of them could be a little ironic about their success—they flaunted their money with the ferocious gaucheness of men who never stopped worrying they might lose it.

Potanin was different. He was a Soviet blue blood, and he was convinced he would become a capitalist one as well. He never had to barter theater tickets or drink vodka with airport customs officials; he went straight from a promising Soviet career to a \$300-million bank. While the other oligarchs were still decorating their offices with leopard skins and mirrors, Potanin was buying graciously battered English antiques. He spoke the best English, hired Westerners first and most aggressively, started doing deals with major Western players the earliest. Potanin aspired to become more than an oligarch; he wanted to lunch in the best boardrooms on Wall Street as an equal, not just as some exotic specimen from the Russian taiga.

Potanin looks like a quintessential Russian, only healthier and in better shape. He has pink skin, a pug nose, blue eyes, and sandy hair. He is trim and moves with the coiled grace of an athlete. Give him an extra six inches (Potanin is five foot six, on a good day) and he could walk into one of the worker-hero groupings of statuary so favored by Soviet socialist-realist artists and not look out of place.

The son of a senior Soviet foreign trade official, Potanin, who was born in 1961, spent his childhood following his father to overseas postings, including New Zealand and Turkey, an almost unheard-of privilege in the cloistered USSR. When he returned to Moscow, it was to attend the prestigious Institute of International Relations, the training ground of the Soviet diplomatic corps. He was born to rule and, with the unselfconscious arrogance of his caste, he knew it. "I was usually chosen as the captain of the team when we played sports," Potanin told me. There was no embarrassed chuckle, no hint of self-deprecation, no body language to suggest, My PR told me to say this, but I realize I sound like an egotistical jerk. "In youth organizations, like the Komsomol, I was always in a leadership position as well. I was good at organizing people."

After graduating in 1983, Potanin began his inevitable climb through the bureaucratic power structure, following his father to work at the Ministry of Foreign Trade. He shone, winning prizes and promotions. By 1989, he was offered one of the ministry's plum jobs: a foreign posting, probably in either Belgium or Canada.

The opportunity to go abroad was one more sign of privilege. Yet, ironically, as the Soviet Union's collapse accelerated, the advantages that had ensured Potanin's advancement suddenly threatened to become golden handcuffs. While the other future oligarchs—many of them outsiders—had been laying the foundations of their market empires, he was building a civil service career in a country that would soon no longer exist.

Just in the nick of time, Potanin grasped the enormity of the changes going on around him. He refused the coveted job abroad and decided to set up his own business instead. At first, Potanin hoped to make up for his late start by leveraging his *nomenklatura* connections into ownership. In 1990, he approached his former bosses and colleagues, urging them to convert their state-owned trading firm into a private company, which would be owned by its own workers and managers.

Potanin's old comrades agreed with his idea in theory, but they couldn't quite summon the nerve to put it into practice. After months of nagging and cajoling and persuading, a frustrated Potanin finally gave up. Instead, he decided to concentrate on his own, small venture: Interros, a foreign trading company whose starting capital was just $10,000 and which had only a handful of employees.

Interros used Potanin's experience and connections in the foreign trade sector to help steer imported consumer goods through the labyrinth of Russian officialdom. At first, its only clients were the minnows of the *kooperativ* economy. Potanin helped Microdean, one of Russia's first homegrown private retailers, stock its expanding chain of Moscow shops with computers and other imported consumer goods. He also worked closely with Oleg Boiko, one of the most prominent private entrepreneurs of the time. But Potanin knew the business could not last long. Microdean and Olbi, Boiko's group, were learning how to negotiate the import maze for themselves. Soon, Potanin and his address book would be superfluous.

More important, like so many of the future oligarchs, Potanin swiftly realized that the real money was to be made in banking. Just as Potanin was beginning to plan this strategic move, he met the man who would make it possible: Mikhail Prokherev, the talented young professional banker who would become his business partner.

For Potanin, the encounter was a godsend; years later he still remembered it with a recall of detail so rich and so tender it sounded almost like the memory of a lover. "It was March 31, 1991, in this very building where my office is now, that we were first introduced to each other," Potanin told me, sitting on the third floor of a dirty white skyscraper, part of a row of cold, virtually indistinguishable towers known as the Russian Wall Street. "When I met Prokherev, everything fell into place. The right man had appeared. When you have an idea, you need to add the man and then everything is wonderful. That is what happened."

Potanin now started working furiously to open up his own bank, wooing young, ambitious sons of the *nomenklatura* like himself from the established state-owned banks and starting to court clients. By the spring of 1992, a few weeks into Gaidar's market revolution, Potanin and his partners had a banking license. But Potanin was still lagging behind Russia's capitalist pioneers. When Chubais launched the voucher privatization program, Potanin reluctantly judged his business too poor and too immature to participate. His company, which eventually became known as the Oneximbank group, missed out both on the profits of mass privatization and on the valuable experience of working with vouchers.

At the end of the year, however, his establishment connections came through with another, even more golden, opportunity. The International Bank of Economic Cooperation (IBEC), the state-owned bank where Prokherev had worked and the alma mater of many of Potanin's new employees, was crumbling under the weight of the Soviet Union's collapse. On the verge of bankruptcy, the IBEC was barred from working with Russian clients, lest they (all of them still state-owned companies) be drawn into its crisis. Someone had to take over IBEC's accounts. What could be more natural than turning them over to those bright young men, most former colleagues, at Oneximbank? They worked in the same building as IBEC, they used the same computer network, and—most important of all—they were part of the same *nomenklatura.*

Those accounts were worth $300 million, a huge sum in these early days of Russia's market transition. All of a sudden, Potanin had his big break. Even in a country where most fortunes were built on the back of government connections, Potanin earned an enduring reputation as the *nomenklatura*'s favorite capitalist, the tycoon who had been appointed by the old elites, rather than making his own way. Years later, he was still a little touchy about it. "Basically, they gave us $300 million," he conceded. "Although I admit that for us it was quite a big boost, at the same time it was not a golden spoon with which we were fed."

Potanin was at least partly right: he and his colleagues did do much more than simply swallow what they had been given. They used their powerful starting position to expand aggressively, focusing on the two areas that Khodorkovsky had already discovered were the most lucrative. The first was to begin moving from the purely financial sphere into industry. Potanin began to build beachheads in attractive Russian enterprises by offering them loans, persuading them to hold their accounts in his bank, and starting to make plans to buy some of them outright.

At the same time, he was pushing into a second lucrative business: handling the government's money. Before long, he had been awarded two of the juiciest accounts—the State Customs Agency, which maintained a regular balance of about $1 billion and yielded an annual profit of about $20 million, and Rosvoruzheniye, the state arms-trading company, which kept "a few tens of millions of dollars" on Potanin's books.

What made the state accounts, especially the customs account, particularly valuable for Oneximbank was that holding them allowed the group to create and control a closed circuit of some of the biggest flows of money in the country. Many of Russia's biggest exporters were Oneximbank's clients and often its shareholders. Tariff and customs charges were among the biggest expenditures these companies faced. But, as money moved from the companies to the customs service, it always stayed on the balances of Oneximbank. Potanin says these "long payment chains" brought the bank revenues of tens of millions of dollars a year.

The state accounts swiftly built Oneximbank, already swelled by the clients it inherited from IBEC, into one of Russia's mightiest economic forces. By 1997, after a spree of industrial acquisitions, *Business Week* estimated that Potanin controlled nearly 10 percent of Russia's GDP, a relative share double that of the Rockefellers at their peak, and more than forty times Bill Gates's proportionate stake of the U.S. economy.

Yet Potanin was adamant that it was cutting-edge market professionalism, rather than good old-fashioned Soviet *blat,* that won the business for his group: "We gave [the state] a high-quality product, which allowed the state to receive its payments promptly and smoothly. But our country is such that people now act as if we stole something. We don't deny that it was profitable for us to do this. But it's absurd to think people should work for the state and not make any money doing so."

Potanin's emphatic justification notwithstanding, the billions of dollars of government money that flowed through Oneximbank began to raise eyebrows. Eventually, even Yeltsin, whose style of governance was marked by a Reaganesque disdain for detail, came to discover that somehow this ambitious banker in his early thirties had become the custodian of a huge piece of the Russian state's assets. In October 1997, at one of his Kremlin meetings with all of the oligarchs, Yeltsin challenged Potanin about the accounts, with a jokey comment that had an iron undertone.

"So, I hear you're living well," Yeltsin told the banker.

"How do you mean, living well, Boris Nikolaevich?" Potanin replied.

"I mean that it's good to have Rosvoruzheniye's money!" Yeltsin shot back.

Irritated and defensive, Potanin raised the stakes: "Yes, and it's good to have the customs money, too. If I had my way, I would keep it all, too, because your *chinovniks* don't know how to handle it."

In retrospect, Potanin was enormously pleased with his quick retort: "I think that Yeltsin expected me to be embarrassed that he knew [about the accounts]. I suspect that he had been briefed and told this was a very shameful thing, that people had said, 'As soon as you accuse Potanin of holding the state accounts he will lower his eyes and say, "Yes, Boris Nikolaevich, I'm ashamed to admit it but it's true. We will immediately give it all back.'"'"

Instead, Potanin triumphantly told me, his own robust reaction brought a smile to the president's lips. But that Mona Lisa grin, one of Yeltsin's trademark political expressions, proved to be a Pyrrhic victory. As time went on, resentment about Oneximbank's extraordinary success at winning government business grew, particularly among the other oligarchs, who were fighting for a piece of the same pie. Eventually, it would provoke a devastating conflict known as the bankers' war.

For now, however, Potanin was riding high. And, in dealings with the Russian government, he enjoyed an important advantage: of all the major oligarchs, only Potanin was a full-blooded ethnic Russian. "Many people [in government] were starting to be troubled by the high number of Jewish entrepreneurs in the country," Nevzlin, one of the founders of Menatep who is himself Jewish, told me. "Vladimir Potanin played on that quite intensively. But the thing was that sometimes Vladimir Olegovich was speaking to people who had hidden loyalties. A mother who was not quite Russian, for example. And so on several occasions we learned what was going on."

For the oligarchs, ethnicity never became the big issue, but it never stopped being a small one. Potanin's ethnic Russian roots weren't the only thing that made him a little bit different from the other oligarchs—sometimes the first among equals, other times the odd man out—but they were always part of the equation.

SEVEN

THE NOMAD AND THE IMPRESARIO

THE NOMAD—BORIS BEREZOVSKY

It was a cold winter morning, but Aleksandr Korzhakov, Yeltsin's bodyguard and best friend, was in high spirits. He had just won a game of tennis, the favorite sport of the president's entourage, and was luxuriating in the strong, hot jets of water spraying down on him in the lavishly outfitted shower room of the President's Club, Moscow's most exclusive club for sports and socializing, founded by Boris Nikolaevich himself.

But as Korzhakov lathered up, a familiar face popped up in the shower next door. Boris Berezovsky had inveigled his way into the President's Club and he was not about to let an opportunity to network with the man the Russian newspapers were calling the power behind the throne go to waste.

"There I am, washing in the shower, but does that stop him? No, all the same he comes in and joins me," Korzhakov recalled.

The din of water pounding against the ceramic tiles might have deterred lesser men from launching into conversation, but not Berezovsky.

"I don't hear half of what he's saying, but he keeps on shouting," Korzhakov told me, still torn between awe and digust at Berezovsky's chutzpah. "Berezovsky never did sports. He came to the club to prevent other people from doing sports. To approach the necessary people with his questions, his affairs, his issues. He uses every person to the maximum. That is his principle of life."

By the time he made it to the elite shower rooms of the President's Club, Berezovsky, who was born in 1946, had already made a fortune with his talent for using people to the maximum. Slight and balding, with lovingly manicured hands and a fondness for larding his conversation with Latin phrases, Berezovsky began his unlikely climb to power as a mathematician.

Like most of the future oligarchs, by the late 1980s he had begun to dabble in the private sector. Like all of them, he built his capitalist fortune using bricks—indeed, often entire walls and buildings—torn away from the decaying edifice of the Soviet state. But, while most of Berezovsky's colleagues and competitors were empire builders, hoping to found business dynasties that would endure for generations, Berezovsky was a corporate nomad. He danced from one venture to another, amassing money and influence along the way, but always eventually pulling up his tent and moving on.

Most of the time, the man whom in 1997 *Forbes* magazine named the ninth most powerful entrepreneur in the world denied outright ownership of any of the companies with which he was associated. He had friends in the management, he offered advice, but he rarely admitted to being a direct shareholder. This setup was perfectly legal and, at least in principle, there was nothing untoward about it; yet, somehow, Berezovsky grew richer and richer. Next to the oil and gas barons, he was probably Russia's most effective rent seeker—and all thanks to a genius for getting close to the right people at the right time and using them to the maximum.

Berezovsky's ladder of personal connections began in the late 1980s, with Vladimir Kadannikov, the director of Avtovaz, the central Russian plant that once manufactured more cars than any other factory in the world. Berezovsky's entrée to the Avtovaz empire was through his first career: his mathematical work designing complex industrial systems. But, with perestroika swirling around him, when Berezovsky traveled to the city of Togliatti and saw the army of shiny, salable Ladas rolling off the assembly line in the thick coniferous forests on the banks of the Volga, inspiration struck. He saw a consumer brand that he could ride to prosperity in the new Russia and he persuaded Kadannikov to share his vision. The two schemes they developed—the Logovaz car dealership and the AVVA investment pyramid—would become the prototypes for the financial and political shell games Berezovsky would eventually parlay into one of the most powerful roles in the country.

The economic sleight of hand that created Logovaz was the same technique red directors and nouveaux riches owners across the country, working with everything from aluminum smelters to paper mills and oil fields, were using to enrich themselves and beggar the state. The basic idea was to separate the profit center—the sale of the actual cars—from the cost center—the production of cars. Logovaz, presided over by Berezovsky and Kadannikov, took over selling the cars and collecting the cash, while Avtovaz, like some ancient dowager encumbered with the debts and crumbling estate while her spendthrift son takes his personal income off to the gaming holes of Europe, was left to pay the workers, pay the suppliers, and pay the state its taxes. In principle, of course, there was nothing untoward about the setup: Logovaz and the thousands of analogous sales companies attached to Russian factories, at least in theory, paid for the product. But untransparent accounting made it easy for the daughter firm to prosper while the mother factory languished beneath a growing mountain of unpaid debt.

What made schemes of this kind particularly ingenious was that the government often acted as creditor of last resort, especially when a mammoth factory like Avtovaz was concerned. Even when Avtovaz was unable to pay its taxes or its workers, it never quite went broke. Time and again, the government forgave its tax debts or issued it cheap loans.

Berezovsky's second wheeze with Kadannikov was AVVA, another controversial but perfectly legal venture. In theory, AVVA was an investment fund set up to build a new model Avtovaz car, probably across the border in high-tech Finland. In practice, AVVA's chief purpose appeared to be using Avtovaz's brand-name recognition to tap into the Russian public's weakness for get-rich-quick schemes.

Every society has its moments of money madness, when a natural discovery or a sudden social fetish throws the entire citizenry into a frenzied pursuit of instant fortunes. In seventeenth-century Holland it was the tulip craze, when a single Viceroy bulb sold for two *lasts* of wheat, four *lasts* of rye, eight pigs, a dozen sheep, two oxheads of wine, four tons of butter, a thousand pounds of cheese, a bed, some clothing, and a silver beaker. A century later, the English were avid subscribers to the South Sea Bubble, a scheme that consisted of supposed trading opportunities in South America. Alan Greenspan has hinted that similar animal spirits could be behind the late-twentieth-century American appetite for internet stocks.

But in the first years of market reforms in Russia, the money madness was probably more fevered than it had been anywhere else, ever before, since it was not just about tulips or South Sea bonds or internet stocks, it was about the entire economy. After decades of Communist subsistence, suddenly it was okay to get rich—but only a very visible minority seemed to know how to do it. After a few months of mute shock, the rest of Russia threw itself into a panicked search for the secrets of their lucky compatriots' success. That made Russians an easy mark for pyramid schemes. Terrific fortunes magically seemed to be in the grasp of anyone with the courage to make a simple investment.

AVVA was one of the first schemes to cash in on this naïve desperation, attracting millions from the Russian masses. For its bondholders, AVVA proved to be a poor investment but, along with Logovaz, it produced Berezovsky's first fortune. By the early 1990s, Berezovsky—who in the Soviet era had had to scrimp to buy winter tights and school notebooks for his children and enjoyed the use of just half a car, sharing it with a friend—was wealthy enough to send his two eldest daughters as fee-paying students to Cambridge University in England and to acquire a glamorous young second wife.

But that was just the beginning. In 1993, Berezovsky decided to raise his game. He would try to apply the technique he had pioneered with Kadannikov in Togliatti to Boris Yeltsin in the Kremlin. "Borya saw how Korzhakov had managed to become the *éminence grise* of the Kremlin," another one of the future oligarchs told me. "And he thought, Am I worse, am I stupider than that barely literate guy? No, I'm not. So Berezovsky decided he would do what Korzhakov had done."

To displace Korzhakov, Berezovsky needed a way into the Kremlin and the Yeltsin family circle. By the end of 1993, he had found one. Fresh from his bloody battle with parliament in October, Yeltsin had written his second book of memoirs, *Zapiski prezidenta* (Notes of a president).

Berezovsky, who had formed a useful friendship with Valentin Yumashev, a trusted Yeltsin family friend who had ghostwritten the president's first book of memoirs, offered to publish the work.

For Berezovsky, Yumashev offered the ideal entrée to the Kremlin. To produce Yeltsin's first autobiography, Yumashev, a cheerful, round-faced thirty-six-year-old who had worked as a reporter at *Komsomolskaya Pravda,* a middlebrow Moscow daily, had been thrown into instant intimacy with the president. At one point, for two weeks the men secluded themselves with Yeltsin's in-laws in a village in the Kirov region in northeastern Russia, wandering through meadows and reclining on haystacks as the president poured out his life story to his amanuensis. When Yumashev recommended Berezovsky as publisher of the second volume of memoirs, the first family trusted his recommendation implicitly.

There was something almost endearing about the amateurish, jerry-rigged nature of the project. Here was Yeltsin, president of an erstwhile superpower, nearly two years after the launch of market reforms, looking for a publisher of his memoirs with all the sophistication of some dottering uncle searching for a vanity press.

But remarkably, the Kremlin's fumbling approach was typical of the Russia of that time. By the mid-1990s, red directors and *kooperators* were already salting away tens of millions of dollars in Swiss bank accounts, yet they—like the rest of the Russian establishment—had only the foggiest notion of how advanced capitalism worked. The idea that most things—say, the autobiography of a president—were products, which could be sold for money to someone who could use them to make a profit—a publishing house, for instance—was still alien. The old regime had operated on connections, not cash, and so, as much by inertia as anything else, the new regime continued to do so, too.

Kadannikov, the key to much of Berezovsky's success so far, again played a crucial role. For the denizens of the Kremlin, Berezovsky was a strange, slightly exotic creature, separated from the beefy bosses of the *nomenklatura* as much by his Jewish intellectual background as by his nouveaux riches success. But Kadannikov was "one of us." He was a good-looking man of Yeltsin's age and caste, and an old acquaintance from the days when they had both been mid-ranking apparatchiks.

For Yeltsin, Kadannikov's participation gave the project a seal of legitimacy, the way membership in a Princeton eating club or a Harvard M.B.A. might reassure a sixty-something member of the East Coast WASP establishment.

"Everyone respected Kadannikov, both Boris Nikolaevich himself and those who were with him," Korzhakov told me. "Kadannikov was very wise and Berezovsky was at his side."

The memoirs were duly published and Berezovsky's Finnish "friendly companies" did the Kremlin proud. The book was rolling off the presses within a few weeks and the color was brighter and the pages were thicker than the washed-out onionskin text that Russian publishers produced. Berezovsky had his foot in the Kremlin door. Because the publication of the book had been not a business transaction but a *nomenklatura*-style personal favor, the act of a loyal retainer, Yeltsin wanted to thank his lieges for their faithful service. The best reward, Yeltsin decided, would be to admit them to the President's Club.

For Berezovsky, whose métier was working his personal connections, membership was a priceless gift. The President's Club was a place for the friends of Yeltsin's heart, not his head. It was where the old gang from Sverdlovsk, the Urals region where he had been party boss, and newer friends—like Shamil Tarpishchev, Yeltsin's tennis coach and beneficiary of one of the great Loophole Economy farragoes, the National Sports Fund—took their ease. More recent allies, men like Chubais or Gaidar, with whom Yeltsin had joined forces for reasons of political conviction or expediency, rather than personal affection, were not invited. Neither, of course, were any of the other future oligarchs, for whom, as Friedman put it, the Kremlin was as far away as Mars. Berezovsky was the only one admitted and he immediately took advantage of his exclusive access to get even closer.

"The [Yeltsin] family would often come to the club to play sports, to swim in the swimming pool, or to use the cosmetic beauty treatments," Korzhakov explained to me. "So Berezovsky now had direct access to them. If Tanya Dyachenko [the president's younger and favorite daughter] gave him her direct telephone number, what could anyone do to stop him?"

In forging an ever closer relationship with the Yeltsin family, Berezovsky continued to be served well by the Kremlin leader's memoirs. Even in Russia, offering a naked bribe to the president was beyond the pale. However, as Yeltsin's publisher, Berezovsky had a legitimate reason to deliver a steady flow of royalty checks to the Kremlin. "'This is from the German sales, Boris Nikolaevich,' he would say one month," one presidential aide told me. "The next month it would be another check, maybe from the sales in Japan."

Only Berezovsky could say whether the royalties were real or padded, and in a way it didn't really matter. All that counted was that Berezovsky had found a legitimate, unembarrassing way of supplementing the Yeltsin family income. Like everyone else confined to a state salary amid the voracious consumerism of the new Russia, the Yeltsins could use the extra money.

Traditional *nomenklatura* perks—cars, bodyguards, country retreats, servants—meant Yeltsin and his clan, like the general secretaries of yore, could live in comfort in Russia without spending a single kopeck. But in the new Russia, that sort of Soviet-style extravagance was no longer enough. Western luxuries—like sending Boris Yeltsin Jr., Tatyana's son, to Millfield, an English boarding school—were becoming de rigueur for the Russian elite, and the president's publishing ventures were the way the first family paid for them.

Thanks to this mutually satisfactory financial relationship, together with Berezovsky's immense personal charm, the entrepreneur's intimacy with the Yeltsin family, if not with the president himself, grew. His allies began popping up in key Kremlin positions, including Yumashev, who by 1997 had been elevated from ghostwriter to chief of staff, a job at least as powerful as the prime minister's.

Cleverly, Berezovsky made a special point of cultivating Tatyana, whose tremendous influence on her father would play a pivotal role in the 1996 elections. In his 1997 memoirs, Korzhakov, by then a poisonous enemy of Berezovsky, claimed the latter won the heart of the president's daughter with generous gifts. "He figured her out quickly," Korzhakov wrote. "Tanya worships gifts. So first Berezovsky gave her a Niva [a Soviet version of a Jeep], then he gave her a Chevrolet."

Before long, Tanya was a frequent visitor to the Logovaz Clubhouse, the former Smirnoff mansion in central Moscow that Berezovsky had lovingly restored as a sort of personal salon. Businessmen and politicians summoned to her office in the Kremlin—disconcertingly done up like a snow-princess boudoir, with white marble walls and flouncy ivory curtains—often found their conversation interrupted by calls from Berezovsky on Tatyana's private mobile telephone. One summer, Tatyana was spotted holidaying with Berezovsky and Roman Abramovich, his business partner (a man who would eventually emerge as a Kremlin power broker in his own right) on Berezovsky's yacht in the Mediterranean.

"As for my relations with Tatyana," Berezovsky coyly told me, "I know her very well, although I meet with her quite rarely. I very much hope that my advice to her is helpful."

Soon, Berezovsky began to use his new personal network to expand his business interests. He first took aim at ORT, the state-owned national television company. By then, television had become a lucrative business in Russia. Starved of consumer goods under communism, Russians were shopping with a vengeance and television was the best way to reach them. More important, in Russia, with its huge swathes of steppe and tundra, feeble civil society, and tabloidish regional press, national television was the key to political power. The airwaves would make the next president, Berezovsky realized early on. If he controlled them, they could transform him from a jumped-up car salesman into a kingmaker.

So Berezovsky set about convincing his new friends in the Kremlin that it was in the president's interests for him to control ORT. Korzhakov, who, in a Russian illustration of the Peter Principle, had climbed to a position of political power that far outstripped his intellectual resources, was a particularly soft target.

The problem, Berezovsky explained to Korzhakov and other paranoid Kremlin apparatchiks, was that the emancipated Russian media had taken Gorbachev's glasnost and Yeltsin's democracy too far. The president was under attack from all sides, particularly from NTV, the private television company established by Vladimir Gusinsky, another future oligarch. The only solution was to create a well-financed, robustly pro-

Yeltsin television station, and Berezovsky promised to do just that if he were given control over ORT. He pushed his plan with characteristic relentlessness.

"They [Berezovsky and Yumashev] began to break me," Korzhakov recalled. "Me and Ilyushin, the [president's] senior aide. Gradually, we said to them, All right, prepare the documents, we will study them and think how it can be done. It was a state-owned channel and to suddenly make it private seemed somehow...unethical. We had to think how to make it look nice. That was one thing. The other thing that was frightening was the financing of that channel."

Berezovsky assuaged these concerns with his usual indirect approach. He wouldn't seek outright ownership—51 percent of ORT would remain in the hands of the state. Instead, he and a group of other "well-off people" would take over the remaining 49 percent, finance the station, and ensure it took a pro-Yeltsin line. By cleverly placing his own people in key positions in the company, before long Berezovsky controlled the station as surely as a majority owner, but without the full burden of financial responsibility.

A year later, the full genius of Berezovsky's conquest of ORT would be apparent. Claiming he needed more money to properly fund the television station, he persuaded the Kremlin to hand him control of another state-owned company at a knock-down price—this time an oil company.

But in 1994, Berezovsky had not yet become that voracious. Instead, he hit on another idea. Around him, other future oligarchs were perfecting ways of enriching their companies by diverting government monies through their own accounts: Potanin had the customs accounts, Khodorkovsky's Menatep had dozens of smaller deals. Berezovsky decided he would make a play for Aeroflot.

The national airline was a clever choice. Thanks to its international routes, it had a steady flow of hard-currency income, some of it paid in cash. And Aeroflot was also a good way to bet on Russian market reforms—if the country grew more prosperous, airline traffic would take off. In fact, taking over Aeroflot, or at least its accounts, was such a good idea that Berezovsky was not the only one who came up with it. Gusinsky, a former theater director turned banker and media mogul, wanted the accounts, too.

The two entrepreneurs had already begun to clash on the airwaves, with Berezovsky bad-mouthing the political line taken by Gusinsky's NTV to score points for himself in the Kremlin. With Aeroflot, the struggle intensified. "Berezovsky at that moment entered into a very fierce conflict with us," Sergei Zverev, one of Gusinsky's senior executives, told me. "Eventually, either one or the other had to triumph."

Gusinsky decided he'd try to cut a deal. The two men held several meetings at which Gusinsky offered to compromise and described to Berezovsky the plan he had worked out for restructuring Aeroflot. Berezovsky heard him out attentively, then shook his head. The wheels of the apparat had already been set in motion, Berezovsky explained, and it was now too late to stop them: "Whoever wins, wins."

Initially, Gusinsky thought he was winning—a government resolution was even passed formally appointing him Aeroflot's banker. But he didn't hang on to the juicy accounts for long. Just as the conflict reached its peak, Sasha Bekker's story about the Novosibirsk Tin Factory was published. The article had tremendous repercussions in Moscow, thanks to one of the more creative maneuvers of Dugelny, the plant's director. To make sure state officials backed his privatization scheme, Dugelny gave everyone who mattered in government, from local KGB agents to central bank economists, free tin factory shares. The recipients of his largesse included one very powerful Moscow minister—Soskovets, the leader of the party of war.

When Bekker revealed this fact on the pages of *Segodnya,* a newspaper owned by Gusinsky, Soskovets was outraged. The article did so much damage to Gusinsky's links with the government that Bekker was nicknamed the $100-million journalist, because that is what his articles cost his employer in lost business. The first casualty was the Aeroflot deal. An infuriated Soskovets sent an aide to tell the Aeroflot board that the Russian cabinet had considered the matter and recommended that Avtovazbank, a company linked to Avtovaz and Logovaz and closely connected to Berezovsky, should handle the Aeroflot accounts.

The board members of what was then still a state-controlled company knew better than to disagree. The Aeroflot accounts went to Avtovazbank and Berezovsky became the airline's not-so-hidden puppeteer. Before long, a number of Berezovsky allies were installed in key posts, including Valery Okulov, the husband of Yeltsin's elder daughter. Berezovsky had perfected his technique: "As for Aeroflot, I have no financial interest in it," he told me. "I have no Aeroflot shares. I have, at times, taken an interest in what happens at that company and I have a lot of people who used to work with me who now work with Aeroflot, which I think is very good."

Swiss authorities would later allege that Aeroflot's hard-currency receipts had been systematically misappropriated, to the tune of at least \$200 million, through Andava and Forus, two Swiss-based companies that ostensibly provided the airline with financial services. But, thanks to the Kremlin connection—Aeroflot had, after all, become the Yeltsin family firm—inside Russia, the airline had political Teflon. No matter what machinations investigators uncovered, they could never seem to make them stick; Berezovsky dismissed the allegations as a political campaign to discredit him. (In early 2000, Swiss and Russian prosecutors were still investigating the Aeroflot affair, but all personal charges against Berezovsky had been dropped.)

With his victories at ORT and Aeroflot, by the middle of 1994 Berezovsky had clawed his way out of the provinces. He was in the big leagues now. But his new prominence came at a price. In the summer of 1994, his Mercedes was blown apart by a bomb. He survived, but his chauffeur was killed.

The violence shocked the future oligarchs. All of them admitted to sharp practices, but the one line they prided themselves on drawing was not resorting to physical violence against one another. That was the purview of the petty hustlers of the hinterland, the ex-con mafiosi, or a few fiercely competitive sectors like the metals trade. The attack on Berezovsky suggested that the one rule of big business in Russia was starting to blur.

Russia's future oligarchs were scared. Most of them already had their own bodyguards, but now they began to hire musclemen to shadow their wives and children. More and more started to send their families to live permanently abroad. In their anxiety, old rivalries seemed to melt away. Even Gusinsky rallied round. The day after the explosion, in a show of solidarity, he and Zverev went to visit Berezovsky. A few days after that, Gusinsky lent Berezovsky an armored Mercedes to use while the latter waited for a replacement for his old, shattered car.

The rapprochement did not last long. By the end of the year the two men would be locked in their bitterest conflict yet. This time it would be a battle that would go beyond their personal business interests to threaten Russia's fragile post-Communist democracy.

THE IMPRESARIO—VLADIMIR GUSINSKY

Going to see Vladimir Gusinsky always made me nervous. Not because he was mean (although he could be) and not because he hated me (although occasionally he did), but because he was so damn unpredictable. One moment he would be all jokes and bonhomie and bear hugs, deciding to be interviewed over lunch in a trendy restaurant and bringing his vivacious wife, Lena, along. But the next minute, or the next time, he would be in a rage, furious and Olympian. Once he began an interview with a full-fledged Russian tirade—yelling, purple faced, arms pounding the air for emphasis—accusing me of misrepresenting him in particular and Russian businessmen in general. Then, in a flash, he subsided. "It's okay, Chrystia," he said with a wink. "I know it's not your fault, I know there is a wider conspiracy against me in your company and I know you can do nothing about it." When I tried to contradict him, he looked at me pityingly, but kindly: I was obviously too young and unimportant to have been let in on the corporate plot.

It wasn't just me; Gusinsky acted the same way with everyone. His employees always breathed a sigh of relief when he went on holiday: they would have a respite from the tears and screams and generally living life in fast-forward. Even on vacation, Lena told me, he couldn't let up. For Gusinsky, the stress, the high drama, the constant conflict, were an addiction, and after seventy-two hours away from it all he would go into withdrawal, usually quite literally getting sick.

The best word for his temperament—with all his volatility, his passion, and his mania for control—is operatic. It's a description that is especially apt because in his past, Soviet life Gusinsky was a theater director. Even after he left the stage to become a *kooperator* and later an oligarch, Gusinsky never stopped being a larger-than-life, theatrical figure, always convinced that, God-like, he could control the action from his director's chair.

Gusinsky even looks like a theater director, of a particular kind. He's not one of those European auteurs, all angles, irony, and shabby-chic clothes. Instead, Gusinsky looks more like a Las Vegas impresario, the old-fashioned kind. He's a little flashy—he used to wear a huge diamond pinkie ring, until his PR chief told him not to—and his wife, whose tongue is as sharp as her manicure, favors leopard print and leather. Gusinsky is neither tall nor heavy, but he seems big. He has an outsized, square face, a color so high it is almost aubergine, and dark chocolate hair and eyes. He wears large, ugly, rectangular glasses, but his expression is so mobile you don't really notice them.

Like every Russian of his generation, Gusinsky belongs to a family that was battered on the Bolshevik anvil: in the 1937 purges, his maternal grandfather was executed and his grandmother was imprisoned in a labor camp. Gusinsky was born just as the terror was abating, in 1953, the year of Stalin's death. As a boy, Gusinsky wanted to be a physicist, but, like so many of the oligarchs, he was rejected from his chosen university because of his Jewish background. Instead, he studied engineering at a more humble institute. But by the time Gusinsky graduated, his plans had changed: he got a degree from a Moscow drama school and began to stage plays in a few provincial theaters.

Then, one cold, gray February day in 1987, Gusinsky decided to change his life again. All at once, he was fed up with the obsequiousness, the compromises, the petty politicking of life on the Soviet stage: "I suddenly thought to myself, goddamnit, I am so sick and tired of it all." He decided to try his hand at business.

The dramatic decision, the willingness to turn his life upside down based on a moment's ennui, was trademark Gusinsky. We tend to think of Russians as fearful stoics and that is what both communism and tsarism taught most of them to be. But Russia has also always had its wild men: the *skoptsy*, Orthodox religious fanatics who castrated themselves in the name of God; the escaped serfs who fled to the freezing freedom of the Siberian forests; the dissolute aristocratic gamblers who gave us Russian roulette. Gusinsky, like most of the New Russians, was a throwback to this freewheeling tradition.

"I've always had a healthy streak of adventurism in my character and a certain feeling of being bulletproof. All idiots and madmen probably feel the same way," Gusinsky once told me. "I always risk everything. A man must regularly, every five to seven years, change his life. If he doesn't do that, he becomes internally boring. Girls stop loving him, and his own children stop respecting him. Even dogs no longer come up and sniff him. Don't laugh, it is true—a man must be loved by women, children, and dogs. Those three categories are the essentials of life."

As a struggling entrepreneur, Gusinsky had plenty of scope to indulge his love of risk. He tried everything: driving a gypsy cab, hawking blue jeans on the black market, trading Western cigarettes. His first success was copper bracelets, the 1980s Soviet equivalent of New Age crystals. Vaguely connected with the ill-digested Eastern philosophies then in vogue, copper bracelets were popular as a putative defense against high blood pressure and general ill health. Gusinsky figured out a cheap way to make them, using the copper wire from broken-down streetcars. In exchange for a few bottles of vodka, he could get spools of it, enough to make hundreds of bracelets. He was rich enough now to move into the bigger leagues of construction and real estate.

It was in these early days of eclectic business activity that Gusinsky struck up his first important political friendship, meeting Yuri Luzhkov, a mid-ranking Moscow bureaucrat who would later become mayor and one of Russia's most powerful politicians. As Luzhkov, a small, muscular man, with a bald, bullet-shaped head and boundless energy, grew more powerful, Gusinsky prospered with him: Gusinsky's construction company got city jobs, his real estate firm had an easier time than most getting city land and permits, and Luzhkov even let Gusinsky, who had been working from a basement in a suburban factory, set up his headquarters in Moscow city hall.

Gusinsky's real breakthrough came when he realized that the city of Moscow's most valuable resource was its operating capital. He persuaded Luzhkov to transfer the money from Soviet-era banks to a consortium of commercial banks led by Gusinsky. Up until then, Gusinsky's bank had been a sideline, little more than the accounting department of his wider operation. Now, suddenly, Gusinsky was transformed into a banker of real substance. Many of the oligarchs made their first big fortunes the same way—Potanin with the customs accounts, Berezovsky with the Aeroflot accounts—but Gusinsky had the dubious distinction of coming up with the idea first.

No matter how big his empire grew, Gusinsky would always be a little bit tainted by these early years. He would always be Luzhkov's oligarch, the street-smart hustler who figured out how to parlay a political friendship into a fortune, and cut every corner he had to along the way. What I liked about Gusinsky was that he admitted it. Once they became rich enough to buy their suits in Italy and their investment bankers on Wall Street, some of the other oligarchs started trying to forget they had been spawned by a sordid system; Gusinsky at least had the decency to remember.

"I cannot say I am an absolutely honest man, an example for everyone," he told me. "Nor can any person who survived in this country before 1985, or who built great things after 1985. We all have things that we would not like to tell our children. As we say in Russia, the lucky child suckles on two mothers. There are people with whom you can establish relations and receive a lot."

Like so many of the oligarchs, in the beginning, Gusinsky was a corporate omnivore. In early 1992, when Mikhail Leontiev walked into his office, the latest enticement became the newspaper business. Not even Gusinsky, with his fondness for bold, self-flattering predictions, could have predicted then that by the end of the decade the humble proposal would grow into Russia's dominant private media empire and the healthiest part of Gusinsky's conglomerate, known as the Most group.

Short, dark-haired, bright-eyed, and given to iconclastic opinions, Leontiev was one of the new Russia's most influential journalists. Born in 1958, Leontiev was part of the Soviet baby-boomer generation, which grew up without ever truly believing in communism. He studied economics at one of Moscow's most prestigious institutes, but soon fell out of mainstream Soviet professional life because of what he calls "light dissent activities," the sort of political unorthodoxies that were enough to spoil an official career but too mild to provoke real repression.

As a consequence, Leontiev spent his working days in the 1980s scraping a living on the fringes of the official Soviet economy—for a while he survived by tutoring university students for their exams; later he became a night watchman. But, in his off-hours, Leontiev moved in the intellectual circles that were plotting what would become, in less than a decade, the economic and political transformation of Russia. Before long, Leontiev began to contribute articles to the Soviet Union's increasingly daring newspapers and magazines and, by 1989, he had a full-time job in Moscow's first private daily newspaper, *Kommersant.*

As a reporter, Leontiev took a special interest in the brash, slightly shady *kooperators* who were starting to emerge on the Moscow scene. By the time the Soviet Union collapsed, Leontiev had met, interviewed, and befriended most of the future oligarchs. He became closest to Gusinsky. Soon, Leontiev and Gusinsky were going out together with their wives and children, spending long Sunday afternoons in each other's homes eating and scheming.

In those days, Gusinsky was still a lot closer to peddling copper bracelets and driving a gypsy cab than to advising the Kremlin and jetting around in a private Gulfstream jet, and it was he, as much as Leontiev, who stood to benefit professionally from the new friendship. Leontiev introduced Gusinsky into his intellectual circles and began to put his name forward when, for instance, a visiting World Bank official was in town and wanted to meet some of Russia's budding capitalists.

In the middle of 1992, it was Leontiev's turn to ask Gusinsky for a favor. By then, Leontiev was working for *Nezavisimaya Gazeta,* an independent newspaper founded in 1991, in the heat of the pro-democracy movement. Frustrated with their mercurial editor and their starvation wages, *Nezavisimaya Gazeta*'s top journalists decided to try to set up a publication of their own. They began to canvas Moscow's moneymen to see if they could find a backer. But no one was interested.

Finally, Leontiev was deputized to approach Gusinsky. After long consideration, Gusinsky decided to back the project. One reason was his friendship. Another was Gusinsky's theatrical personality and love of the public stage. Most important of all, Gusinsky was the first of the future oligarchs to grasp how central a role the media would play in the advancement of business interests. All of them, of course, had already discovered that politics and commerce were intimately intertwined. Yet Gusinsky was the first to fully appreciate to what extent in Russia's nascent democracy the political process was not confined to the corridors and saunas of the Kremlin, but extended to its newspapers and television programs.

The first issue of Gusinsky's new paper, christened *Segodnya* (Today) rolled off the printing presses on February 23, 1993. It was an instant success. Gusinsky had the subtlety and his journalists had the professional integrity to save *Segodnya* from becoming the sort of blatant mouthpiece for its proprietor's commercial and political interests that many of the newspapers later established by other oligarchs would become. Instead, *Segodnya* was allowed to become one of Russia's freest, most honest liberal daily newspapers, rivaled only by *Izvestia,* the slightly mustier, but occasionally more authoritative Soviet-era dowager.

Even so, Gusinsky's vested interests did not go unserved. For one thing, although most of *Segodnya*'s journalists were too proud to write *zakaznye,* or "ordered," articles, they submitted to a milder form of censorship. Gusinsky's own businesses were definitely out of bounds. As Gusinsky put it: "My own publications don't write negatively about me. I am the publisher and there must be some limits." Sometimes, the limits would go further than that. Periodically, Most executives would ask *Segodnya* not to criticize some politician or businessman with whom crucial deals, like the bid for the Aeroflot accounts, were being transacted. (As in the case of Aeroflot, the journalists sometimes ignored such requests.)

For Gusinsky, these measures were defensive; he was careful not to use the newspaper as his puppet. It's not that Gusinsky was a champion of the free press, although he sometimes posed as one. But he had a keen interest in preserving *Segodnya*'s reputation. If this paper was credible and influential, Gusinsky thought, then maybe some of its luster would rub off on him.

Even by 1993, as Gusinsky began to become seriously rich, he was finding it hard to shake his image as a slightly shady small-timer. Founding and owning a high-brow newspaper, one committed to the democratic and capitalist values supported by Moscow's liberal intelligentsia, magically transformed Gusinsky into a player, a man whose views counted. At the price of a few million dollars a year—*Segodnya*'s annual losses—it was a bargain.

Later on, as Gusinsky's commercial appetites became more focused, his media interests would become a source not only of image and influence, but also of profit. But in the early, heady years of Russia's capitalist transformation there was so much of what Leontiev called "stupid money" in Moscow, and so many easy ways to make a killing, that running a newspaper as a profitable business simply didn't make sense. When the *Segodnya* team asked Gusinsky to send in some number crunchers to help make their newspaper more economical, he told them it would be a waste of resources. "Think about it," Gusinsky exhorted. "Managing a newspaper is just as complicated as managing a bank, and requires a whole new language. Imagine I take a man, who is currently either making a profit for me or making savings for me of $100 million a year. I send him to work at the newspaper, which is currently costing me losses of $8 million a year. As a result of his work, the losses are cut from $8 million to $2 million. So, what did it cost me—$94 million! What do I need that for? You should all just do what you like. I know you don't steal."

Gusinsky's calculated decision to let *Segodnya* lose money was characteristic of the forces and the logic that shaped the earliest years of Russian capitalism. Western advisors and aid donors unrelentingly counseled Russians to restructure their rust-belt factories and run their new businesses in accordance with the best Western corporate practices. They were frustrated when the Russians failed to heed their advice. But the problem wasn't a lack of entrepreneurial drive or an insufficient passion for money. It was simply that Russia's narrow layer of talented businessmen and managers directed their efforts where they would yield the highest reward. In the early years of Russian capitalism—and to a worrying extent in the later ones as well—that tended to be in exploiting the arbitrage opportunities between lingering Soviet prices and the world market, in buying up cheap state assets, in profiting from the Central Bank's negative real interest rates, and in securing juicy government contracts.

Even after much of the "stupid money" had dried up, *Segodnya* failed to become a major money-spinner for the Most group. But establishing the newspaper was Gusinsky's defining business move. As *Segodnya* swiftly gathered public kudos, frustrated journalists in other media began to see Gusinsky as a potential benefactor. Among them were two leading television figures: Yevgeny Kisiliev, Russia's most popular anchorman, and Oleg Dobrodeev, a top producer.

Both worked for ORT, the state-owned television channel. As 1993 wore on, and the conflict between the hard-line parliament and the president began to escalate, the two men found their journalistic freedoms at ORT increasingly curtailed. They decided to look for a moneyman to help them go private: Gusinsky was the obvious choice.

Their first point of contact with the Most group was Sergei Zverev, an old friend and onetime fellow pro-democracy activist. At the end of May, Zverev invited Kisiliev and Dobrodeev to his office in the Moscow city hall skyscraper overlooking the Moskva River. As the two men laid out their proposal to set up an independent production company, Zverev grew more and more excited. *Segodnya* had been up and running for just over three months, and recently he and Gusinsky had begun mulling over the idea of making a bolder foray into the media business by setting up their own television network. Now, he had two of Russia's top television executives sitting before him.

Abruptly, Zverev called for a break in the meeting. He liked their idea, he told Kisiliev and Dobrodeev, but maybe they should set their sights higher. Why not create not just a production company, but a whole television station? As the two visitors tried to absorb this escalation in their plan, Zverev rushed out of his office to Gusinsky's far grander suite just around the corner. His eyes sparkling with excitement, he burst into Gusinsky's private room and exclaimed: "You know how we were talking about creating our own television station? Well, I have two people in my office who can do it for us. There are no two better men for the job in all of Russia."

Zverev fetched Kisiliev and Dobrodeev, introduced them to Gusinsky, and the four men sat down to a two-hour discussion. By the end of it, what would become Russia's first privately owned television station was born.

"To be honest, when we walked into the building we had no idea about forming an entire television station," Kisiliev, a fair-haired, handsome man with a Walter Cronkite growl, told me. "But we left it with the thought, Why not?"

For the new station to work, Gusinsky knew it needed more than creative talent. It needed a progressive manager, someone hard-headed, politically savvy, and able to swim in the violent currents of Russian capitalism. For Dobrodeev and Kisiliev, the right candidate immediately sprang to mind: Igor Malashenko, the thirty-eight-year-old Soviet army brat, Dante scholar, and former Central Committee ideologue who had worked with them at ORT before being sacked as part of the new, repressive climate at the station. Malashenko, desperate for revenge against the apparatchiks who had kicked him out, jumped at the offer.

Just a few days after that first May meeting, the group went to work. In contrast with *Segodnya,* creating a brand-new television station required serious investment. According to Malashenko, in its first fifteen months of existence the new television company, which was dubbed NTV, the Russian acronym for Independent Television, ate up more than $30 million. Almost all of the money came from Gusinsky (he had invited two other bankers to join him in the project, but they dropped out almost at once).

The biggest challenge was to find a way to get on the Russian airwaves. Initially, NTV struck a deal with a regional St. Peterburg channel and in October 1993 began to broadcast a few of its news programs there. But Gusinsky's ambitions were much higher than that. He wanted to create Russia's first, national private television station. To do that, he needed to be granted broadcasting rights to one of Russia's main national VHF channels, at the time a state monopoly.

In most Western countries, the divvying up of precious VHF television channels is a formal, carefully regulated, competitive process. But in Russia, with its legacy of state ownership and central planning, there was no established system. One thing was clear, though. Only one man had the power to make a decision of such tremendous political, and potentially commercial, significance—Boris Yeltsin. To win the Kremlin's approval, Most set its formidable lobbying and PR machine in motion—drawing on everything from intelligence gathered by the ex-KGB agents in its private security force to friends in parliament and good ties with Moscow journalists.

First, they needed to find a soft target. Dobrodeev suggested Most focus its sights on taking over Channel 4, a mongrel jointly controlled by the two state-owned, national television companies, each with channels of its own. By day, the underfunded channel showed amateurish programs prepared by Russian universities and by night it broadcast cheap shows rejected by the two main state channels.

Next, they needed to refine their arguments. For Most, the battle between the Kremlin and the parliament, which erupted into open street fighting in October, just as the first NTV shows began to appear in St. Petersburg, provided a helpful backdrop. The Most group strongly supported the president throughout the conflict. State-owned television, never completely certain who would triumph and instinctively somewhat sympathetic to the Communist-dominated parliament, was more ambivalent. The contrast helped Gusinsky and Zverev make a powerful case that the Kremlin would benefit from giving Most a channel of its own.

But neither the weakness of Channel 4's programming nor Most's firm support of Yeltsin played a decisive role. What was really crucial, as with all government decisions, was steering the draft presidential decree through the corridors of power, until it landed on Yeltsin's desk with all the signatures of his subordinates reassuringly saluting at the bottom of the page. As usual, Zverev, who served as a sort of foreign minister for the Most group, orchestrating its relations with all levels of government and with other private financial empires, led the campaign.

Zverev began his offensive by nudging the public debate in NTV's favor. "We unveiled a whole campaign in the mass media on the theme that Russia needed independent commercial television," he told me. "There were many articles written and published on that theme, various people spoke out about it, leading television personalities and so forth."

Once the public was softened up to the idea, Zverev began the laborious process of *vizirovat,* or getting signatures on, the draft presidential decree. For two months, he walked the corridors of the Kremlin, drank tea in waiting rooms, lobbied old friends, and persuaded the heads of the two state-owned channels that controlled Channel 4 to back the plan.

Yet, for all Zverev's contacts and cunning, somewhere, the decree was being blocked. Worse still, Zverev had no idea who was blocking it. His breakthrough was serendipitous. One autumn afternoon, Zverev and Kisiliev were sitting in one of the white-walled mansions in the Kremlin complex waiting for a meeting with a presidential advisor. After they had been kept waiting for the obligatory twenty minutes, the advisor's office door was pushed open and they were invited in. Zverev and Kisiliev recognized the man he had been ensconced with—Shamil Tarpishchev, the tall, lean, Tatar athlete who had become Yeltsin's tennis coach and a member of his inner circle.

Nudging Kisiliev, Zverev asked if the television anchorman knew Tarpishchev. He did. "I see that his office is just across the hallway," Zverev told his colleague. "When we're finished here, let's drop by and talk to Tarpishchev about Channel 4."

They did, and in the course of the conversation, Zverev realized it was none other than the infamous tennis coach who was blocking their deal. Zverev couldn't believe his luck. Now that he knew what the problem was, he could try to solve it. Tarpishchev's objection, it turned out, was that he had a plan of his own for Channel 4—he wanted to turn it into Russia's first all-sports network. It was easy to convince him to drop that plan—"Where will you find the funding?" Zverev asked—and even easier to win him over to Most's rival proposal by promising to devote a certain amount of airtime to sports. As ever, Zverev was relying on one important bit of ignorance: like everyone else in Russia apart from the Most group, Tarpishchev hadn't yet figured out that television could actually make money.

With Tarpishchev neutralized, the signature-gathering process picked up speed. By the middle of January 1994, the decree had been signed and NTV was born, with airtime on Channel 4 every night from 6 P.M. to midnight. Like Tarpishchev, the Kremlin hadn't yet twigged to the commercial value of television: Most got the channel almost for free.

"The license, in practice, never cost us anything at all," Malashenko admitted. "The cost was just a few kopecks. It was such a small sum that it wasn't even worth remembering. It was a purely political decision."

As usual—the same was true of government bank accounts, export licenses, and natural resources—the Russian state seemed unable to appreciate that its assets had a market value. And, as usual, the smartest, best-connected businessmen were the beneficiaries of the government's ignorance.

With NTV on air every day and *Segodnya* on the desk of every Russian opinion maker, Gusinsky had transformed himself into Russia's first media baron. He began steadily to acquire new titles and expand into other media: before long his empire would include a newsmagazine, a trashy Russian version of *People* magazine, a radio station, and satellite TV. His real estate and banking deals with Moscow city hall had given him money; his media interests gave him influence. Gusinsky had become what no private Russian businessman had been since 1917—a significant, independent, political force.

As his power grew, Gusinsky began to change. He had always been a volatile, frenetic workaholic. Now he started to become a bit grand. Gusinsky might not yet be opening doors in the Kremlin with his foot, but among Russian businessmen he carried himself as the first among equals. He had always had a weakness for personal ostentation. Now he began to seriously indulge it, buying his private jet and a fleet of ever showier new cars.

Gusinsky now began to make public political pronouncements. In private, he sometimes allowed himself to hint that he had more real power than the faltering state itself. When Tatarstan, an autonomous republic in central Russia, began to clamor for greater independence, forcing the Kremlin into political contortions to retain its loyalty and prompting murmurs of civil war, Gusinsky half jokingly told his partners: "What's all this about Tatarstan? If it's necessary to take care of Tatarstan, I'll send fifty men from my security force and they'll take care of it and that will be that."

For Russia, especially for its government, this sort of behavior was astonishing. The Soviet Union had been a culture of *uravnilovka,* literally "leveling out," a term for the Party's policy of making sure no individual light shone too brightly against the backdrop of the collective. Imperial Russia had practiced something of the same philosophy, with peasants expected to give way to views of the *obshchina*, or "rural community," and with even wealthy nobles expected to assume positions of groveling subordination before the absolute power of the autocrat.

Even in the new order, cautious up-and-comers took care to strike a loyal pose, at least in public. On one of my first meetings with Khodorkovsky, at the time probably a far richer man than Gusinsky, the future oligarch was careful to insist on his absolute deference to the will of the state. If the prime minister were to ask him to step down as head of his bank, Khodorkovsky said he would do so at once: "That is how Russia is organized. The state is always the dominant force in the economy."

If that was still the rule, as 1994 rolled on, Gusinsky seemed to have forgotten it. Inevitably, it was not long before the Kremlin decided to remind him.

The moment of reckoning came one dreary December afternoon, as Yeltsin and his retainers were finishing off a late lunch. Over the dregs of the meal, the president leaned across the littered table and addressed himself to Korzhakov, his friend and chief bodyguard, and Mikhail Barsukov, the chief of the revamped KGB.

"Why can't the two of you deal with what's-his-name, with Gusinsky?" Yeltsin thundered. "What's he up to? Why does he trample around everywhere? Everyone is complaining about him, including my own family. I can't count the number of times that Tanya [the president's younger daughter] or Naina [his wife] have been driving somewhere and the road has been blocked to make way for Gusinsky. His NTV has gotten too big for its boots, it behaves insolently. I order you: Deal with him."

Coquettishly, Korzhakov put up a few halfhearted objections: Gusinsky did not seem to have broken any serious laws, so how could he, an ordinary, honest law-enforcement official, take action against him?

According to Korzhakov's own scurrilous memoirs, at least, an irritated Yeltsin quickly made clear he had no patience for such pedantry. "It's not important!" the president roared. "Grab on to something, persecute him everywhere, give him no quarter. Create such an atmosphere that the ground burns beneath his feet."

It was exactly the command Korzhakov had been waiting to hear. A year earlier, Korzhakov had helped Gusinsky get a license for NTV. But over the past few months, his attitude toward the businessman had soured. Privately, he had begun to employ all sorts of covert stratagems to curb Gusinsky's growing power. Now, the president had openly instructed him to get rid of this turbulent priest. Korzhakov was only too delighted to comply.

In the Kremlin, hostility toward Gusinsky had been building for months. One source of friction was the inevitable antipathy between a liberal media and an increasingly authoritarian government. In late 1993, when NTV got its license, the great political divide in Russia was still between the Communists and the democrats, and the businessman and the president were still on the same side.

But Yeltsin had always been a problematic champion for Russian liberals, and this moment of harmony, like so many others, quickly slipped into discord. As 1994 rolled on, Yeltsin increasingly began to turn to the party of war and the hard-line measures they recommended. Economic reforms again seemed to stall, as the red directors lobbied for various special protections and most of the young reformers, including Gaidar himself, were pushed out of office. On political matters, the party of war was even more influential. Moscow began to take a tougher line with Chechnya and started to arm its own backers in the region.

The ascendancy of the party of war began to provoke friction between the Kremlin and the Most group. Like most of the Moscow intelligentsia, Most journalists were liberally inclined. Worse yet, from the Kremlin's point of view, they had a disconcerting tendency to discover and publish embarrassing facts, such as the story about Soskovets and the Novosibirsk Tin Factory. The Most group's coverage of Chechnya, especially NTV's evenhanded effort to present the Chechens' side of the story as well as Moscow's, infuriated the Kremlin even more.

"NTV was very dangerous," Gusinsky told me. "Just imagine—for the first time ever, a television channel had appeared that you could not control. To which, if you said, 'Hey there, stop covering Chechnya!' they would just keep on covering it."

Kremlin officials were incredulous. They had given Gusinsky his channel and now he was using that gift to attack them.

A further, even more significant count against Gusinsky was his alliance with Luzhkov. With presidential elections less than two years away, Yeltsin was becoming nervous about his own political longevity. The Moscow mayor, with his robust Russian nationalism and canny combination of Soviet nostalgia with an enrich-yourself spirit, was wildly popular among Muscovite voters. To the Kremlin, he started to look like a potential challenger. "Luzhkov was changing," Korzhakov told me. "He was beginning to think about the presidency and Gusinsky's support was making him feel stronger."

As they watched their televisions or heard fresh gossip about the chumminess between Luzhkov and Gusinsky, Yeltsin and his Kremlin entourage began gradually to accumulate a powder keg of resentments. All that was missing was someone to light the match. Berezovsky was delighted to oblige. "Berezovsky would regularly report to us where and what Gusinsky had said about the president, how he had insulted him, how he wanted to deceive him," Korzhakov wrote in his memoirs. "And Berezovsky achieved his goal—in the president's entourage, Gusinsky began to be viewed as a dangerous enemy." In a conversation with me and in several interviews with the Russian media, Korzhakov even claimed that Berezovsky had tried to persuade him to arrange Gusinsky's assassination. However, many, including Berezovsky himself, dismiss the allegation as unfounded.

Portraying Gusinsky as a menace helped to enhance Berezovsky's own power. The more the Kremlin feared Gusinsky, the more it was prepared to build Berezovsky up as a counterweight. In Leontiev's opinion, and those of many others, Berezovsky's strategy made him a "professional traitor." Rather remarkably, Gusinsky took a more philosophical view. From his perspective, Berezovsky was just playing the game of Russian capitalism according to its own particularly savage rulebook. It wasn't personal, it was business, and when this round was over, there would be no hard feelings.

"Berezovsky just took advantage of the situation," Gusinsky told me. "If he hadn't done it, some other John Doe would have. I don't think it was wrong. Berezovsky is just like me—no better and no worse. We are all the same. Good people are kind and generous but they rarely succeed in life. It is bad people who succeed and they are rarely kind and generous."

Whether Berezovsky's behavior was good or bad, one thing was certain—it was successful. By late 1994, in Kremlin circles Luzhkov and Gusinsky had been established as public enemies number 1 and 2 and the pressure was on. Korzhakov and Barsukov, who generally preferred to hunt in a pack, began to urge Luzhkov to sever his ties with Gusinsky. Twice, Korzhakov told me, they cornered him in the exclusive President's Club and warned him to part ways with his old friend and ally.

In the last days of November, the screw turned tighter. Gusinsky's powerful security service, run by Filipp Bobkov, the former deputy head of the KGB, reported worrying rumors. One version was that a *kiler*, a private assassin, had been commissioned to murder Gusinsky. Another was that, in some unknown way, Korzhakov was preparing to attack.

Then, on December 1, the president gave Korzhakov the fateful command to deal with the turbulent priest—at least according to Korzhakov's memoirs. That day, Gusinsky got an unexpected call. It was Georgi Rogozin, Korzhakov's deputy, inviting Gusinsky to the Kremlin for a meeting.

When Gusinsky arrived, Rogozin's agenda was immediately apparent. The Kremlin was unhappy both with Gusinsky's friendship with Luzhkov and with the coverage of the Kremlin and the war in Chechnya on NTV. To appease the president, Rogozin suggested, Gusinsky should produce some *kompromat*—the Russian term, inherited from the suspicious Soviet era, for compromising materials—about the Moscow mayor.

"It was suggested to me that I betray Luzhkov," Gusinsky recalled. "He said, 'We need Luzhkov's bank accounts.' I said I didn't know about them, but even if I did, how could you think I would give them to anyone? What do you think my children would say about me after that?"

It was, Gusinsky said, a "very long and complex conversation." But by the end of it, he thought he and Rogozin had agreed to a truce. It wasn't until the next morning that Gusinsky realized he had disastrously misjudged the situation.

Like most New Russians, Gusinsky had moved from Moscow's crowded and polluted city center to a country dacha, where he lived with his wife, Lena, his two-year-old son, his mother, and the family's nanny. The home, like all of the Most empire, was heavily guarded by Gusinsky's private security force. At about 9:15, the usual time he set off for the forty-minute drive to his office, Gusinsky stepped outside into the lightly falling snow and his two-car cortege prepared to head down Rublovskoe Shosse, a four-lane highway known as the President's Road, because it was the route Yeltsin took from his own dacha to the Kremlin.

But, as Gusinsky was climbing into his armored car, Zhenya, the head of his personal guard, warned him there had been some problems. A group of armed men had driven up to the house and tried to provoke Gusinsky's guards into a fight. Some of the men were masked and most carried automatic weapons. Worst of all, Zhenya was sure they weren't what the Russians called *bandity*—they had the look and bearing of professional soldiers, perhaps KGB or the Ministry of the Interior.

When Gusinsky's motorcade set off for the city, these mysterious armed men followed in three cars, one of which was the personal vehicle of Barsukov, the KGB chief. They wanted to be noticed, waving their machine guns outside their car windows, openly videotaping Gusinsky and his entourage, and trying to force the Most vehicles into the ditch.

"We decided to demonstratively tail Gusinsky," Korzhakov recalled in his memoirs. "The banker's bodyguards were nervous and Gusinsky himself was frightened to death."

Once he arrived at his twenty-first-floor office, a shaken Gusinsky summoned his closest advisors—Zverev, his PR and information chief; Malashenko, the head of NTV; and Bobkov, the ex-KGB agent who ran his security service—and frantically began trying to figure out what was going on, and how to respond. Gusinsky's first move was to call two senior Moscow police chiefs and ask them to help him identify the armed group that had pursued him into the city and was now surrounding the office building. The policemen soon came back with an answer: the armed pursuers worked for the infamous Presidential Security Service, headed by Korzhakov.

Gusinsky blanched. The Presidential Security Service was, to his mind, the modern equivalent of the *oprichniki*, Ivan the Terrible's notorious death squads. "Absolutely everything was permitted to them," Gusinsky later told me. "They drove around the streets of the city drunk, they did anything they wanted. There was no more terrifying and powerful person in Russia than their chief, Korzhakov. It was the most terrifying service in Russia. It was like a regiment of death."

Worse still, the Most executives realized immediately that even Korzhakov would never put on such an overt show of force without the explicit approval of the president himself. Gusinsky had become a pawn in a larger Kremlin game, and he was on the wrong side.

Yet, despite his strong suspicion that Yeltsin had personally authorized the siege of his office, Gusinsky, ever the impresario, decided to try to stir things up. He had an influential friend in the security forces: Yevgeny Sevastyanov, a bearded, soft-spoken academic who had joined the pro-democracy movement in the late 1980s and been rewarded with the post of head of the Moscow municipal branch of the FSK, the revamped KGB. Gusinsky telephoned Sevastyanov and told him about the armed men outside his building. "You should send someone out immediately to investigate," he urged—after all, the gunmen were just a hundred yards from the White House, which by then served as the seat of the Russian cabinet.

Of course, Gusinsky, who knew perfectly well who the men were, was setting his friend up: "I was being a bit of a provocateur," Gusinsky later admitted to me. "It was interesting for me to see how the federal government structures would react to the actions of the Presidential Security Service."

Sevastyanov took the bait. Korzhakov, who fancied himself a sort of James Bond–style secret service agent, had neglected standard police procedure and failed to inform other police agencies of his operation. Sevastyanov had no idea the armed men were actually working for the Kremlin, so he sent out an antiterrorist team to investigate.

Korzhakov's men were astonished. They were the crème de la crème of Russia's law-enforcement organizations, the untouchables, and here were five ordinary Moscow KGB agents, brandishing their guns and demanding to see their documents. Before long, a fight broke out. One of the Moscow agents fired a shot into a tire of one of the three cars driven by the president's men. Another bullet grazed the shoulder of a presidential guard, leaving him unharmed but, to his fury, spoiling his new leather jacket. Another one of the president's men was knocked to the ground by a powerful right-hand hook from a young woman who was part of the Moscow KGB team.

Just as the two forces were on the verge of a pointless and bloody shoot-out, one of the Moscow KGB agents recognized one of the presidential guards: they had once worked together. The hostility dissolved into stiff smiles, guns were holstered, hands were roughly shaken, and the Moscow KGB agents drove away.

But the violence had raised the stakes. All morning long, Gusinsky and his team had been watching events unfold in the icy, concrete parking lot twenty-one stories below. From the start, Malashenko had insisted that the Most group's only defense was the weapon that had helped to get it into trouble in the first place—the media. Bobkov demurred. Perhaps a backroom political solution could be found, he argued. After all, going public was an extreme move, and one that would put the Most group openly and inexorably into conflict with the president.

As Sevastyanov's team drove away, Gusinsky realized that taking to the airwaves was now his only option. Malashenko and Zverev hit the telephones, personally calling all the journalists they knew, particularly Western ones, and inviting them to come to the Most offices immediately.

Their SOS signal did not go out a moment too soon. Infuriated by the behavior of Sevastyanov's team, Korzhakov sent an additional group of men to the Most building. They wore black balaclavas and camouflage fatigues and were heavily armed. The men began roughly to search Gusinsky's cars and ordered the three bodyguards who had been sitting inside to get out. Then they forced them to lie down on the snow-covered concrete of the parking lot.

The ensuing scene—the three bruised and bloody bodyguards lying facedown on the snow, encircled by a group of masked men beating them with their heavily booted feet and the butts of their guns—became the defining image of the conflict. Dubbed as the faces-on-the-snow incident, the confrontation was almost immediately seen as a turning point in Russia's political and economic development—but no one yet could tell what kind of a turn it signaled.

The battle took on such iconic significance because the arrival of Korzhakov's bruisers coincided with the appearance of the press. As the president's men bore down on the hapless security guards, more than thirty television cameras, belonging to everyone from CNN and Japanese TV to NTV itself, were there to record every blow of icy boot to broken rib, each rivulet of blood seeping onto the snow below. Korzhakov's men might still behave with the lawless brutality of the *oprichniki*, but they were *oprichniki* operating in the television age.

"Our [journalistic] colleagues really supported us," Gusinsky recalled. "I think what stopped those butchers was the presence of hundreds of journalists here, who understood that what was happening was lawlessness."

Eventually, at the personal order of Viktor Yerin, the minister of the interior, who had been petitioned by his friend Korzhakov, a police team arrived at the Most building and arrested the beaten bodyguards. By 1 A.M., however, they had been released. The Moscow police were disgusted by the flimsy charges, which had been conjured up in a transparent effort to get at Gusinsky. In fact, a local government prosecutor was so incensed by the incident that he tried to bring criminal charges against the Presidential Security Service for exceeding its authority. A delighted Gusinsky declared the pugnacious lawyer a civil society hero.

But Korzhakov—against whom the investigation was, of course, swiftly dropped—had already taken one scalp that day. Sevastyanov, the head of the Moscow KGB, was fired by presidential decree even as the president's men were beating Gusinsky's bodyguards. As Sevastyanov later wryly told me: "We have a saying in Russia: Don't fight with the strong, or take the rich to court. As soon as my boys called me up and said, 'These are Korzhakov's men but, while we were figuring that out, we got into a fight with them,' I told them, 'Well done. You can congratulate yourselves on having gotten the chief of the Moscow KGB fired today.'"

When Gusinsky finally made it home at two that night, his wife was so nervous that she greeted him at the door with a Winchester in her hand. When he saw the gun, and Lena's fierce stare, Gusinsky smiled, probably for the first time that day. "I can tell you, she was ready to defend herself," he recalled with a proud grin. "She's a Kuban Cossack."

Over the next few days, things became even more tense. Korzhakov publicly declared that he was going hunting for "geese," a reference to one of Gusinsky's nicknames. The pressure on Luzhkov, on Most bank, and on the Most media interests intensified. All of this occurred against the background of an escalating conflict between the Kremlin and the separatist fighters in Chechnya. The fighting was going badly wrong and it was making the Kremlin even more defensive and trigger-happy than usual.

Three days later, on Monday, December 5, Gusinsky decided to send Lena, their son, and the nanny to London. Normally, they would have flown in the private jet, which was one of Gusinsky's favorite executive toys. But the businessman worried that a still wrathful Korzhakov might not allow his private plane to leave Russian airspace. Instead, the family bought tickets for British Airways' scheduled daily late-afternoon flight to Heathrow.

As Lena and her small entourage wove their way through the dirty winter slush and the evening traffic toward Sheremetyevo Airport, Gusinsky headed for the Kremlin. Rogozin had called him in for another meeting. Gusinsky's first request was that his wife and son be allowed to leave the country. Korzhakov's deputy responded with a coy non-answer: maybe they would be, maybe they wouldn't be—it all depended on Gusinsky's conduct. With that, Gusinsky, never the most tranquil of men, exploded.

"I started cursing him, his relatives, his mother, his father, his grandfathers, and his grandmothers," Gusinsky said. "Then I told him what would happen to him personally [if my wife was not allowed to leave]. I said that I wouldn't need my security guards or anything, I would strangle him with my own bare hands. I said that I would kill him. It was all very clear. Because you know what we say—there is no fiercer fighter than a scared Jew."

Years later, Gusinsky was still proud of his outburst, and certain that it had helped to ensure the safe passage of his wife and son out of Russia. But, of course, Rogozin and Korzhakov were far from vanquished. Over the next few days, as the pressure continued, Gusinsky realized he was a sitting duck. The only option, he decided, was to leave Russia—temporarily, he hoped. On December 18, 1994, four days after the Kremlin sent its army to Chechnya and three days after my brother, Adik, left Russia forever, Gusinsky followed his wife to London.

Two months later, I joined Gusinsky in the genteel salon of London's Park Lane Hotel. He was chairing one of his weekly meetings with his top executives—during those days, the entire Most team shuttled back and forth so often that "going to London became like catching the metro for us," one of them told me. The group of gesticulating, leather-jacketed Russians—surrounded by a haze of cigarette smoke, the proud ringing of mobile phones, and the bright, hard smiles of young wives—looked profoundly out of place in that sedate English sitting room.

But Gusinsky was deeply indifferent both to the snooty looks of the waiters and to the elegance of his surroundings. His interest was talking about Russia and wondering whether it would ever be safe for him to go back: "It is very simple to find a reason to arrest a man in Russia. I could wake up tomorrow and be told that I drink the blood of young babies, or have been molesting teenage girls. Anything, any trumped-up charge at all, is possible."

While Gusinsky watched and waited, his businesses began to die. Although NTV continued its brave coverage of the Chechen war, on other issues Gusinsky's journalists were muzzled as he sought a truce with the Kremlin. "He imposed a very strict censorship on us," Leontiev recalled. "It was a request from him that we could not refuse. We used to say to him, 'You know that you are destroying the newspaper. We are now more boring than everyone else.' And he would reply, 'Guys, I understand you, but be patient. Wait another month and a half and then, well, if we have to die, let's die with music.'"

The banking arm of Gusinsky's group was in even greater jeopardy. Of all businesses in Russia, banking was the one most deeply dependent on the favor of the state. Now that Gusinsky had been officially declared the Kremlin's bête noire, other banks and retail clients began to fear that

Most was no longer creditworthy. After all, any day now, it seemed, Korzhakov might close the bank down altogether.

The attack on Gusinsky also sparked a crisis for Moscow city hall. To a large extent, Gusinsky had been hounded as a proxy for Luzhkov. Luzhkov's initial reaction was exactly as the Kremlin had hoped. He quietly cooled his alliance with Gusinsky—on the day when Korzhakov's men swooped down on the Most group, the mayor was unavailable to speak with his erstwhile friend—and he took care to pledge his fealty publicly to Yeltsin.

But, even as he bowed his head to the tsar and distanced himself from the tsar's enemies, Luzhkov privately vowed to never again be so dependent on the whims of the central government. The faces-on-the-snow incident had underscored Luzhkov's vulnerability. When faced with a choice between city hall and the Kremlin, many of Luzhkov's closest financial and political allies had deserted him. In the aftermath of the attack, the Moscow mayor withdrew from public life and considered how to protect himself against future betrayals.

Luzhkov's solution was to become an economic tycoon in his own right. Now convinced that he could trust no one but himself, Luzhkov used Moscow's tremendous political clout to build up a vast financial and industrial empire directly run by himself and his first lieutenant. This new conglomerate, an unwieldy hybrid of business and politics, was called Sistema. Controlled by a branch of government, but operating in the private sector, Sistema soon became the most muscular practitioner of what Russians eventually began to call state capitalism—a new, increasingly popular genre of economic life that was not quite central planning, but not a free market, either.

"The ideology of Sistema was born out of the conflict with Yeltsin," Gusinsky explained. "He [Luzhkov] understood that he had to do something so that no one would betray him again. To ensure that no one betrayed his business, he had to have control. To have control he had to own a share. That's all. It was very simple."

With Gusinsky trapped in London and Luzhkov focused on building up his own financial and political machine, Korzhakov and the party of war seemed to grow more influential every day. No longer content merely to advise the president on matters of war and peace, the bodyguard began to dabble in the economy. Ten days after the faces-on-the-snow incident, Korzhakov took it upon himself to write to Prime Minister Chernomyrdin, instructing him on how to conduct negotiations with the World Bank for a multimillion-dollar loan.

The letter, which was leaked, horrified the Moscow intelligentsia. *Izvestia* was prompted to ask its readers, "Who rules Russia—Yeltsin, Chernomyrdin, or General Korzhakov?" Some pundits drew parallels with Rasputin and the chaotic final days of the Romanov dynasty. Others compared Korzhakov and his crackdown on Most to the attacks on Soviet businessmen that had marked the beginning of the end of the New Economic Policy, the brief respite in the 1920s when the Bolsheviks allowed small and medium-sized business to flourish. Just as that was cut short by the Great Terror and Stalinism, many Russians had worried all along that Russia's young capitalism would come to a bitter end. The brazen attack on Gusinsky seemed to signal that the naysayers might be right.

"It wasn't a conflict between Korzhakov and Gusinsky," Sevastyanov argued. "It was a conflict between the nascent, free society and a newfangled totalitarianism. Korzhakov was the carrier of the idea of a new totalitarianism. It seemed to him that the emerging system of government, and the situation in the country as a whole, was spinning out of control. It would only be possible to reassert control using coercive methods."

Even the darkest prophets did not predict a return to Soviet-style dictatorship, but the freedoms and promises of 1991 did seem to be at an end. Instead, Russia seemed to be settling for a newer, lazier version of totalitarianism, in which some political liberties and some economic opportunities would be allowed, but the aging and ill-tempered bear of the state would have the power to interfere wherever and whenever it liked. After three tumultuous years of market and political reforms, the party of war seemed to be ruling Russia.

EIGHT

THE FAUSTIAN BARGAIN

It doesn't happen very often, but every once in a while a really Big Idea—a premise so timely or so powerful it changes the shape of our lives—comes along. A disaffected Russian intellectual reads Marx, is inspired to marry his theories to the indigenous terrorist tradition, and, bang!, the world's first Communist dictatorship is born. A group of paranoid U.S. military engineers decide to use their fancy new computers to create an electronic communications network so decentralized it will be safe from the Soviet threat, and, yahoo!, forty years later that network has become the internet and is transforming the global economy. In post-Communist Russia, the Big Idea was an intricate privatization scheme known as loans-for-shares and its ultimate result was the deformed capitalism that has impoverished and embittered the country.

Loans-for-shares wasn't the obvious kind of Big Idea: it wasn't a grand political theory or a brilliant invention. It wasn't idealistic, like Gandhi's nonviolent resistance movement, or particularly smart. It didn't even have the distinction of being soul-numbingly evil, like Nazism or apartheid. Instead, loans-for-shares was a Big Idea very much in the cheesy, sleazy, look-out-for-number-one spirit of the new Russia. Its strengths were audacity and cunning, so much so that it was months before anyone outside a small circle of Moscow insiders realized what was really going on.

At heart, the loans-for-shares deal was a crude trade of property for political support. In exchange for some of Russia's most valuable companies, a group of businessmen—the oligarchs—threw their political muscle behind the Kremlin. What made that bargain a Big Idea and not just ordinary corruption was its scale. Over the course of four months, the government privatized the behemoths of the Russian economy, a half dozen huge enterprises, including the world's dominant producer of nickel and several reserve-rich oil companies, selling them for a fraction of their potential market value. It was the sale of the century.

Loans-for-shares was also politically radical. Thousands of red directors had already been terrifically enriched by privatization. The Soviet-era managers of Gazprom, Russia's natural gas monopoly, and of Lukoil and Surgutneftegaz, two of the largest oil companies, for example, were savvy enough to use mass privatization to become the owners of huge chunks of Russia's mineral wealth. But that was essentially a process of redefinition, rather than of redistribution, with the Kremlin just formalizing the red directors' ownership of assets they had already effectively controlled in the Soviet era.

Loans-for-shares was revolutionary because it did the opposite. It took companies away from their red directors and gave them to a handful of thrusting entrepreneurs. These men became oligarchs—and it was the convoluted loans-for-shares scheme that created them. It was a scheme so brazen and so bizarre that five years later it's still hard to understand why the Russian government actually did it. Think about it: It couldn't be purely out of weakness—it would have been easier just to give the enterprises to their red directors. It couldn't be sheer corruption, either—if it had been, why not give them to the real political insiders, like Yeltsin's daughters or Chubais's wife?

So what was the motivation? Of course, in the messiness of real life—and Russia is nothing if not messy—there were many reasons. The state was weak; many of its apparatchiks were corrupt; the future oligarchs were brilliant lobbyists, adept at playing on all the divisions in Yeltsin's schizophrenic government. But, in the end, loans-for-shares was implemented for one central reason—because the government in general and the young reformers, who still controlled the privatization process, in particular took the calculated gamble that this was the Big Idea that could save Russia's capitalist revolution. Loans-for-shares bought Yeltsin the political, financial, and strategic support of the future oligarchs in the upcoming presidential elections. It meant pawning Russia's crown jewels, but if that was the price of keeping the Communists out of the Kremlin, the young reformers were willing to pay up.

"I understood the loans-for-shares program perfectly well," Gaidar told me on a rainy afternoon in his office three years later. "The loans-for-shares created a political pact. They helped to ensure that [Communist leader Gennady] Zyuganov did not come to the Kremlin. It was a necessary pact."

That "necessary pact" turned out to be a Faustian bargain. The young reformers defeated the Communists, but they lost their souls in the process. They had come to power as democrats; to stay there, they created a shadowy, unelected cabal. They had come to power to create a fair, equitable, law-abiding market economy; to keep it, they sponsored one of the world's sleaziest insider deals. Ultimately, loans-for-shares destroyed the young reformers: it cost them their ideals, their reputations, and eventually their jobs. Worse yet, ultimately, it scotched any short-term hopes there still were for the emergence of healthy, prosperous Russian capitalism. Instead, Russia's market economy is now corrupt, distorted, and inefficient, and loans-for-shares is both cause and symbol of its malaise.

It took us a while to abandon the image of Boris Yeltsin on the tank as the defining icon of the new Russia. The collapse of the evil empire, the velvet revolution, and the end of history were such hopeful stories—and ones we in the West had such a stake in—they were hard to stop believing. But now that so many of us have given up on the dream of a resurrected Russia, we've been seduced by a titillating new set of images: gangsters, shoots-outs, drugs, prostitutes, money laundering, and kickbacks. Blaming Russia's woes on these lurid forms of crime and corruption is easy, and it's exciting—but it's not really true. Russia has been looted all right, but the biggest crimes haven't been clandestine or violent or even, in the strict legal sense, crimes at all. Russia was robbed in broad daylight, by businessmen who broke no laws, assisted by the West's best friends in the Kremlin—the young reformers.

The loans-for-shares program began to creep into life in the dying days of 1994. It was a dark time for Russia and for the lurching effort to create democracy and capitalism. Yeltsin was becoming authoritarian and bellicose, curtailing press freedom and threatening war against Chechnya. Economic reforms seemed stalled. Voucher privatization was almost complete, but it was not at all clear what would happen to the companies still in state hands. The macroeconomic outlook was bleak: the annual inflation rate was 215 percent, the ruble grew weaker every month.

But, for at least one man—Vladimir Potanin, the Soviet blue blood—this harsh political and economic environment looked like an opportunity. He had been the slowest to join the capitalist race, but once he decided to become a capitalist he thought big. Managing the government's money or buying up the rust-belt factories the state was selling for a song was a nice enough racket to start with, but soon Potanin wanted much more. He sensed that now, in the embryonic years of Russia's capitalist revolution, the great fortunes—the ones that would make names and endure for generations—would be built. To create his, to establish the house of Potanin, he wanted a piece of the only assets the demented system of central planning had been unable to destroy: Russia's natural resources. By the autumn of 1994, Potanin had already decided which nugget he wanted—Norilsk Nickel, the gargantuan producer of nickel, cobalt, and other precious metals in the far north.

It was a daring choice. Norilsk Nickel, eked out of the frozen tundra through almost immeasurable collective sacrifice in the 1930s, was not just a metals mine. It was "the pearl of the north," a national legend and a potent symbol for millions of Russians of both the pain and the achievements of the agonizing Stalinist industrialization drive. With annual sales estimated at more than $2.5 billion, it was also one of the few truly valuable enterprises in an economy dominated by unprofitable Soviet albatrosses.

Potanin already had a significant link with Norilsk Nickel. It was one of the clients Oneximbank, his company, had inherited after the collapse of the Soviet banking system. Now Potanin wanted to elevate himself from Norilsk Nickel's banker to its owner. To make this brazen proposal more palatable, Potanin hit on the idea of disguising it with weasel words. He wouldn't actually suggest "buying" Norilsk Nickel at a reduced "price"; instead, he would offer to "manage" the company in exchange for a "loan." He had come up with the cunning rhetorical device that would soon mature into the loans-for-shares scheme.

Potanin's idea made fantastic progress. By October 1994, Yeltsin had signed a decree authorizing Interros, Potanin's holding company, to manage the state's stake in Norilsk Nickel and other major enterprises with which Potanin already had a relationship. But, as Potanin soon discovered, getting a decree signed was one thing—implementing it was something altogether more difficult.

Potanin needed allies. To get them, he decided to make his plan more ambitious. He wouldn't just try to capture Norilsk Nickel for himself; he would set his sights on an entire herd of valuable Russian companies and bring together a pack of up-and-coming private businessmen to join him in the hunt—and in feasting on the eventual kill.

The men Potanin invited into the deal were a veritable who's who of Russian business. Potanin remembers consulting with Khodorkovsky, the apparatchik oligarch; Aleksandr Smolensky, another future oligarch who had begun as a small-scale Soviet entrepreneur and gone on to found the Stolichny banking group; Vladimir Vinogradov, head of Inkombank, and later a sort of junior oligarch; Pyotr Rodionov, of Imperial, a bank established by the oil and gas barons; and Vitaly Malkin, of the Rossisky Kredit bank, and eventually a junior oligarch. Friedman, the outsider oligarch, was also in on the preliminary talks.

The series of meetings this group held, generally either at Potanin's headquarters or at Khodorkovsky's, was epochal. It was the first time the small, disparate band of adventurers who had made fortunes in the wild early days of Russia's capitalist transformation gathered and sought to advance their private interests collectively. It was the beginning of the oligarchy.

The reaction to Potanin's plan was mixed. According to Leonid Nevzlin, one of Khodorkovsky's partners, their group was immediately enthusiastic. Smolensky was more reserved, saying he wouldn't participate directly, but would be happy to help finance deals fronted by other future oligarchs. A few were totally dismissive: the plan seemed too grasping, even by Russian standards, ever to work. "The scheme proposed selling property that was worth billions of dollars for mere kopecks. It seemed unrealistic and I reacted coldly," Friedman told me ruefully. "But, as you see, it turned out to be very realistic."

A core group committed to the plan quickly emerged. Perhaps surprisingly, that group readily agreed on a rough-and-ready division of Russia's most valuable companies. "We reached an agreement of who would take what. We agreed not to get in each others' way," Nevzlin admitted. "In this respect there was an element of insider dealing." Potanin would get the best company—Norilsk Nickel—because he had come up with the plan in the first place. Khodorkovsky would get Yukos, a huge Siberian oil company. Other, smaller enterprises were earmarked for the more junior players.

The next hurdle for Potanin was to win government support for his new, expanded scheme. At the time, the Russian political establishment was split. In early 1995, the conflict was particularly intense. The party of war had just persuaded Yeltsin to launch the disastrous attack on Chechnya. In response, for the first time, Russia's horrified liberals began to attack the Kremlin. Yegor Gaidar publicly announced his opposition to the president, and many of the young reformers thought that Anatoly Chubais, who was still clinging to a cabinet seat, should resign. To implement loans-for-shares, Potanin needed to get the support of both factions and of their warring leaders: Chubais and Oleg Soskovets.

Soskovets, the deputy prime minister, was the easier to win over. He was, as Potanin put it, one of the "ideologists" of the FIGs, the huge financial-industrial groups the loans-for-shares program would eventually create, and he had backed Potanin in his initial efforts to take over Norilsk Nickel. Just as important, he and the future oligarch spoke a common language and belonged to a common tribe. Potanin was a *nomenklatura* baby and he had no problem charming a middle-aged red baron like Soskovets.

Chubais, also a deputy prime minister, was more difficult to convince. He was reluctant to compromise his principles—and to tarnish his golden Western reputation—by condoning insider privatization. But if anyone could persuade him, it was Potanin. The two men were not yet close friends, but they, too, already had a lot in common. Both were young, English speaking, and so aggressive as to sometimes be called arrogant. Moreover, Potanin, with his well-cut suits and mastery of Western business jargon, was exactly the sort of home-bred tycoon Chubais had hoped his market revolution would create. Potanin began to meet with Chubais to sell him on the scheme.

For Chubais, one of Potanin's most powerful arguments was that loans-for-shares would raise money for the cash-strapped Russian treasury. By the beginning of 1995, the young reformers had succeeded beyond their wildest expectations in their pledge to transfer property to private owners. But they had failed miserably in their promise to stabilize the economy. Chubais vowed that 1995 would be the year the government finally brought down inflation and rescued the ruble. To do that, he needed to find non-inflationary sources of state revenue: precisely what Potanin and his consortium so temptingly offered. Chubais also liked the idea of using the future oligarchs to break the back of the red directors and—he hoped—to bring better management to Russia's moribund industry.

But, still, Chubais had reservations. So far, the young reformers had tried to make privatization as fair and as open as they could. The loans-for-shares scheme, by contrast, was a naked insider giveaway. "There is no competition, no openness," Chubais complained to Potanin. "It is not in our tradition." Once Potanin promised to make the process at the very least look less egregiously corrupt, the future oligarchs won their second vital government supporter.

Finally, the business consortium was invited to present its scheme to the full Russian cabinet at a meeting on March 30, 1995. Potanin was chosen as spokesman. Khodorkovsky and Smolensky went with him to offer moral support.

The plan Potanin outlined was an early version of loans-for-shares. Speaking in the name of the business consortium, Potanin said the group was prepared to offer the government a loan of up to 9.1 trillion rubles ($1.8 billion). In exchange, the consortium would be entrusted with the management of the state stake in a number of leading companies, including Norilsk Nickel and Yukos (which ultimately were sold off through the scheme), and United Energy Systems, the national power company, and

Rostelekom, the national telecommunications operator (which were eventually excluded from the program).

Potanin's historic offer would transform Russian politics and the Russian economy; it was also a measure of how dramatically Russia had already changed. Three men, two of them barely in their thirties and all unknown ten years earlier, had become so powerful they could presume to make a bargain with what was left of the once omnipotent Soviet state. For men born and bred in the belly of the Soviet system, it must, I thought, have been a bit intimidating to enter the vast, chandeliered cabinet meeting room and address the assembled ministers on equal terms.

Apparently not.

"Me worried? What did I have to worry about?" Potanin replied in answer to my question. "We, in our banks, had comfortable material circumstances. It was the government that had a hole in its budget. They were the ones who were worried. I just wanted to calm them down, say to them, there is a concrete idea. We'll collect a billion or two dollars."

As it turned out, Potanin's sangfroid was perfectly justified. After Potanin finished speaking, Prime Minister Chernomyrdin said he liked the sound of his scheme. Then he asked the two most powerful figures in his cabinet—Chubais and Soskovets—what they thought. This was the crucial moment: Soskovets and Chubais disagreed over almost everything, and either one was probably strong enough to stymie the program. But Potanin's skillful lobbying paid off.

"Soskovets said that he, in principle, at a preliminary stage, thought it was interesting," Potanin remembered. "Chubais just silently nodded his head, meaning, we'll work on it. And that was it."

Loans-for-shares had passed its first and most important political test. History was being made.

But, apart from the future oligarchs and a few cabinet ministers, almost no one realized what was going on. The scheme was so brazen, and so downright weird, that many of the smartest observers of the Russian economic scene, especially the Western ones, refused to take it seriously.

My notebook from April 1995, a few days after the fateful cabinet meeting, records the views of one such doubter—Anders Aslund, a

Swedish economist. "It's absolutely outrageous," Aslund sputtered. "The implication is, we should get richer at the expense of the state." But Aslund, an intelligent analyst and generally one of the best informed, assured me that I need not fear the plan would ever be implemented. And why not? "Because it's so stupid!" Aslund went on to insist that Chubais, a personal friend, would never allow the program to go ahead: it was "impossible" that Chubais could ever sanction such a rip-off. My editors at the *Financial Times* and I were almost equally dubious.

A few of my Russian friends were a lot smarter. The day after the cabinet meeting, Kakha Bendukidze, the owner of the gas exploration company in arctic Gaz-Sala, warned me that loans-for-shares was an effort "to set up an oligarchy in the Russian economy." That afternoon, Mikhail Zadornov, a leading liberal member of parliament who would later become minister of finance, voiced the same fear in exactly the same terms, telling me that the proposal could be "the beginning of an economic oligarchy." Unfortunately, they were right.

Throughout the spring of 1995, the businessmen continued to push their radical plan. Two tasks remained. The first was patiently to nudge the scheme through the sclerotic Russian bureaucracy. The more complicated job was to finalize the list of companies that would be sold off. Doing that was more difficult than it might seem. Loans-for-shares was not implemented by a Western government, with full control over its own bureaucracy and property. It was the act of a desperately enfeebled state, so anemic it was unable to perform basic functions such as collecting taxes or maintaining its monopoly over coercive force. Although this shadow state formally "owned" the companies that were ultimately sold off, the Kremlin had little real political or economic control over them.

That meant that loans-for-shares wasn't quite a straightforward giveaway. Instead, the Kremlin basically gave the future oligarchs a federal mandate to try to wrest control of some choice assets away from the red directors who were their effective owners. A good parallel is with the Crown mandates the British monarch granted to "companies of adventurers," like the Hudson's Bay Company, to exploit the Canadian wilderness. The Crown granted them a monopoly to try to squeeze profits out of vast expanses of forest, but their success depended on their ability to persuade or coerce the indigenous people to do business with them.

"These were companies that the government was simply unable to sell," Khodorkovsky told me. "They were run by very powerful directors, men who could raise up eighteen governors, eighteen regions. That was why they were not included in the first stage of privatization. So it wasn't a question of just making a list of what the government would sell and choosing what you would buy. It was a question of whether you were able to reach an agreement with the [red] directors. That was the basic condition."

So the businessmen set about wooing the Soviet-era directors of the companies they wished to acquire—Khodorkovsky spent weeks befriending the managers of Yukos, the oil company he had set his sights on; Potanin won over the directors of Sidanko, the oil company he would eventually obtain, but met a more prickly response at Norilsk Nickel, the prize he most ardently desired.

Some of the red directors were strong enough to fend off the oligarchs altogether. Vagit Alekperov, the head of the oil company Lukoil, and Vladimir Bogdanov, the chief of Surgutneftegaz, another leading oil group, did this by forcing the Moscow businessmen to admit them to their group and effectively becoming oligarchs themselves. Other Soviet-era directors were not strong enough or smart enough to buy out their own companies, but they did have the muscle to force the government to withdraw their enterprises from the loans-for-shares list.

Through these tussles, in the echoing corridors of Moscow ministries, on the floor of the Duma (the lower house of the Russian parliament), and in dozens of provincial cities, the final list was reduced and reduced until, in the end, just twelve companies remained. All that was left now was to get final approval for the process from the Kremlin and to kickstart the sale of the century.

The key man in this last stage was Alfred Kokh, a round-cheeked young reformer from St. Petersburg with an unruly mop of dark hair, an exuberantly dirty mouth, and a biting sense of humor. By the summer of 1995, Kokh had replaced Chubais as acting head of the GKI. Potanin, who would eventually become Kokh's personal friend, was dispatched to sell him on the loans-for-shares scheme.

Kokh was almost instantly sympathetic to what he described in his memoirs as "Potanin's brilliant idea." Like the rest of the young reformers, he immediately grasped the essential political logic of the proposed pact. "We had to survive all the political strife of the next one and a half years," he later told me. "In this fashion, we ensured the support of the banks for the president in the presidential elections." He also liked the thought of outwitting the Communists by disguising privatization as a loan program. But it was the fiscal argument—that the scheme would almost instantly provide revenue for the cash-strapped Russian treasury—that, according to Kokh, finally swung the political balance in the future oligarchs' favor.

The crunch came in the middle of August. Kokh had just returned from his summer holiday and was starting his new job at the GKI. But his first cabinet meeting was a disaster: "I was very forcefully beaten over the head." The problem was money. The year was nearly over and the GKI had raised only a fraction of the 8 trillion rubles it was budgeted to bring in through privatizations.

Anxious not to be attacked a second time, Kokh was ready with a sheaf of specific proposals when the cabinet held its next weekly meeting. He presented his list: one plan was still in its infancy, another was 20 percent developed, a third was just over half complete, a fourth was almost ready to be implemented. Desperate for cash, it was this technically advanced proposal that piqued the interest of Kokh's fellow ministers. What idea, they asked, was so nearly ripe for the picking?

"Oh, you remember, it's the one that Potanin was talking about with the loans," Kokh replied. "The technical work is done, there is even a draft presidential decree."

And that, Kokh recalled, was all it took to persuade the Russian cabinet to go ahead. "Right, that's it," his cabinet seniors decreed. "We have no alternative. There's nothing else we will have time to prepare between now and the end of the year."

Months of intense bureaucratic lobbying had finally paid off. The plan was ready to roll: all the decrees were drafted, all the laws were written, all the apparatchiks were appeased. The government, by contrast, had been too disorganized and too aimless to come up with a privatization scheme of its own. As they would so often over the next few years, the future oligarchs had beaten the state at its own game. On August 31, just a few days later, Boris Yeltsin signed Decree 889, the document that would make a handful of lucky Russians billionaires.

The program signed into law by the president was not too different from the plan proposed by Potanin five months earlier. The government would still allow private businesses to manage the state stake in a group of key companies in exchange for loans. But, instead of doing the deal directly with a single consortium, the government would auction off the right to manage the state's shares, in a process that would ostensibly be "open and competitive," but that in reality was dominated by insider deals. Thanks to the fierce lobbying of the future oligarchs, foreigners were barred from directly participating in the competitions for seven of the companies on offer, including Norilsk Nickel, Sidanko, Yukos, and Lukoil.

auction

The government also elaborated on the terms on which the loans would be offered. For the first three months, the state would pay its creditors a low rate of interest. The loans would run out in September 1996. After that, the government would have two options. One would be to pay back the loan and take back its shares. The second would be to sell off the shares that had been used as collateral. If the state opted for the second choice, the lender would be paid 30 percent of the difference between the privatization sale price and the initial sum he had loaned the state. More important, the lender would act as the government's sales agent, organizing the second auction himself. (In theory, this second round of auctions, too, would be open to all comers, although when the time came the initial lenders all succeeded in buying the stakes they had held in trust.)

It was a fiendishly complicated scheme, but few of its twists had much practical significance. Loans-for-shares was designed as a vehicle to deliver valuable state companies to the future oligarchs and that is exactly what it did. But there was method in the seeming madness of cloaking so straightforward a transfer of ownership in convoluted loan schemes and multistage auctions.

One advantage of the complexity was that it shielded the plan from many of its potential critics. The Communists could be appeased with assurances that Russia's crown jewels were not actually being sold, merely pawned to help the treasury through a momentary tight spot. And Western observers, always lecturing Moscow about the virtues of competition and the dangers of cronyism, were reassured by the government's promise that both the first and second stage of the loans-for-shares process would be managed through open, competitive auctions. In September 1995, even that staunch defender of free markets, *The Economist,* gave the final version of the plan its grudging approval. The whole process would be above board, the magazine confidently pronounced: the Russian businesses "will not be allowed to sell shares to themselves on the sly."

Perhaps most important of all, the complicated two-step plan implicitly bound the economic fortunes of the future oligarchs to the political fortunes of the Yeltsin administration. In the autumn of 1995, the businessmen received stakes in Russia's most valuable companies only in trust. The final, formal transfer of ownership would not take place until the autumn of 1996 and in 1997—after the presidential elections. A Communist Kremlin would probably cancel the second, crucial stage of the loans-for-shares process, but Yeltsin was more or less guaranteed to finish the program he began. When he signed the decree, the Kremlin chief bought himself the constituency that would a year later guarantee his reelection.

As Aleksei Ulyukaev, one of the young reformers, put it: "We gave them just one of two keys [to the property]. They would receive the second key only after the elections."

The stage was now set for a final, ferocious struggle for the loot. A few red directors made a last minute bid to hang on to their Soviet inheritances. The clubby alliance of Moscow businessmen, formed so readily in the spring, began to fray, and conflicts, both public and private, started to break out. Entrepreneurs excluded from the deal, including future oligarchs temporarily out of favor with the Kremlin like Gusinsky, began to protest.

But, in the autumn of 1995, the loans-for-shares scheme rolled invincibly forward. The smoothest auctions were for a 5 percent stake in

Lukoil and a 40.12 percent share in Surgutneftegaz. Strong enough to fend off the future oligarchs and rich enough to contribute a bit of money to the treasury, the Soviet barons of these companies, acting in part through closely affiliated firms, bought the companies they already managed. They were not shy about using every inch of their local control to ensure that they won—on the day of the Surgutneftegaz auction, the nearest airport was mysteriously shut down and roadblocks manned by armed guards materialized on the main land routes into the remote Siberian city of Surgut (where the sale was held), thus physically preventing one outside bidder from competing.

Things became even more heated when it came to Norilsk Nickel, the inspiration of the entire process. The most serious clash was between Potanin and Anatoly Filatov, the mine's red director. Taking on a figure of Filatov's national stature took a lot of chutzpah. Potanin later admitted that he felt he was attempting the impossible, "like something out of a fantasy novel." More audacious still was Potanin's aggressive strategy. Instead of trying to make a deal with Filatov, Potanin risked a head-on conflict. Even when Norilsk Nickel's management suggested a compromise—Potanin would get lucrative contracts to export their metal to the West but not the company itself—he turned them down.

Potanin's rejection meant war. Filatov deployed the whole weight of his three decades as a Soviet industrial boss to fight off the thirty-four-year-old upstart. He fired off a threatening letter to Kokh, he lobbied the Kremlin, he got the local governor to protest the sale. But, somehow, perhaps thanks to his alliance with Soskovets, an even more powerful red baron, Potanin fended him off.

Prevailing over Filatov was the crucial victory. But, back home in Moscow, with the auction set to go ahead, Potanin encountered a final rival. Rossisky Kredit, a bank that had been on the fringes of the springtime consortium, broke away from the pack. In defiance of the tacit agreement that Norilsk Nickel "belonged" to Potanin, Rossisky Kredit mounted a rival bid.

It was doomed from the start. Potanin's bank, Oneximbank, was an official organizer of the loans-for-shares privatizations, even though it was also a participant. Would-be bidders had to register their intention to take part with Oneximbank and place a cash deposit in the private bank as a guarantee of their seriousness.

Did Potanin's role at the heart of the process mean the auction itself was skewed in his favor? He claims it was not; his rivals insist it was. At any rate, on the fateful afternoon of November 17, 1995, when the bids for Norilsk Nickel were opened, Potanin's friend Kokh suddenly discovered an irregularity in Rossisky Kredit's submission. As Kokh, full of shocked propriety, put it in his book: "I smelled a rat."

In the view of this most impartial of judges, the $170 million guarantee Rossisky Kredit had issued to Kont, the company through which it was making its bid, exceeded the bank's total capital. Rossisky Kredit tried to make some new last-minute provisions, but Kokh insisted the rules did not allow it. The bank was disqualified.

That left just three bidders, all of them stalking-horses for Potanin. The starting price for the 38 percent stake was $170 million. Two of Potanin's companies bid $170 million exactly. The third one bid $170.1 million and, just like that, Potanin owned a controlling interest in the world's leading producer of nickel and platinum. A few weeks later, Potanin acquired a majority stake in the second asset on his shopping list—the Siberian oil company, Sidanko—obtaining control of 51 percent for just pennies more than the state's floor price of $130 million. Two years later, British Petroleum would pay more than four times that price for a 10 percent stake in the oil company.

Meanwhile, Khodorkovsky was preparing to claim "his" enterprise: Yukos, another vast Siberian oil company. In contrast with Potanin, Khodorkovsky sought—and achieved—a velvet takeover, winning the cooperation of the company's top management. But, like Potanin, Khodorkovsky feared rival buyers might step in. His nonaggression pact with Potanin meant Khodorkovsky was fairly confident he could fend off Russian rivals. But he was still vulnerable to a wealthy indirect foreign bidder.

Yukos had been classed as a "strategic company," one that foreigners were officially banned from buying, but Khodorkovsky worried that might not be enough. Outsiders might try to find loopholes in the law, perhaps by acting in concert with a Russian company. To neutralize this threat, Khodorkovsky first tried to find his own foreign partner to beef up his bid. But, he told me, his tentative feelers to a few Western banks were frigidly rejected: "They looked at us as if we were crazy." The loans-for-shares scheme was so byzantine and Russia, on the eve of elections that might bring the Communists back to power, was considered such a poor bet that Western banks were not willing to risk their money.

But Khodorkovsky was still worried that some other outside investor might not be so cautious. To keep foreign rivals away, Menatep, Khodorkovsky's group, launched an intense legal and political campaign, spearheaded by Konstantin Kagalovsky, a whip-smart Muscovite with a pink face and floppy, caramel-colored hair. Kagalovsky was perfect for the job: before joining Menatep, he had been one of the young reformers and had gained both an insiders' knowledge of the Russian government and of the West, having served as Russia's representative to the IMF.

A few years later, Kagalovsky agreed to explain to me his technique for keeping the foreigners out. The key, he said, was to ensure that the law banning foreign participation was intentionally vague. It would thus be open to multiple interpretations. If the foreign firms did decide to try to find a legal loophole and make a bid for Yukos through Russian partners, Kagalovsky would warn them that Menatep would take them to court. With a law so open to interpretation, and the home court advantage, Menatep would stand a strong chance of winning.

The whole point, he said, was to transform the decision for foreign firms from a purely legal question—Could they find a legal technicality that would permit them to participate in loans-for-shares?—into a political one—Did they have the domestic connections and savvy to outfox a powerful Russian company in a battle waged in the murky swamp of Russian legislation?

"When the laws are unclear, then you can't simply hire lawyers [and have them decide the issue]," Kagalovsky explained. "You have to decide yourself whether you are willing to run the risk. It was possible to explain this to our competitors."

It was an impressively devious scheme and it worked. But, how, I wondered, had Kagalovsky ensured that the laws had been written in so precisely vague a fashion as to make it legally too risky for foreigners to participate. I assumed, as a matter of course, that Kagalovsky wouldn't tell me, but out of a kind of journalistic duty, I asked anyway.

To my surprise, Kagalovsky gave me a frank, and rather proud, answer: "Well, of course, I wrote the law myself, and I took special care with it."

It was a sort of epiphany for me. In the nearly four years I had spent in Russia by then, I had listened to dozens and dozens of foreign businessmen complain about the country's obscure and fuzzy laws and explain how they were a barrier to investment. It was a really serious problem, everyone agreed, but—with more than a bit of condescension—we Westerners assured ourselves it was part of the terrible legacy Russia had inherited from the Soviet Union. After all, we sagely concluded, surely a new, market-based legal system could not be created overnight.

The one explanation that I don't think occured to any of us foreigners was that maybe the Russians were just as smart as we were, and quite aware of the obscurity of their laws. Blinkered in equal measure by our patronizing attitude and our innocence, I don't think any of us imagined that Russia's laws were vague on purpose; that their obscurity was not an accidental barrier to investment, which would be removed as soon as the ignorant Russians understood the problem, but something quite intentional, with the explicit goal of keeping us out.

Having thus discouraged foreign competitors, Khodorkovsky still faced a domestic challenge. A troika of Russian banks—Rossisky Kredit, which had made the attempt to claim Norilsk Nickel, Inkombank, and Alfa, Friedman's company—decided to make a bid for Yukos. Frustrated by their failure to make inroads against their more established rivals during the first wave of loans-for-shares auctions, the group decided to make their campaign a public and political issue. At least two members of the troika had been part of the Russian business group that first plotted the loans-for-shares scheme in the spring, but now they decided to blow the whistle on their colleagues.

The three banks issued a public statement calling on the government to halt the "ill-prepared and questionably organized" program and accusing Khodorkovsky of being unfairly favored by the Kremlin. Their angry complaint fell on fertile ground. The December 17 parliamentary elections were just a few weeks away and both the left and the right were looking for ammunition to use against the government. The Communists happily seized on the conflict as further evidence that the entire privatization program had been a corrupt and nefarious plot. The liberal opposition was almost equally vociferous. Boris Fyodorov, a former minister of finance and future deputy prime minister, warned that unless the government swiftly called a halt to its "shameful" scheme, complicit ministers were likely to "wind up behind bars."

The game, it would seem, was up. The businessmen's clique had fallen apart; December parliamentary elections were just a few weeks away; politicians of all stripes were attacking loans-for-shares. Surely the government would lose its nerve and, at the very least, postpone the controversial privatizations until after the ballot? Absolutely not. As usual, the criticism served only to harden the young reformers' determination. By questioning the auction process itself, the troika of banks was questioning the integrity of the government and of the young reformers, and that was the one thing Chubais would never countenance.

"The government told us, 'We are going to punish you for kicking up such a fuss,'" Friedman, head of the Alfa Group, said, claiming the authorities dispatched inspectors from the tax service and the central bank to harass his company. "Chubais told me: 'You are putting the auctions themselves in jeopardy, and that is not permissible. It is better for me to have a bad auction than no auction at all.'"

To no one's very great surprise, when the auction for Yukos took place on December 8, the outsider troika of banks found themselves excluded for technical reasons, just as Rossisky Kredit had been. That left the field open to Khodorkovsky, who, acting through Laguna, a front company, won 45 percent of Yukos for $159 million, just $9 million above the starting price. (In a simultaneous "investment auction," Khodorkovsky's team won an additional 33 percent stake in exchange for a pledge to invest $150.125 million.)

There was only one major loans-for-shares auction to go, and it was the most byzantine of all. Its protagonist was Berezovsky. Busy networking, Berezovsky was slow to wake up to the huge financial potential of the loans-for-shares process. But as 1995 rolled on and he watched the scheme transform younger and less well-connected entrepreneurs into world-class tycoons, Berezovsky decided that he wanted a piece of the action.

Getting it would not be easy. Unlike Khodorkovsky and Potanin, who had already spent a few years building up a corporate team and industrial base, Berezovsky was still a nomad. He was brilliant at making the right friends at the right time, but how in the world could he single-handedly take over a huge company and then run it? Berezovsky needed an ally with experience at the coal-face of Russian business and, in 1995, he found one in Roman Abramovich and his team of young turks at Runicom, an oil trading group. The two decided to try to take over an oil company.

But by then it was already late in the game. All the big enterprises were spoken for. With the creativity that marked his ascent in Russian business and politics, Berezovsky found an iconoclastic solution: he decided to create a new company, Sibneft, by combining the Omsk Refinery, one of Russia's best equipped, with a Siberian oil production enterprise, Noyabrskneftegaz. It was a logical combination, Eugene Shvidler, a Runicom trader who became president of Sibneft, told me later, because the refinery, the oil production company, and the oil trading firm had close links already.

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Creating Sibneft may have been an elegant idea, but time was running out. Yeltsin's decree stipulated that the loans-for-shares process must be completed by the end of the year. After that, with presidential elections just a few months away and the appetites of Potanin and Khodorkovsky already satisfied, who knew if the Kremlin would ever again authorize such a giveaway. Desperate to secure his prize before the stroke of midnight, Berezovsky turned to the man who, in that enchanted autumn, was the fairy godmother for all of the future oligarchs—Alfred Kokh.

Late in November, Berezovsky visited Kokh's office and asked what he needed to do to get Sibneft included in the loans-for-shares process. Kokh sketched out a complicated bureaucratic and political process, concluding with the biggest obstacle of all: there was a requisite thirty-day public notification period before the auction could take place. To get his sale in before the end of the year, Berezovsky needed to complete the paperwork by the last day of November—in just three days.

As soon as his afternoon meeting with Kokh was finished, Berezovsky worked out a rough timetable. Every minute counted. Suddenly, he realized he needed to begin lobbying the Kremlin the very first thing the next morning. But, to do that, he needed the right draft decrees. So, even though it was already late, he summoned his armored car and ordered his chaffeur to drive him to Kokh's apartment on Tverskaya, Moscow's glitzy downtown thoroughfare. Russia's privatization chief was already undressed and in bed watching television, but he didn't resent the intrusion.

"I got up, drove to work, sat at my computer, and wrote the draft presidential decree," Kokh told me. "It was in my interests. I wanted to earn $100 million for the [state] budget."

Now the ball was in Berezovsky's court, and all his manipulative talents and political connections would be put to the test. He faced one formidable adversary—Prime Minister Chernomyrdin, who, according to Kokh, was fiercely opposed to the creation of Sibneft and its inclusion in the loans-for-shares process. But Berezovsky had no time left for diplomacy and so, risking a rift with Chernomyrdin, he went to work directly on the Kremlin. There, he argued that he needed to be given Sibneft in order to finance ORT, the television network he already controlled thanks to Yeltsin's largesse. Hopeful that under Berezovsky's influence ORT would act as a sycophantic counterweight to Gusinsky's critical NTV, the presidential clique, including Korzhakov, was readily persuaded.

With Korzhakov's support, Berezovsky somehow managed to electrify the stiff cogs of the Kremlin machine. On November 27, just three days before the last possible moment, a special presidential decree creating Sibneft and authorizing its sale through the loans-for-shares process was signed. With that stroke of the pen, Yeltsin made his publisher an oil baron. The sale itself, on December 28, provoked the by now routine controversy. Unbowed by their previous defeats, the troika of dissident banks decided to make one last stand, this time led by Inkombank. Yet again, the outside contender was disqualified. The group backed by Berezovsky won, with a bid of $100.3 million, just a shade more than the starting price of $100 million.

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Loans-for-shares was such a naked scam, such a cynical manipulation of a weakened state, that—especially now, as a ravaged Russia struggles to rebuild itself—it is tempting to dismiss the rapacious oligarchs who instigated it as just plain evil. Yet, as I watched them plot and profit, I couldn't help asking myself how different the Russians really were from our own hero-entrepreneurs, the gizmo makers and internet tycoons and financial wizards our society so fawningly lauds for producing an era of unprecedented prosperity. Every businessman seeks the most profitable opportunity. Russia's tragedy is that the best opportunity was ripping off the decaying state. Expecting the future oligarchs to forgo that Klondike—to piously retool an ancient Soviet factory or energetically hawk copper bracelets, when they could be taking over vast oil companies—would be like asking the cat to stop hunting mice, or Bill Gates voluntarily to stop decimating his weaker rivals. The future oligarchs did what any red-blooded businessman would do. The real problem was that the state let them get away with it.

Most of the time, the Russian government let the oligarchs get away with murder because it was too weak to stop them. But with loans-for-shares, there was a further twist. The young reformers created the oligarchs, thinking they could harnass their avarice and their cunning astucia to their own ends—first by employing them as a wrecking ball against the red directors, and then by using them as a tool in the 1996 presidential campaign. But eventually, and maybe inevitably, it went wrong. As Aleksei Ulyukaev explained, "We were like Doctor Frankenstein and they were the monster."