RUNNING IN PLACE:
THE LATEST ROUND OF RUSSIAN ECONOMIC MODERNIZATION

RUSSIA POLITICAL ECONOMY PROJECT

FOREIGN POLICY RESEARCH INSTITUTE
MARCH 2018

The Foreign Policy Research Institute thanks the Carnegie Corporation for its support of the Russia Political Economy Project.

COVER: Matrioshka with coins, Adobe Stock.

Foreign Policy Research Institute

Mission

The Foreign Policy Research Institute is dedicated to bringing the insights of scholarship to bear on the foreign policy and national security challenges facing the United States. It seeks to educate the public, teach teachers, train students, and offer ideas to advance U.S. national interests based on a nonpartisan, geopolitical perspective that illuminates contemporary international affairs through the lens of history, geography, and culture.

Educating the American Public: FPRI was founded on the premise than an informed and educated citizenry is paramount for the U.S. to conduct a coherent foreign policy. Today, we live in a world of unprecedented complexity and ever-changing threats, and as we make decisions regarding the nation's foreign policy, the stakes could not be higher. FPRI offers insights to help the public understand this volatile world by publishing research, hosting conferences, and holding dozens of public events and lectures each year.

Preparing Teachers: Unique among think tanks, FPRI offers professional development for high school teachers through its Madeleine and W.W. Keen Butcher History Institute, a series of intensive weekend-long conferences on selected topics in U.S. and world history and international relations. These nationally known programs equip educators to bring lessons of a new richness to students across the nation.

Training the Next Generation: At FPRI, we are proud to have played a role in providing students – whether in high school, college, or graduate school – with a start in the fields of international relations, policy analysis, and public service. Summer interns – and interns throughout the year – gain experience in research, editing, writing, public speaking, and critical thinking.

Offering Ideas: We count among our ranks over 120 affiliated scholars located throughout the nation and the world. They are open-minded, ruthlessly honest, and proudly independent. In the past year, they have appeared in well over 100 different media venues- locally, nationally and internationally.

FPRI

Foreign Policy Research Institute

ABOUT THE AUTHOR

Yuval Weber, PhD, is the inaugural Kennan Institute Fellow at the Daniel Morgan Graduate School and also serves as a Global Fellow at the Woodrow Wilson Center. Dr. Weber previously served as a Visiting Assistant Professor in the Department on Government at Harvard University and is currently a Center Associate at the Davis Center for Russian and Eurasian Studies at Harvard University. He is currently on leave from the Faculty of World Economy and International Affairs at the National Research University – Higher School of Economics (Moscow, Russia). Dr. Weber is working on a project on the sources of liberal and anti-liberal dissatisfaction for powers in the international system and the strategies they employ to stake their claims for revising the international order. The first manuscript under contract (Agenda/Columbia UP) evaluates the tension between demands of economic modernization and the security state in Russian political economy. His work has appeared in *Problems of Post-Communism*, *International Studies Review*, *Survival, Cold War Studies, Orbis: FPRI's Journal of World Affairs,* and the *Washington Post*.

Executive Summary

Yuval Weber

"There's no money, but hang in there!" — Prime Minister Dmitri Medvedev's now infamous exhortation to a group of Crimean pensioners crystallizes the familiar and onerous reform environment confronting President Vladimir Putin. He faces the same set of choices as has many Russian leaders before him, having to balance the demands of the security state and the needs of economic modernization.

This paper sets out three tasks. First, I show that ahead of the March 2018 elections, Putin has acknowledged dissatisfaction with the economy and solicited three discrete plans for turning around growth. The first proposes reduced state intervention in the economy to free up entrepreneurs. The second advocates increased state intervention to jump-start the economy. The third seeks no radical changes, betting instead on Russia's ability to better use existing resources. The last time he was in this position, Putin declined to make a clear choice between rival plans, instead seeking to increase the power of the state over economic actors instead. Finally, I argue that he is likely to repeat this tactic, providing enough economic reform to appease demands for change, but not enough to alter the state's position as the source of economic opportunity, leading to a reaffirmation of the state over the market.

Reform in the Era of "Hang in There"

In May 2016, two years after welcoming Crimea into the Russian Federation following the peninsula's disputed secession from Ukraine, Prime Minister Dmitri Medvedev visited the newly acquired jewel of Russia's regional security policy. Russian politicians undoubtedly possess many talents, but the sort of common-touch, person-to-person politicking that Boris Yeltsin and Viktor Chernomyrdin excelled in has not been common under Vladimir Putin's presidency. Medvedev found himself in the center of a scrum of older women uninterested in discussing the merits of Russia's geopolitical challenge to the Western liberal order. These pensioners were angry that the government's promises of indexing pensions to keep pace with inflation had not been kept—a particularly sore issue given that Russian officials had promised such inducements in March 2014 to urge Crimean residents, like these women, to vote to join the Russian Federation.

The interaction between one of these women and the prime minister illustrates the difficulties of economic reform at a time of foreign policy turbulence (To Medvedev's everlasting regret, the episode also entered the pantheon of Russian political humor.). She started yelling at the prime minister, complaining that her pension was only 8,000 rubles (then $119). She exclaimed, "You damn well said that there will be indexation, where is it in Crimea, this indexation? What is 8,000? It's miserly. They're wiping their feet on us here!" Medvedev attempted to argue that it was impossible to index pensions to inflation in just one place. That is, Crimea couldn't get special attention—a new and wholly unwelcome claim compared to the pre-referendum promises. The woman responded that "One cannot survive on this pension, prices are out of control!" Sensing that this interaction with a shouting *babushka* was veering wildly out of control, Medvedev responded, "There is no [indexation] anywhere. We haven't done it, simply because there's no money. We'll find the money, and we'll do the indexation. You guys hang on here, best wishes, and cheers, take care!"

Medvedev's exhortation to the Crimean pensioners—"There's no money, but hang in there!"—crystallizes the difficulties defining Russia's political economy: balancing an expansive foreign policy and economic revitalization under a series of serious, and often conflicting, challenges. The result is a familiar and onerous reform environment confronting Putin and his next government.

This report introduces and examines Russia's dilemma of economic reform. It explains each of the three main reform paths on offer and evaluates the political consequences for Putin. The first option is a classically liberal approach advocated by Alexei Kudrin, who served as Finance Minister from 2000 to 2011. The second option is a statist intervention approach advocated by Boris Titov and Sergei Glazyev, the President's Commissioner for Entrepreneurs' Rights (business community ombudsman) and the President's Advisor on regional economic integration, respectively. The third option is the government's placeholder status quo approach led by current Economy Minister Maxim Oreshkin. These competing approaches—less state intervention in the economy to free up entrepreneurism, more state intervention to jump-start the economy, or simply seeking growth through productivity gains via better utilization of existing resources—form Putin's set of choices.

A central theme to all problems facing Putin and Russia was the question "how much market can we handle?"

The choices facing Putin are familiar. He has been here before, albeit in a far less difficult security environment. As explored below, when Putin first took power in 2000, he faced numerous questions about how to balance competing government objectives: introducing market mechanisms to wean the economy off Soviet habits and pathologies, while also protecting citizens and stakeholders from the consequences of too-rapid competition. At the time, there was a dizzying array of problems to address: managing the recovery from the August 1998 ruble collapse, restoring the collapsed supply chains across the country and across the Commonwealth of Independent States, and handling macroeconomic issues like the country's massive debt load to the International Monetary Fund (IMF) and size of social insurance programs such as pensions and food subsidies.

A central theme to all of the problems facing Putin and Russia was the question of "how much market can we handle?" One key issue was the country's monotowns, the industrial centers scattered inefficiently across the country by Soviet planners. The choice of whether to abandon them or keep them going cut to the heart of Russia's political and economic debate because the political and moral versus economic choices were both clear and contradictory. Putin drafted economic bureaucrats with opposing viewpoints to devise competing plans. The first plan proposed cutting off subsidies and allowing market conditions to put factories out of business while the government helped people move away. The second envisioned the use of government funding to maintain the status quo and diversify slowly. Instead of picking a clear side, Putin created an ad hoc, mixed approach that balanced viewpoints and forced compromises upon all. In Russia's informal political environment, this public decision to split viewpoints and place the state at the center of the issue signaled to other political and market participants how Putin was going to address the far bigger and thornier issues in Russian political economy.

In the relatively benign external security environment of the early 2000s, even limited economic reform was rewarded. The current effort of Russian authorities takes place under a very different external security environment, making the necessary reforms much more difficult. This policy brief performs three tasks. First, it serves as a guide to understanding the political context of the reform plans from 2018 onwards evaluating the structure of economic reform in Russia, where expansive foreign policy commitments and authoritarian domestic politics leave only limited space for modernization efforts. Second, this report reviews Putin's last serious effort at economic reform, which suggests that he will consider all plans, delay as long as possible, and then choose elements from each, mindful of the difficulties posed by external pressure. As observers of the president have often noticed, Putin likes to postpone decisions to allow other actors to reveal their cards first. Finally, it explains the reform plans currently in front of the president. Recognizing the political context of foreign policy expansionism and apathetic public opinion, the choices, personalities, and consequences of each potential path are outlined. The reports concludes that Putin will enact sufficient structural reforms to suggest seriousness and prudence, but then relax these reforms where they generate significant bureaucratic or popular dissatisfaction. At that point, the government will hope that it can revert to the previous status quo.

Putin likes to postpone decisions to allow other actors to reveal their cards first.

The underlying theme of this report—and Russia's political economy overall—is that change will only be pursued when the alternatives are far worse. Vladimir Putin's conservative leadership style reflects the tried-and-true practices of Russian governance: reliance on the state, the bureaucracy, and international glory in place of power-sharing and a wider distribution of resources. Such governance, however, presents a familiar political dilemma—the combination of a faltering economy, a closed political system, and an activist foreign policy pulling the leadership in opposite directions.

Endnotes

1 "Медведев пенсионерам в Крыму: денег нет, но вы держитесь [Medvedev tells pensioners in Crimea: there's no money, but hang in there]," Radio Svoboda, May 24, 2016.

Economic Modernization vs the Security state

The demands of economic modernization and the demands of the security state have pulled Russian leaders in opposing directions for centuries. While this report chiefly evaluates the reform environment ahead of the March 2018 presidential election, it is worth noting that Putin finds himself in a situation that is not unfamiliar.

Throughout history, Russian leaders have approached the market tentatively, recognizing that a loss of central economic control runs counter to the demands of the security state. This highly centralized and bureaucratic Russian state dates back to the imperial period. The tsarist economy was fairly autarchic, and the Soviet economy even more so. While both political systems allowed episodes of reform, they were not pursued because leaders wanted pro-market change. Rather, the alternatives—falling behind geopolitical competitors and losing domestic power—were clearly more dangerous.

When even limited marketization threatened the ruler's ability to distribute rents or control the structure of economic opportunity, a turn away from the market and towards greater statism and bureaucratization often occurred. For Pyotr Stolypin, Vladimir Lenin, Alexei Kosygin, and Mikhail Gorbachev, attempts to strengthen market mechanisms resulted in losses of power or policy reversals by subsequent leaders. As Table 1 shows, the authorities have pursued economic reform on a number of occasions — each of them ending in explicit failure.

All of these leaders, however, recognized that they operated in difficult external security and domestic political environments, similar to Vladimir Putin's current—but not early 2000s-era—situation. In these situations, strategic retrenchment could alleviate international tension and reduce the need for military spending, but doing so unilaterally would identify the limits of Russia's capabilities and the maximum extent of the leader's bargaining positions. On the domestic side, allowing political competition could bring opposition forces and the public into governance and thus reduce dissatisfaction. Yet, in this outcome, Putin runs the risk of losing political power and seeing the next leader and his entourage use the powers of the state to expropriate the current leader and his entourage.

If diplomatic retrenchment and political openness are not possible, then the government must turn to economic reform to alleviate social dissatisfaction. Modernization in Russia is a top-down process by which leaders, otherwise upholding the status quo, attempt to maintain power through the promise of economic growth.

Modernization in Russia is a top-down process by which leaders attempt to maintain power through the promise of economic growth.

That is, Putin is in the same position as many modernizers before him. The country's foreign policy—specifically its muscular grand strategy of challenging the international order—is a central base of Vladimir Putin's legitimacy. Indeed, the Russian leader personally boasted that the Crimean gambit illustrated how Russia "had risen from her knees."[1] Additionally, after eighteen years in power and where the Duma does not have a single deputy who is not either in the government's United Russia "party of power" or to a loyal opposition party, there are no alternative sources of legitimacy from within the government to draw policy ideas or forge consensus.

This context defines the current iteration of modernization in front of Putin. He could either retrench from foreign policy positions in Ukraine, Syria, and elsewhere, or allow political competition. Both would help to relax tensions with the West and possibly lead to economically beneficial sanctions relief. Yet, either option poses unacceptable risks to Putin's hold on power. While retrenchment makes sense economically—eliminating sanctions, reducing international isolation, limiting the draw of capital flight, and opening the country to foreign investment—it would make the privation and isolation experienced thus far appear in vain. Allowing political competition risks either suffering an attack from insiders or seeing a non-systemic successor investigating Putin and his subordinates.

Certain aspects of modernization will be easier to pursue relative to past attempts as Russia boasts solid macroeconomic fundamentals from mainstream, macroeconomic policies pursued in the early 2000s. However, the economy is stuck in boom-bust cycles springing from familiar structural maladies: an over-reliance on energy exports, poor diversification, corruption, inefficiency, and inconsistent public good provision.

The result is that expanding foreign policy commitments into Ukraine and Syria (and allegedly into the electoral processes of adversaries) have raised the political costs of retrenchment. Any unilateral concession on these issues to improve economic relations with Russia's main trading partners would identify the limits of Putin's foreign policy akin to Mikhail Gorbachev's policies in Eastern Europe in the late 1980s. Yet, recession and stagnation have raised the opportunity costs of maintaining increasingly autarchic economic policies. In the early 2000s, Putin faced these economic issues but not the security ones. Discussing Putin's tenure and actions in the early 2000s may help to show what policies Putin might pursue during Russia's latest, and his second,

Table 1. Previous Reform Efforts

Pre-Revolutionary	Sergei Witte & Pyotr Stolypin
Sergei Witte and Pyotr Stolypin pursued efforts to transform pre-revolutionary Russia from the semi-feudal, semi-industrial state into a modern industrialized economy with private ownership of agrictultural land by the peasantry to alleviate the social dissatisfaction expressed before and during the 1905 Revolution. They ran into considerable difficulties when sustatining those reforms (particularly social justice, monetary, and land reforms meant to empower peasants and the fledging bourgeoisie) meant undoing the Tsar's monopoloy on political power.	
Post-Civil War	**Vladimir Lenin**
Vladimir Lenin's New Economic Policy recognized the danger to the Revolution posed by the effects of War Communism, leading him and later Nikolai Bukharin to reintroduce selected elements of market exchange to encourage peasants to bring more food to market and alleivate urban privation. Following Lenin's death, Bukharin continued the policy until Joseph Stalin took power. Stalin then repressed Bukharin and other rivals, and re-introduced agricultural collectivization, promoted rapid industrialization, re-nationalized the means of production, and promulgated central planning to end any market element in the Soviet economy.	
Post-Stalin	**Alexei Kosygin & Evsei Liberman**
Alexei Ksygin and Evsei Liberman spearheaded "cybernetic" domestic price and market oriented reforms in the mid-1960s to reintroduce prices, the profit motive, and, quite tentatively, unplanned industrial economic activity. In effect, they advocated moving from Stalinist orthodox Marxist economics that could no longer be sustained without coercion and from Nikita's Khrushchev's idiosyncratic passions to "optimal planning" and emphasis on mathematical models and cybernetics. These reforms were shelved when large-scale production of oil allowed policymakers to revert back to administrative methods of economic planning	
End of the Cold War	**Mikhail Gorbachev**
Mikhail Gorbachev engaged in probably the most radical "restructuring" of the Soviet economy to break it out of its moribund state in the late 1980s. These efforts included trying to replicate Deng Xiaopeng's concurrent agricultural reforms in China, opening up private commercial activity, and retrenching from extensive and financially ruinous military spending levels and diplomatic commitments in the Eastern Bloc and in the Third World with the intent of creating a "market socialism" to increase domestic consumption. These efforts led to a conservative coup d'etat that eventually led to the collapse of the entire country.	

attempt at major economic reform.

Putin's Reform Style, 1990s Edition

The Russian economy has recovered from the last recession that began in 2015. The worst of the oil price crash and post-Crimea sanctions have been taken in stride, but the political imperative to do something puts Vladimir Putin in a delicate situation. There must be enough reform to justify his continued rule, yet as highlighted above, too much reform can unleash public demands for political change or opposition from within the elite.

Vladimir Putin has been in this situation before. Upon his selection as prime minister in 1999 and almost immediate elevation to president, Putin's concerns revolved around *internal* and *regional* security: a series of mysterious bombings around Russian cities, a renewed war in Chechnya, and an uncertain diplomatic relationship with the United States. All of these concerns were addressed: the bombings stopped after Putin assumed office; the war turned tides once a new "Chechenization" strategy saw a local leader, Akhmad Kadyrov, willing to work with Russian authorities against the common Islamist enemy; and the September 11 attacks provided an opportunity to deepen cooperation with the United States. In a more favorable security environment, Putin then turned to Russia's institutional and industrial inheritance, which, unresolved since Gorbachev began *perestroika*, had helped precipitate the financial crash of the late 1990s. This experience is instructive for contemporary debate.

The key issue in the early 2000s was what to do about the Soviet legacy of industrial allocation, a system motivated by defense and political concerns outdated after the collapse of the Soviet Union. Putin convened two important political actors—Minister of Economic Development and Trade Herman Gref and Governor of Khabarovsk (in the Russian Far East) Viktor Ishaev—to generate long-term state development strategies. Gref represented the liberal, market-oriented school of thought, while Ishaev represented the state capitalist viewpoint.

Even while most political actors at the time were committed to markets and modernization, they differed in how to induce competitiveness. The liberals wanted to challenge the spatial misallocation of Soviet industry by ending the special privileges accorded to monotowns. Migration, they argued, would undo the poor decisions of the past. This strategy would include eliminating subsidies, liberalizing energy sectors to introduce market prices and reduce wastefulness, and ridding industry of special protections to allow winners and losers to emerge endogenously. On the other side were the regional governors who wanted to modernize their cities through budgetary transfers and who rejected the principle of market-led depopulation. In effect, they advocated a go-slow approach on reform to reduce social dislocation. The former position fell in line with international norms, but the experience of the 1990s had soured many on excessive reliance on the market. The latter position promised greater stability, but also a continuation of the sorts of policies that had so clearly

Vladimir Putin meets with Rosneft CEO Igor Sechin. (Source: Kremlin.ru)

reduced direct individual payments for people in the most remote regions. For the conservatives, the government affirmed its commitment to large-scale industrial enterprises to prevent the proliferation of ghost towns. This mixed strategy confirmed the state's central role in "promoting growth, revitalizing core industries, and reforming and regulating natural monopolies. While supporting liberal ideas about introducing competition into natural monopolies, [Putin] ultimately sided with an activist strategy that privileged select national champions or strategically important enterprises" for eventual entry into global and regional markets.[2]

These efforts showed that Putin could recognize the context of a problem, identify the relevant stakeholders advocating divergent policy prescriptions, and yet maintain the center's predominance by pushing through a mixed solution. Within a few years of this episode, the dramatic upturn in energy prices and the government's expropriation of key oil assets such as Yukos alleviated the government's financial difficulties considerably. It is this experience that will be called upon for the current crisis, wherein a faltering economy and social dissatisfaction are similar, but the external environment is far more threatening.

Endnotes

1 Constantine Pleshakov, The Crimean Nexus: Putin's War and the Clash of Civilizations (New Haven: Yale University Press, 2017), p. 64.
2 Susanne A. Wengle, Post-Soviet Power (Cambridge: Cambridge University Press, 2015), p. 91.

Putin's Current Dilemma

Unlike the early 2000s and the opportunities provided by a fresh start following an unpopular predecessor, Putin now faces a very different set of conditions to pursue reform. First, he will soon enter his third decade of rule and faces term limits in 2024. He needs to protect his legacy, appease a large swath of political supporters, and prepare public opinion for political change: his own retirement, another placeholder like Medvedev from 2008-2012, a constitutional amendment permitting another presidential run in 2024, or a new constitutional structure placing him at the head of some sort of governing council. The data presented below shows the weariness of the Russian electorate, who are being asked to turn out and vote for the president at levels far beyond what public opinion suggests is possible. Another key issue is what numerous political commentators describe as the president's growing fatigue with domestic politics and increased concentration on foreign policy.

Russia's muscular foreign policy and weak economic performance create a difficult environment for reform.

This robust and expansionist foreign policy has created a largely adversarial relationship with Europe and the United States, the traditional sources of foreign direct investment (FDI), technology, and expertise. Additionally, Russia's partnership with China to bolster mutual political and economic objectives has been met with more rhetorical approval from Beijing than material benefits. The incipient partnership has seen Russian political support for China's Belt and Road Initiative trade routes through Central Asia, yet Chinese FDI has yet to alter the structure of bilateral trade away from natural resources going east in exchange for finished products going west. Most Asia-originated investment into Russia comes from Singapore and Hong Kong, likely indicating Russian re-investment via offshore tax havens.

Russia's muscular foreign policy and weak economic performance create a difficult environment for reform. Yet, public dissatisfaction with the economy has emerged as the central theme of the March 2018 presidential elections. The Levada Center, Russia's only independent polling agency, indicates the extent of public anxiety over the economy since the Ukraine crisis began. In Figure 1, nearly 80% of respondents agree that Russia is probably or definitely in an economic crisis. Even more worrisome is Figure 2. Longitudinal data from the Russian Academy of Sciences Institute of Sociology shows that for the first time since 1999—prior to Vladimir Putin's selection as prime minister—more Russians want substantial change rather than stability. Even in a state without vibrant political competition, Putin cannot ignore the median voter. His legitimacy relies on mass electoral turnout to demonstrate an overwhelming mandate and prevent potential rivals from shaping his departure. This is why he needs to identify and at least attempt to pursue a modernization agenda. If he cannot convince regular people that life will be better with him, then his real base—the super-wealthy, the *siloviki* (people from the security services and military), and the bureaucracy—will begin to make plans without him.

Putin's chief domestic concern is the relative apathy shown by the population for a fourth official mandate. As of December 2017, public opinion polling indicates that only 58% of Russians intend to participate in the upcoming election (24% for sure and 34% likely), with 53% of all eligible voters expressing a preference for Putin. This implies that Putin's vote share might not exceed one-third of the total electorate by the time of the vote.

A key difficulty for the president is motivating voters concerned about the economy. Studies show that Russians are peculiarly sensitive to economic anxiety relative to their peers. Although pocketbook concerns exist in most countries, Russians consistently report greater "survival" versus "self-expression"

Figure 1. Do you agree or disagree with the opinion that Russia is currently experiencing an economic crisis

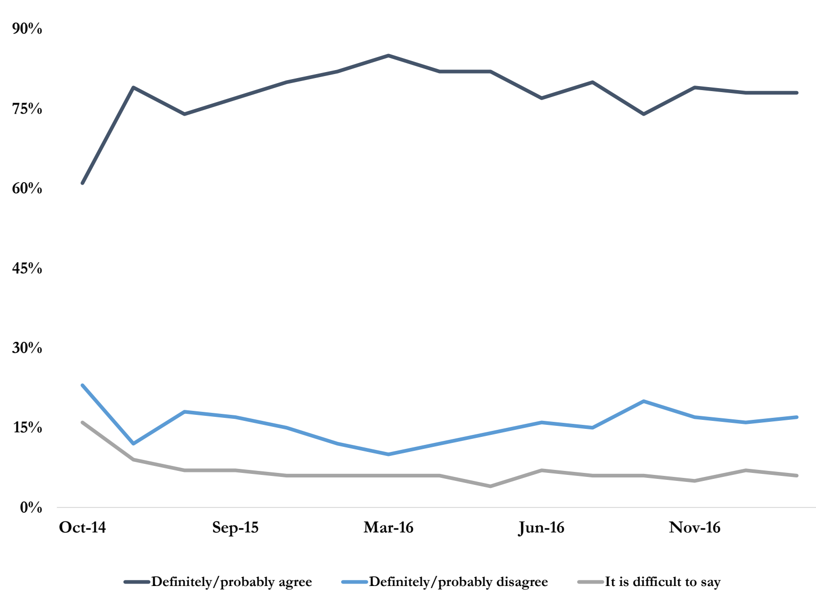


Figure 2. Do you believe that Russia needs substantial chagnes, or does it need stability?

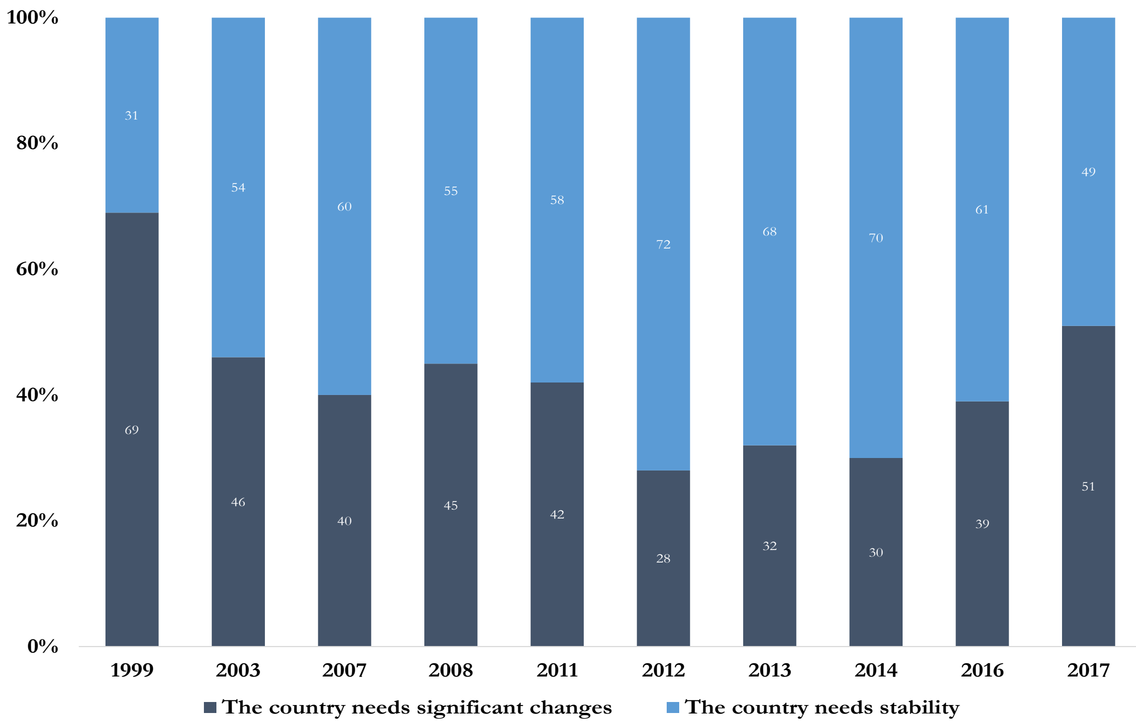


Figure 3. What do you believe are the main problems in society today? (Multiple answers possible)

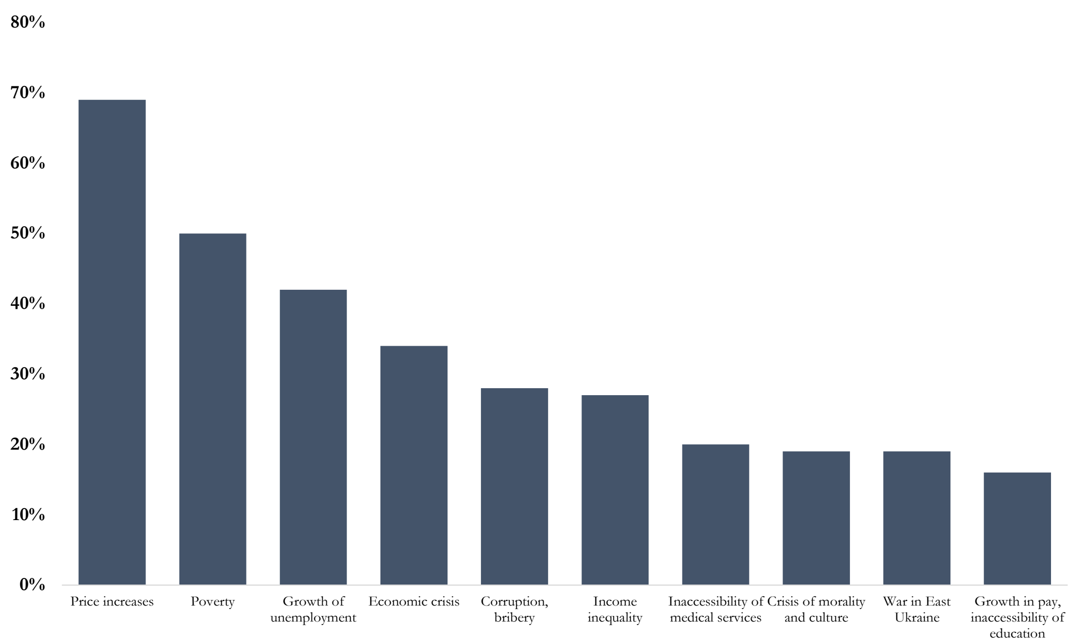


Figure 4. Dmitri Medvedev approval ratings

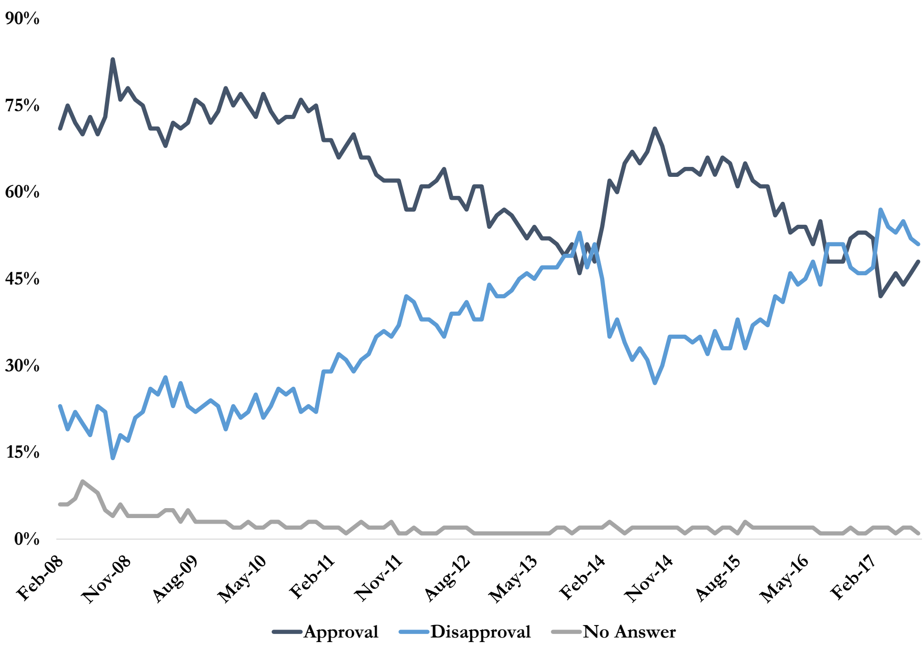


Figure 5. Government of Russia approval ratings

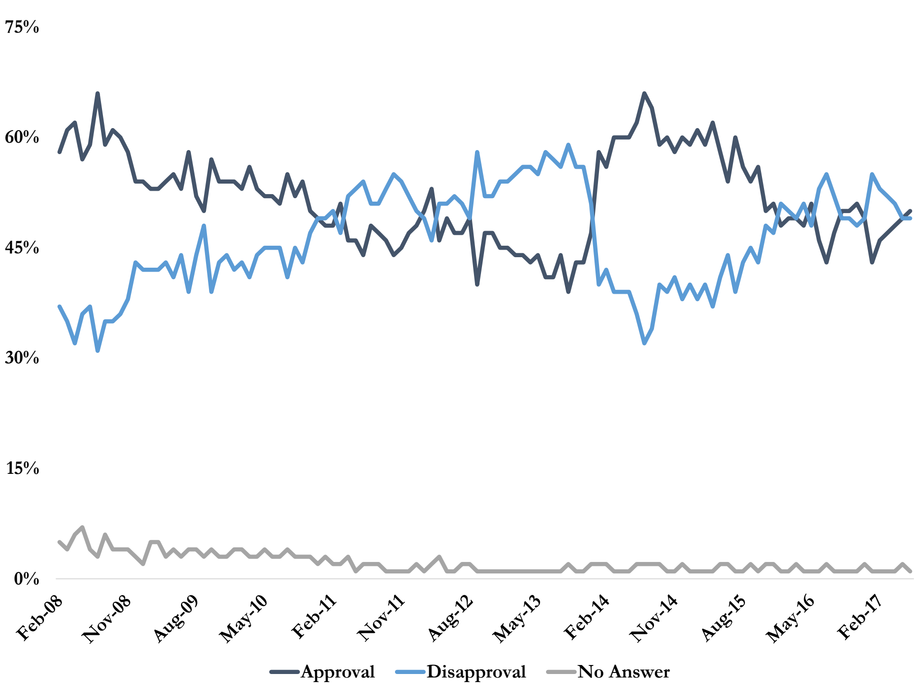


Figure 6. Economic Protests

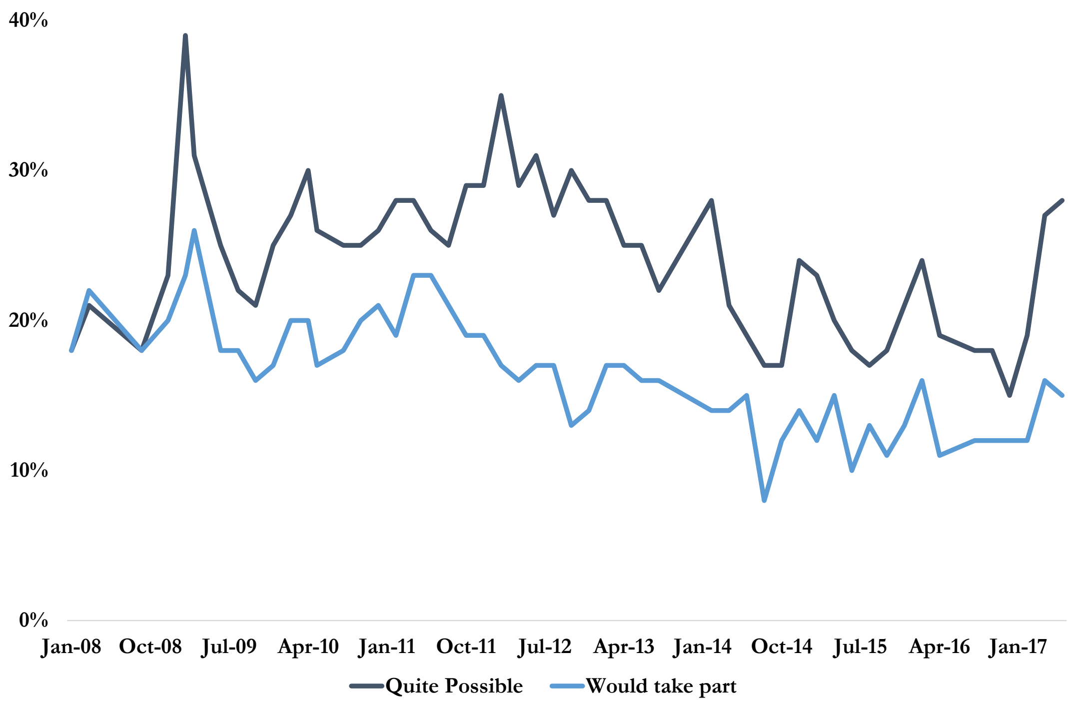


Figure 7. Political Protest

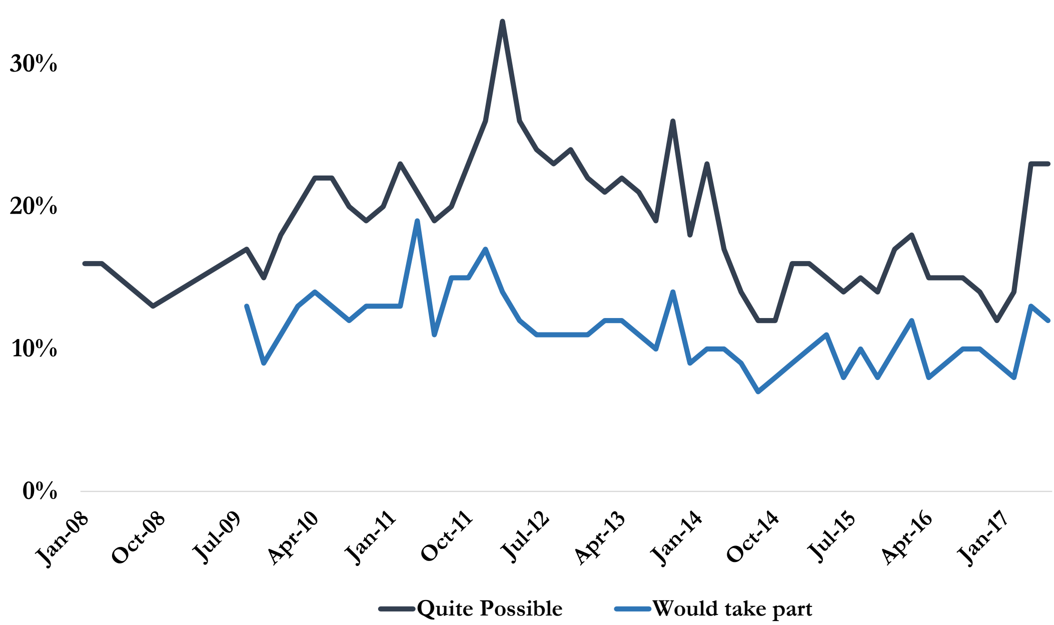
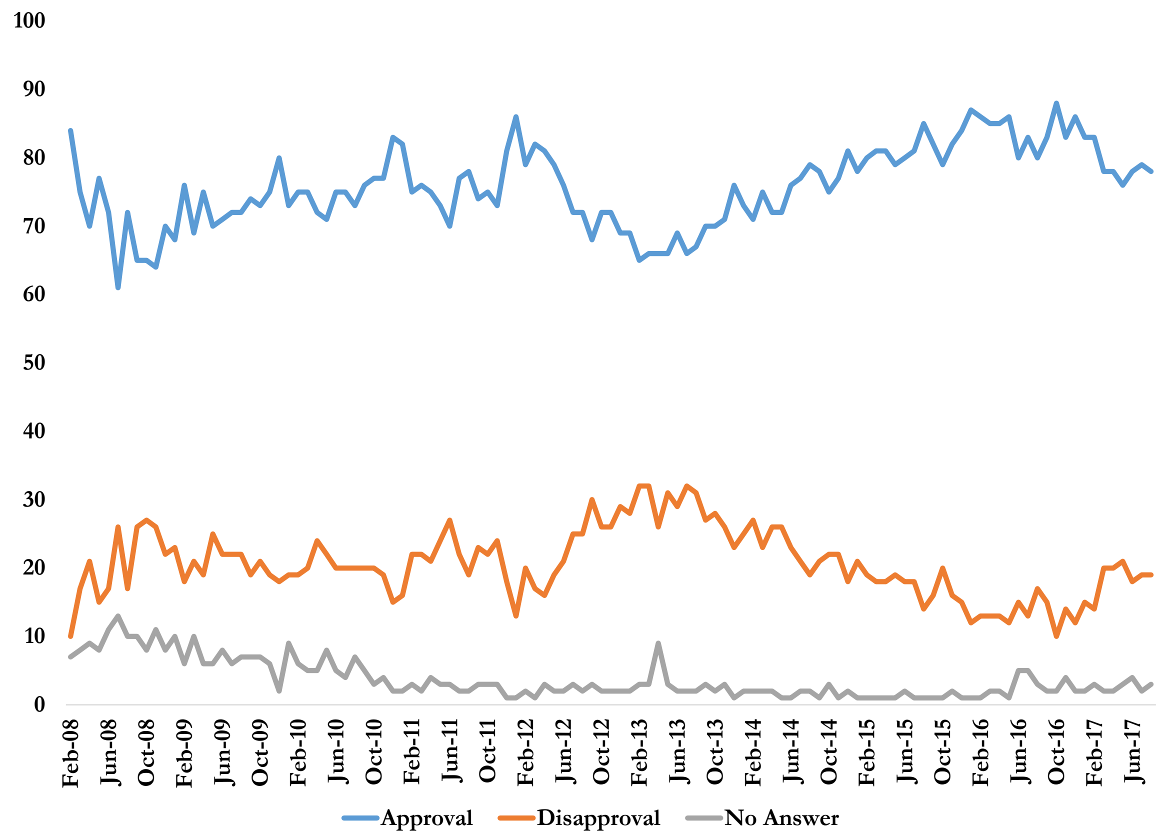


Figure 8. President Putin's Approval Ratings



values than countries with similar levels of national wealth and similar "survival" values to countries in far worse economic shape. The difficult political history of the last century (revolutions, civil war, collectivization, purges, invasion, stagnation, state collapse, post-imperial contraction, and economic crisis) has produced a population both fairly resilient yet exceedingly sensitive to relative declines in consumption.

Figure 3 reveals the full economic anxiety of the Russian population, whose top concerns in a multi-choice survey betray apprehension over the current state of the economy: price increases; the impoverishment of the majority of the population; unemployment growth; the poor state of industry and agriculture; corruption, bribery; sharp stratification of the rich and poor/the unfair distribution of income; and inaccessibility of many types of medical services, to name a few.

This economic anxiety has filtered up to Russia's political leaders, escaping Putin only. In a classic "good Tsar, bad boyars" effect, the president routinely scores above 80% approval ratings. Yet, only about half of the electorate is motivated to vote for him. Journalists going into Russia's heartland routinely find apathy for the president. Nataliya Vasilyeva of the *Associated Press* quoted a pensioner and former Putin voter in the Siberian city Novokuznetsk saying, "Change? If he could do it, he would have done it by now. If nothing gets done, then maybe we will need a new person."[1] If Putin cannot convince such voters that he has a plan, his political future will become increasingly difficult.

Other politicians and political institutions find support similarly tepid. Figures 4 and 5 show approval ratings for Dmitri Medvedev—the junior member of the "tandemocracy" ruling the country and the second-most well-known figure in Russian politics—and the government to be a net negative for the entirety of 2017. Each has lost the post-Crimea "rally around the flag" bump. Moreover, Figures 6 and 7 show that public opinion on the possibility of economic and political protests—as well as individuals' potential participation in them—has also risen, indicating latent weariness with the status quo and lack of political options.

Endnotes

1 Nataliya Vasilyeva, "In Putin's Heartland, Apathy and Disappointment Rule," *Associated Press,* December 11, 2017, https://apnews.com/938d1cd74ed24ca583daf95d7c23beab.

The Plans in Front of the President

In this environment, Putin has commissioned several long-term development plans on how to break the economy out of its rut. The plans have been solicited from two think tanks and from the government itself. Drawing on the political strategy of the Gref-Ishaev debates in the 2000s, Putin aims to engage the entire elite in the reform process. Seeking input from both inside and outside of the government deters any malcontents from challenging the process ahead of the March 2018 elections.

The three plans can be broadly categorized as a "stay the course" effort led by Economy Minister Maxim Oreshkin, a more radical liberal plan developed by Alexei Kudrin, and a statist interventionist plan advocated by Boris Titov and Sergei Glazyev. These competing approaches—a relatively centrist approach located between a more libertarian view of removing the state as much as possible from the economy and a more populist approach to heat up the economy—provide the range of politically appropriate modernization strategies. As detailed below, each have clear ideological underpinnings and are identified by their chief avatars and supporters. Alexei Navalny, Russia's leading "non-systemic" political opposition figure, also has a plan to modernize the Russian economy. His plan, addressed in Box 2, is far more radical and completely outside of the political mainstream. However, Navalny does not cooperate with the government or with Putin, so his plan is not currently being considered by Putin's regime. Navalny is also not permitted to run against Putin in 2018, but he represents a highly confrontational anti-corruption point of view in Russia. While his overall support is quite low, he has been able to organize both specific events and a political movement across the entire country in ways professional politicians have not been able. Should any bureaucrat not appreciate or agree with Putin's decision on reform, Navalny poses a different threat altogether.

The government's plan has not been officially released, but Oreshkin, only 35 years old and touted as a potential future prime minister, has been laying out the main points of his proposal in recent months. Unsurprisingly, he defends the government's current policies and advocates deepening them, arguing that recent growth will benefit from continuity. His chief goal is increasing total factor productivity and getting more out of the existing Russian economy. This plan offers a significant political benefit: it supports the claim that the government has been doing its job correctly and blames external factors, such as Western sanctions, for sabotaging economic

Vladimir Putin meets with Economy Minister Maksim Oreshkin. (Source: Kremlin.ru)

success.

The primary elements of Oreshkin's plan include continuing import-substitution industrialization to reduce reliance on foreign trade, excluding bureaucratic input on specific investment decisions, emphasizing the digital economy and macroeconomic stability, increasing labor productivity, and creating a stable business environment by pledging to introduce no new corporate taxes.

This reform plan argues that the fundamentals of the economy are strong, yet more time is needed to allow the private sector to return to previous levels. The ideological underpinning is that state capitalism and reliance on traditional virtues, such as stability, the state, collective self-reliance, and patriotism, will carry Russia through this difficult period. To that end, Oreshkin has also proposed greater transparency of economic statistics (although taking Russia's Statistical Service, Rosstat, as a department under his own ministry might have the consequence of generating excessively rosy results) and funding "pilot projects for selected companies that might have costs and consultants covered . . . [to include] a package of tax discounts on investment loans, discounted lease programs and loans with interest as low as 1% granted by the Fund of Industrial Development (FRP)." As the plan advocates the status quo and does not address the immense growth of the bureaucracy, security services, and military-industrial complex, it is supported by those benefiting from the system and "systemic" liberals—a very broad cross-section of the government, big business, and the *siloviki*. Despite Medvedev's alleged concern about the rising profile of his junior colleague, he has given the plan his implicit approval.

From the "think tank" world, there are two more radical plans that define the outer limits of potential reform. First is the liberal position, encapsulated in the Center for Strategic Research's plan advanced by Alexei Kudrin. The former Finance Minister, who left government in 2011 over a disagreement about defense and social spending, espouses a classically liberal approach to economic reforms. Kudrin advocates reducing defense spending, distributing government resources to health and education to raise human capital, increasing transport infrastructure spending, lowering inflation and budget deficit targets, reducing the government workforce, and raising the pension age. The program shares many of the transparency and business environment stability goals of the government plan.

The similarities between this program and Kudrin's policies as Finance Minister are clear. The plan notably does not shy away from one of the key reasons Kudrin left government—his conviction that the state should prioritize social spending over geopolitics. Kudrin believed that then-President Medvedev's plans to bolster the military and security services would lead to economically unproductive uses of oil money. This plan recognizes the ultimate consequences of Medvedev's fiscal decisions—a socially unsustainable imbalance between guns and butter.

As one might expect, this program is supported by the "non-systemic" liberals and most professional economists opposed to the easy money Stolypin plan. The military and security services—unwilling to cut into their own budgetary priorities—have strong objections. The ideological underpinnings of the plan are clear: it aims to make Russia's political economy less unique and more in line with Western norms.

On the opposite end of the ideological

Table 2. Alexei Navalny's Campaign Promises

Source of Revenues
• Fighting corruption through expropriation of state officials, reducing the state bureaucracy, cutting subsidies to state corporations. • Raising taxes on the gas sector, on dividends paid by the state companies, on previously privatized state resources, and on luxury items.
Economic Goals
• Establishing a minimum wage of 144 rubles ($2.45) per hour or 25,000 rubles ($424) per month. • Raise monthly pensions by 54% to 20,000 rubles ($340). • Lowering the mortgage rate from 11% to 2%. • Doubling federal spending on healhcare and education. • Ban warrantless raids and life taxes on small businesses. • End the draft and cut Russia's military budget in half, shifting resources to increasing professional soldier's wages. • Reduce or eliminate the number of state officials, law enforcement and judicial officials, and mass media "propagandists."

spectrum lies the Stolypin Club has put forth a robust state-interventionist plan. Led by Boris Titov (state business ombudsman) and Sergei Glazyev (advisor to the president on Eurasian regional integration and long-time advocate of populist, command-style economics), and championed by Andrei Belousov (assistant to the president in economic affairs), this plan identifies low demand as the cause of sluggish growth. These statists want the government to inject at least 1.5 trillion rubles ($26 billion USD) into the economy through a combination of budgetary funds, contributions from the Central Bank, state orders, and lower interest rates. This would represent a stimulus equivalent to 11% of Russia's 2017 budget. Additionally, they seek to end the ruble's free float and limit "speculation" on the currency. They call for greater government intervention into all parts of the economy: export assistance across sectors, food and medicine subsidization, and a reduction of tax and tariff burdens for infrastructure and raw material monopolies. Finally, they advocate for the business community, calling to reduce criminal prosecution of business disputes and to diminish the state's ability to conduct extortive "regulatory" checks.

This plan is notable for heavily discounting the future by maximizing present state resources to jumpstart the economy as quickly as possible. Although Glazyev in particular has long, and unsuccessfully, advocated a return to command-inspired economics, this plan would constitute a break from Russia's fairly orthodox macroeconomic policies since Putin took office. Accordingly, the government, the Finance Ministry, the Central Bank, and most economists oppose the plan, fearing that the rapid influx of cash into the economy could stoke inflation, create exchange rate volatility, and thus violate Russia's World Trade Organization commitments. The plan finds support in the most conservative elements of the state: those who wish to take the geopolitical confrontation with the West into the economic realm and who see ideological value in autarchy. While this group does not have wide support within the government or among financial elites, they remain present to justify populist measures and ensure that the status quo and liberal options are not the only choices available to Putin.

The three development plans could not be clearer or more distinct from each other. They serve not only their stated role of providing reform plans to Putin in a sensitive period, but they also afford Russian elites and bureaucrats the opportunity to understand the parameters of legitimate debate. Understanding the rules of the game allows the government to function—even if little policy actually changes—by coordinating the expectations of political participants. Political participants such as elites, bureaucrats, and policymakers also recognize that a challenge from outside of the political system exists, which helps tamp down dissension within the ranks.

Endnotes

1 Vadim Dumes, "Minister of Economy Maxim Oreshkin has a plan to boost productivity in Russia," bne IntelliNews, August 30, 2017.

Predictions and Consequences

In the early 2000s, Putin confronted a knotty reform challenge by adopting liberal elements of market competition while protecting powerful stakeholders and assuring the state of its central role in development. The result helped the state reconsolidate power and build capacity, which had been under considerable strain since the beginning of *perestroika*. When energy revenues rebounded dramatically a few years later, Putin found himself in a prime position to redistribute wealth and opportunity to his political supporters *and* increase social spending and improve public infrastructure. The president now likely seeks to repeat that formula. Yet, this time, circumstances appear less propitious, as popular fatigue and the expansion of foreign policy commitments far outstrip the early-2000s environment. Putin is caught between needing to make bold changes to satisfy the population and knowing that too radical a deviation could catalyze unknown and undesirable outcomes.

In the upcoming March 2018 presidential elections, Putin will seek reelection on a platform of patriotism and social stability. In effect, it will be like 2012, when the lack of meaningful competition meant that Putin ran against the 1990s—but with more Crimea. (Quite literally, the Duma passed a law to move the election by a week to coincide with the anniversary of Crimea's accession to the Russian Federation.) Barring a cataclysmic shock, Putin will return to office for another six years, although perhaps failing to reach his election target of "70% turnout with 70% of the vote."

Putin's chief task ahead of that time is to evaluate the plans under advisement and make a decision for the government: pursue one plan or mix elements of several, either simultaneously or in a more politically palatable sequence. The plans, presented in Box 3, individually offer clear paths and winners and losers.

The government's proposal stays the course and does not rock existing stakeholders; the Stolypin Club's plan juices the economy; and the Kudrin plan leverages the need for reform to undertake otherwise unpopular decisions. Historical precedence, external political realities, and the structure of the Russian economy suggest that Putin will not pick a single plan and follow it to its logical conclusion. Instead, he will likely pursue a sequence of reforms that manage acute concerns, burnish the state's central role in the economy, and push any deeply painful decisions into the future when more palatable conditions arise.

Through a process of elimination, it appears likely that Putin will combine elements of the Kudrin plan and the government's plan while substituting

Table 3. Winners and Losers from Reform Plans in Front of President Putin

Policy Principals	General Problem That the Plan Addresses	General Solution and Policies	Winners	Losers/Opponents
Maxim Oreshkin Minister for Economic Development	Low factor productivity and lack of policy stability	Stay the course and allow existing policies, including import-substitution and statistical transparency, to raise growth and allow market participants to plan better	Current elites: government, military-industrial complex, security services, and big business	Small and medium-sized businesses and individual borrowers
Alexei Kudrin, Center for Strategic Research) former Minister of Finance, 2000-2011)	Excessive state intervention into economy and socially inefficient spending	Reduce the size and impact of government: reduce defense spending, redistribute government resources to health and education to raise human capital, increase transporation infrastructure spending, lower inflation and budget deficit targets, reduce the government workforce, and raise the pension age.	Future generations	Current elites, government, military-industrial complex, security services, and big business
Boris Titov (state business ombudsman) and **Sergei Glazyev** (advisor to the president on Eurasian regional integration)	Insufficient demand	Large-scale government stimulus, looser monetary policy, government intervention and subsidization in food/medicine sectors, and reduced taxes and tariffs for exporters	Socially disadvantaged people, exporters, and individual borrowers	Mainstream economic actors: Ministries of Finance and Economic Development, the Central Bank, and most economists

Vladimir Putin with adviser Sergei Glaziev. (Source: Kremlin.ru)

populist measures for the statist interventionist program. As public dissatisfaction with the economy presents the chief internal challenge to Putin, staying the course raises the risk of economic and political protests—which are already on the rise—increasing in size, frequency, and severity. The statist interventionist plan could provide a short-term boom, but once the jolt comes to an end, an increase in inflation could exacerbate the problems faced by individuals with fixed or low incomes. Additionally, high inflation would impinge on the military's ability to conduct external wars. Populist measures akin to the May 2012 decrees, which included raising the wages of public sector employees by a whopping 50%, can address the most acute concerns.

In turn, selecting elements of the Kudrin plan, especially the most painful elements such as raising the pension age, could acknowledge some of the serious issues in the economy. Putin could then name Kudrin, or someone similar, as prime minister or an economic "czar" in the American sense to oversee reforms while utilizing the mandate derived from the election victory.

As Kudrin or other non-systemic liberals would pursue as many structural reforms as possible, the consequences would echo those of liberal reforms of the past. History shows that the pain of adjustment is often funneled toward the reformer, not the president. The latter then allows the reforms to run as long as possible until bureaucratic or popular dissatisfaction becomes unbearable. At that point, the government can replace the reformist prime minister and turn to a cooling-off approach: the previous status quo plan—with money directed at specific problems—or the interventionist plan of the Stolypin Club if dissatisfaction is acute enough.

Ultimately, the Oreshkin, Titov and Glazyev, and Kudrin plans are not mutually exclusive. Putin will cycle through the various plans as required to avoid deep structural reform. While many Russians want an overhaul of the country's political economy, such reform runs counter to Vladimir Putin's needs. His intent is to maintain the status quo. The appearance of reform and movement, without actually doing very much, will keep the status quo—and the president—undisturbed.

Outside observers and many within Russia are looking for Putin to make bold decisions and chart out a clear path towards Russia's future. Yet the lack of decisiveness is the key to Putin's longevity. Putin's system of rule, dubbed the "power vertical", is not the totalitarian system of Stalin's years, but the most familiar and comfortable mode of governance in Russia: an indispensable leader, faceless cadres, informal mechanisms of control, and a populace held in check by patriotism and the fear that things could always get worse.

Endnotes

1 Christopher Jarmas, "The Kremlin and Russia's regional governments are at odds. That's a problem for Putin," *The Washington Post*, February 24, 2017.

FPRI

Foreign Policy Research Institute

www.fpri.org

Foreign Policy Research Institute
1528 Walnut Street, Suite 610,
Philadelphia, PA, 19102