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## VLADIMIR POPOV

One of Russia's most original comparative economists, Vladimir Popov was born in Moscow in 1954, and graduated from Moscow State University in 1976. Initially specializing on the economies of the US and Canada, he turned his attention to the USSR during the perestroika period, and co-authored, with Nikolai Shmelev, a series of texts on the reforms initiated by Gorbachev; these appeared as *The Turning Point* in 1989. *From Plan to Market: The Soviet Economy in Transition* followed in 1991. Strikingly, Popov predicted an imminent, deep recession, estimating that the contraction would be of the order of the American Great Depression. While many free-market apologists, awaiting an instant capitalist miracle, dismissed Popov's warning as overly pessimistic, it in fact proved insufficiently so: instead of shrinking by a third, GDP dropped by over 50 per cent, and the slump lasted for nearly a decade.

Over the course of the 1990s Popov taught and researched in a number of countries—Germany, Finland, Italy, Japan, Sweden, the US and Canada—before directing his gaze eastwards, to co-author, with Manuel Montes, *The Asian Crisis Turns Global* in 1999. Popov's sober analysis, solid empirical data and strongly comparative approach were on display again in his landmark 2000 essay, 'Shock Therapy vs Gradualism: The End of the Debate'. Here, the outcomes of marketization reform in the ex-Soviet Union, Central and Eastern Europe were assessed alongside those undertaken in China and Vietnam. Neither the speed nor extent of liberalization explained the variations in these countries' subsequent fortunes, according to Popov; rather, these derived from existing conditions, levels of development and strength of institutions.

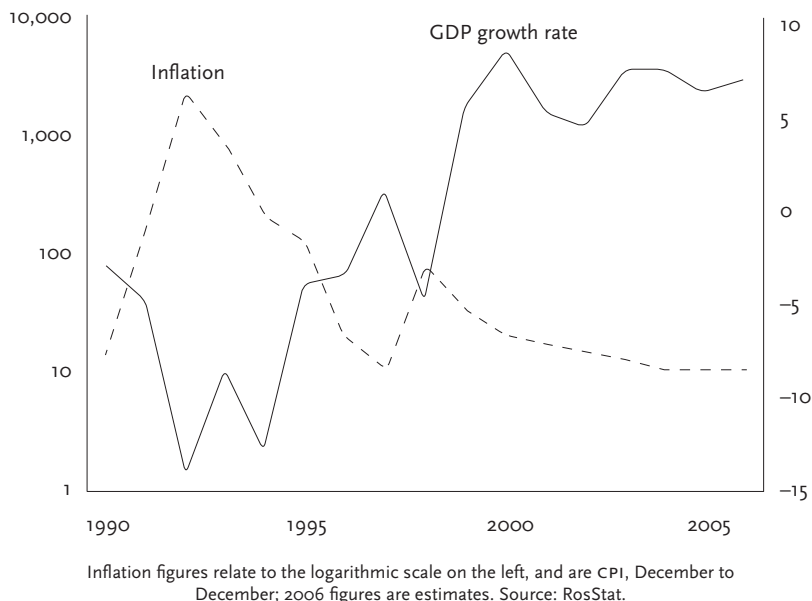
Popov's *Three Drops of Water* (2002) sought to counter a deep-seated sinophobia in Russian culture and policy-making by placing the PRC's record in historical perspective. In a recent paper, Popov has argued that Chinese growth rests on the 'achievements of the Mao period', as well as on an institutional continuity of millennial depth. Noting that China's developmental surge is the first to be based on an indigenous rather than Western economic model, he draws a characteristically thought-provoking conclusion: 'If this interpretation is correct, the next large regions of successful catch-up development would be ME-NA Islamic countries and South Asia, whereas Latin America, Sub-Saharan Africa and Russia would fall behind'.

## RUSSIA REDUX?

**B**Y THE SPRING of 2008, Russia will have a new president and parliament. Though Putin's popularity ratings are extremely high—if elections were held tomorrow, opinion polls suggest he would win in the first round with over 50 per cent of the vote—the constitution bars him from seeking a third term. There has been much discussion in the press of candidates to succeed him—Dmitry Medvedev, First Deputy Prime Minister, is mentioned most frequently—but there can be little doubt that Putin himself will nominate his successor. It is even possible that Putin will remain as leader of the dominant party, head of government, or both. The transfer of power is therefore likely to be smooth, ensuring the continuity of the present regime. However, an examination of Russia's recent social and economic fortunes reveals a number of problems that Putin's successor will inherit, presenting him with a difficult agenda.

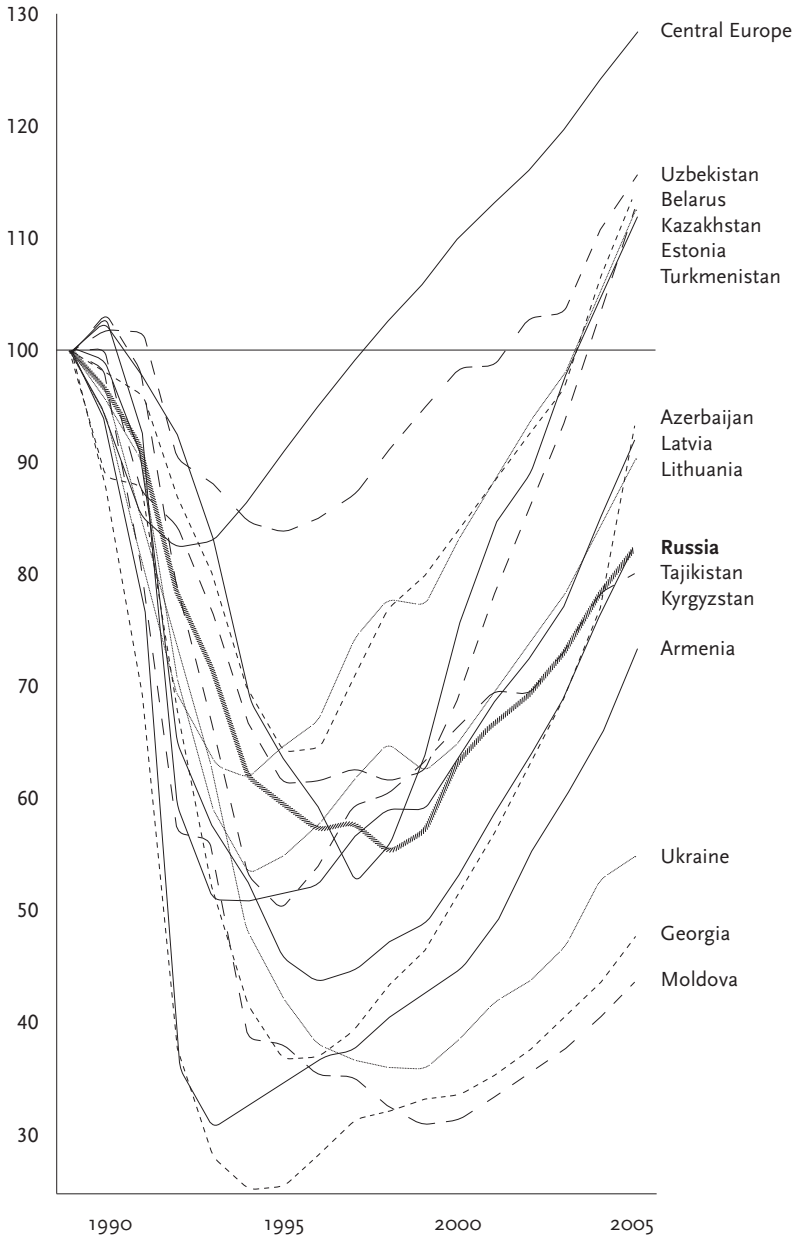
After losing 45 per cent of its output in 1989–98, the Russian economy started to expand as of 1999: GDP grew by 6 per cent that year, 10 per cent in 2000, and 4–7 per cent in 2001–06. The major impetus for this came from the devaluation of the rouble in 1998 and, later, from higher world prices for oil and gas (Figure 1, overleaf); but Putin can at least take credit for not ruining this growth. Inflation fell from 84 per cent in 1998, when prices jumped after the August 1998 currency crisis and rouble devaluation, to 10–12 per cent in 2004–06.

In comparative perspective, however, Russia's performance is not that impressive. Many other former Soviet republics—Azerbaijan, Belarus, Estonia, Kazakhstan, Latvia, Lithuania, Turkmenistan, Uzbekistan and, according to some calculations, Armenia—reached or exceeded their pre-recession (1989) levels of output by 2006, whereas Russian GDP was still only at 85 per cent of the 1989 level (Figure 2, overleaf). Russia's Human

FIGURE 1: *Russian GDP growth rate and inflation, 1990–2005 (percentages)*

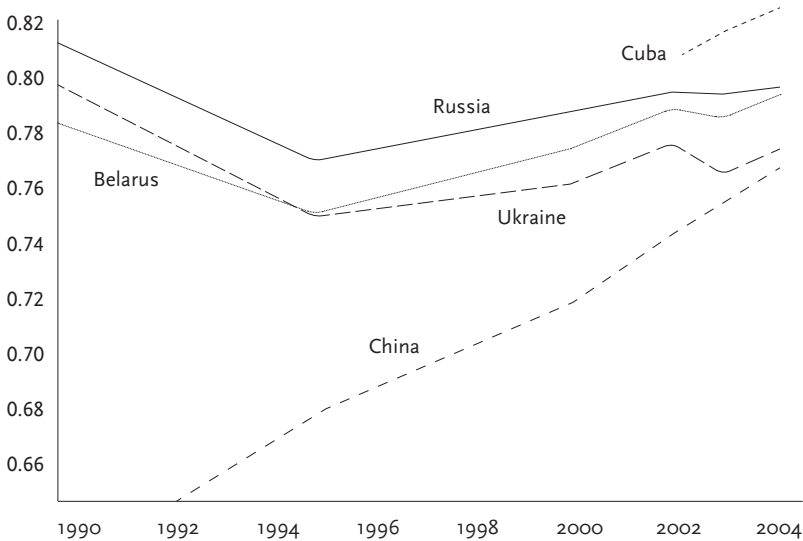
Development Index (taking account not only of GDP per capita, but also life expectancy and levels of education) is still inferior to that of the USSR and even below that of Cuba, where life expectancy is 77 years, against 65 in Russia. China, with a life expectancy of 72, is rapidly approaching Russia's HDI ranking (Figure 3, overleaf).

But at least there is more stability in Russia today than during the rocky 1990s. The government budget balance moved from deficit to surplus, the decline in the share of state revenues and expenditure was halted (Figure 4, overleaf), government debt—domestic and external—decreased (Figure 5, overleaf), and foreign exchange reserves increased to over \$250 billion by the end of 2006 (Figure 6, overleaf). In 2004 the government created a Stabilization Fund to hold the windfall profits from fuel exports; by the summer of 2006 the Fund contained over \$80 billion. Several analysts, however, have pointed out that, given the increase in world fuel prices in recent years, one could have expected an acceleration of economic growth, rather than the slowdown that actually occurred in 2001–06 as compared to 2000.

FIGURE 2: *Change in GDP of former Soviet Union economies*

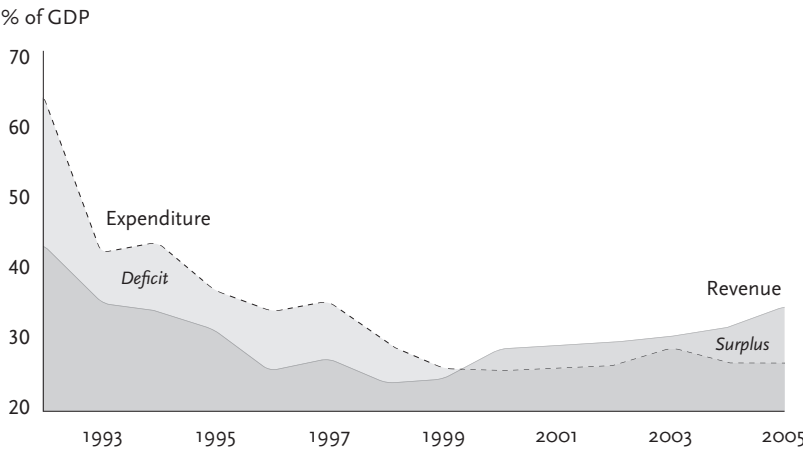
1989 = 100 per cent. Source: EBRD, *Transition Report*, various years.

FIGURE 3: UN Human Development Index, 1990–2002

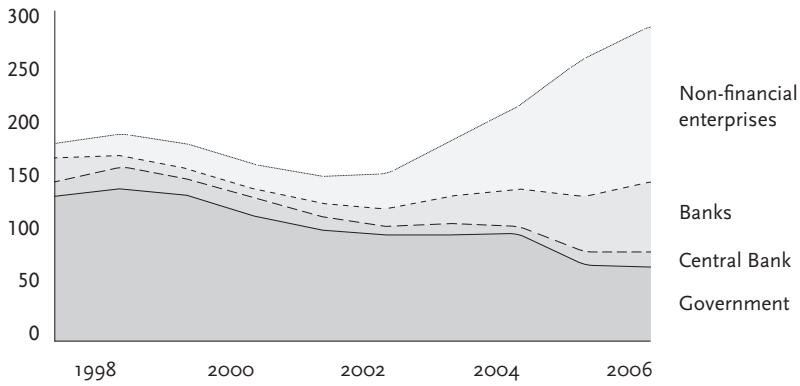


Source: UNDP, Human Development Report 2006.

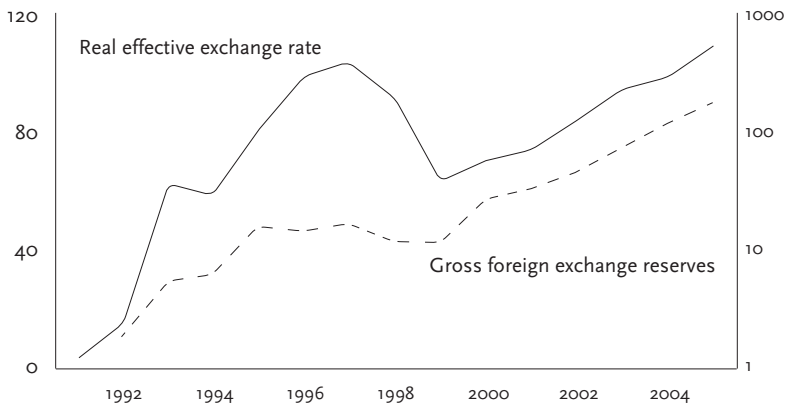
FIGURE 4: Russian government revenues and expenditure



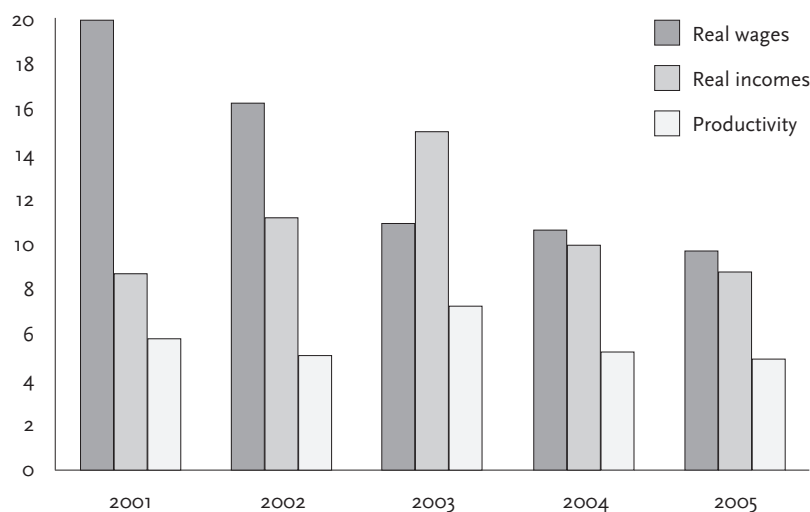
Source: RosStat and Russian Ministry of Finance.

FIGURE 5: *Russia's external debt (in \$ billion)*

Central Bank debt includes government debt to IMF (2006 figures estimates).  
Source: Russian Central Bank.

FIGURE 6: *Real effective exchange rate and gross foreign exchange reserves*

Real effective exchange rate refers to left scale: Dec 1995 = 100; gross foreign exchange reserves refer to logarithmic scale on right; figures in \$ billion, including gold reserves.  
Source: Russian Central Bank.

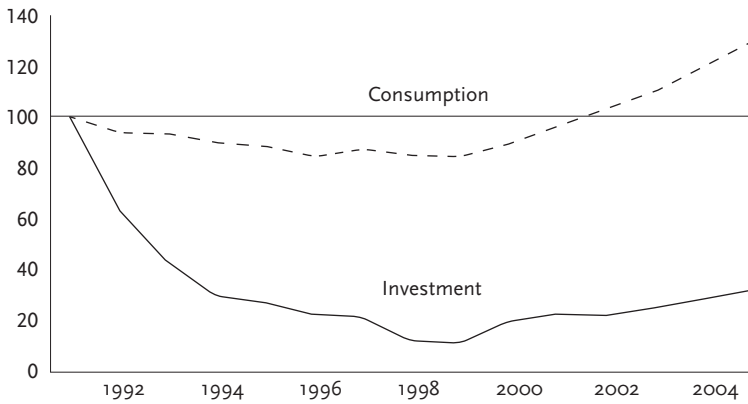
FIGURE 7: *Annual growth rates of wages, incomes and productivity (per cent)*

Source: RosStat.

The reason for the 2001–06 deceleration in growth was the overvaluation of the real exchange rate (Figure 6, previous page)—the typical Dutch disease that Russia has developed once again. It first arose in 1995–98, leading to the currency crisis of August 1998, and it now seems that history is repeating itself. Optimists argue that, unlike in 1998, Russia currently has large foreign exchange reserves (over \$250 billion), but pessimists point out that if oil prices drop and capital starts to flee at a rate of \$5 billion a week, as it did in July–August 1998, these reserves would be depleted very quickly. A future devaluation could take the form of either a currency crisis or a ‘soft landing’, but there is little doubt that it will eventually take place.

Besides, current growth is not based on solid foundations: wages and incomes in recent years have been growing systematically faster than productivity (Figure 7), so that the share of consumption in GDP has increased at the expense of investment. As a result, whereas Russian personal and public consumption has already exceeded the pre-recession level, investment is still below 40 per cent of what it was in the last year of existence of the USSR (Figure 8, opposite). Russian gross savings are large—over



FIGURE 8: *Growth of real investment and total consumption, 1991–2005*

Consumption includes both private and government figures.  
Source: RosStat.

30 per cent of GDP—but they have been funnelled away via the outflow of private capital and the accumulation of foreign exchange reserves; gross investment therefore amounts to less than 20 per cent of GDP.

There is also another important deficiency in the current growth: the government has failed to use windfall revenues from oil and gas exports in 2000–06 to repair badly damaged state institutions and to restore the provision of crucial public goods, such as law and order, education and health care. Instead, the government cut tax rates, allowing profits from natural resources to accumulate as personal and business income, and has amassed a budget surplus. The share of state spending in GDP has barely increased at all, remaining at the extremely low level of 1999—less than half that of the USSR (see Figure 4, above).

### *Social trends*

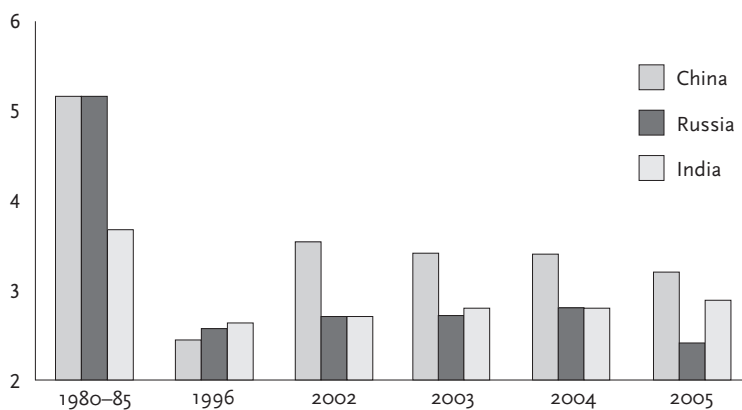
The inevitable economic instability of the coming years will have an important effect on future political and social developments, but perhaps less so than the dynamics of the state's institutional capacities. A strong, efficient state is one that has the power to enforce its rules and regulations, no matter what these are. Crime and murder rates and the

size of the shadow economy are natural measures of the strength of state institutions. Strong states may be more or less democratic: both China and Central European countries, with murder rates of about 2 per 100,000 inhabitants, have a stronger state than Russia, with about 25–30 murders per 100,000.

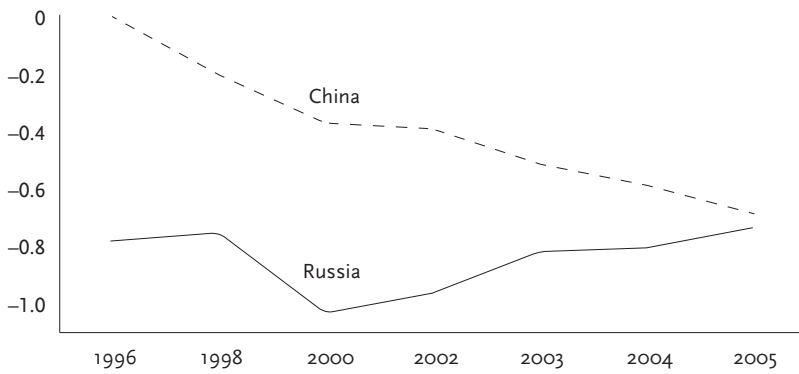
The notion of the state implies that public authorities exercise at least three monopolies: on violence, on tax collection, and on the issuing of money (coinage). All three monopolies were undermined in Russia during the 1990s to such an extent that the very existence of the state was put into question. Government failure became pervasive and much more visible than market failure. In 1998, just before the currency crisis, the payment system was on the brink of collapse: barter deals exceeded 50 per cent of total transactions and enterprises were accumulating non-payments (trade, tax and wage arrears), delaying sums owed to the government, their partners and their workers. After economic growth resumed in October 1998, non-payments and barter transactions quickly disappeared, but there is no guarantee they will not rise again, if the authorities resort to tight monetary policy.

Tax collection, after falling dramatically in 1992–98, increased slightly (see Figure 4, above), but mostly due to the resumption of growth, rather than better tax compliance. Government efficiency has not

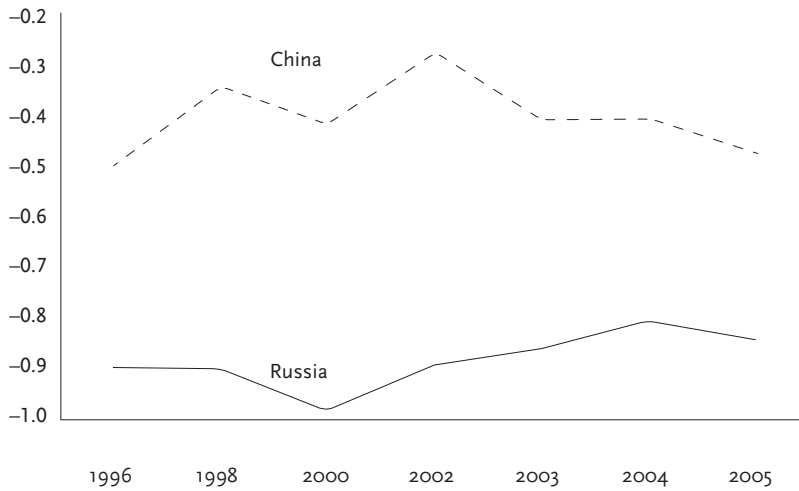
FIGURE 9: *Corruption perception indices, 1980–2005*



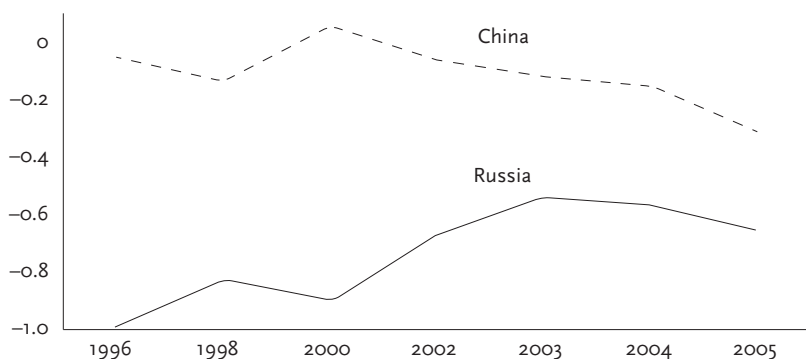
Source: Transparency International.

FIGURE IO: *World Bank control over corruption indices*

Source: World Bank Governance Indicators dataset, 2007.

FIGURE II: *World Bank rule of law indices*

Source: World Bank Governance Indicators dataset, 2007.

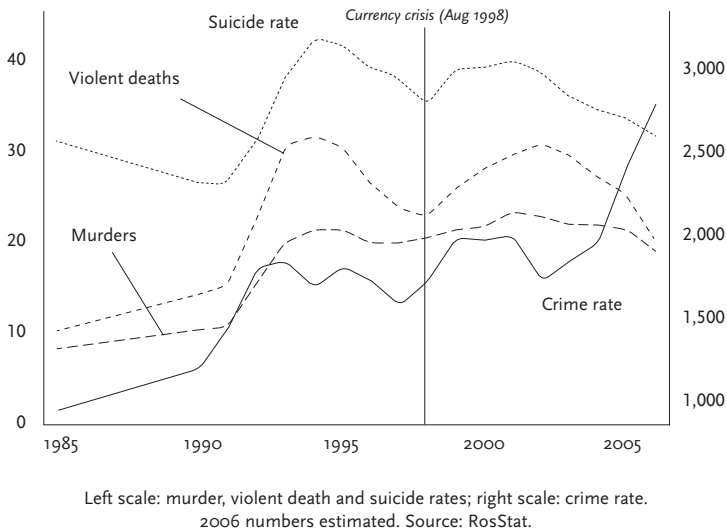
FIGURE 12: *World Bank government effectiveness indices*

Source: World Bank Governance Indicators dataset, 2007.

improved in recent years: different measures of corruption, government effectiveness and rule of law, though inevitably subjective in nature, concur in registering a lack of significant progress (Figures 9–12). Low spending levels, moreover, mean that the state simply cannot provide enough public goods.

But worst of all, the scale and scope of criminality in Russian society remains vast. The crime rate rose gradually in the Soviet Union as of the mid 1960s, but after the collapse of the USSR there was an unprecedented surge—in just a few years crime and murder rates doubled, equalling or surpassing the highest levels in the world (Figure 13, opposite).<sup>1</sup> By the mid 1990s the murder rate stood at over 30 per 100,000 inhabitants, as against 1–2 in Western and Eastern Europe, Canada,

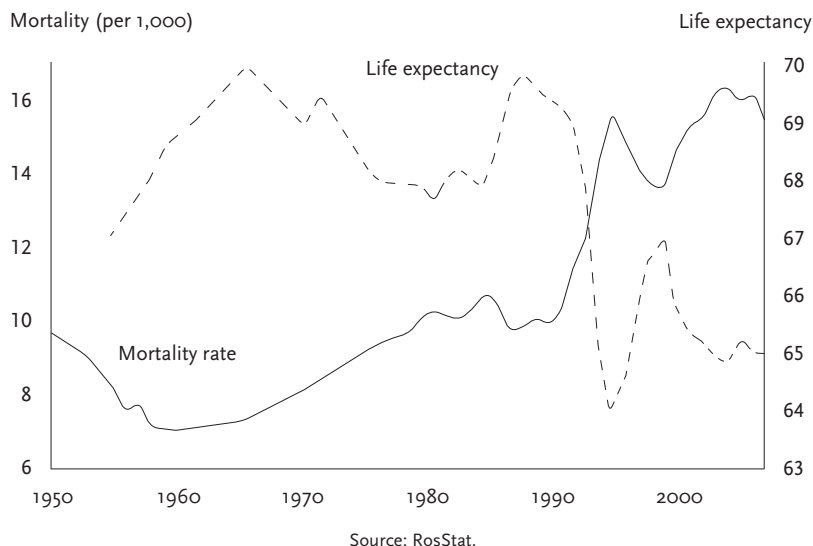
<sup>1</sup> Crime statistics are usually perceived to be incomparable for different countries because of large variations in the percentage of registered crimes. But murders are registered quite accurately by both criminal and death (demographic) statistics. The former are more restrictive than the latter, since they register only illegal murders, whereas demographic figures cover all murders, including ‘legal’ ones—capital punishment and ‘collateral damage’ during wars, anti-terrorist and other police operations. Both rates skyrocketed in Russia at the beginning of the 1990s and remain at extremely high levels. The gap between these two indicators widened during the first and second Chechen wars (1994–96 and 1999–2002); see Figure 13.

FIGURE 13: *Murder, violent death, suicide and crime rates, per 100,000*

China, Japan, Mauritius and Israel. Only two countries (not counting some war-torn collapsed states in developing countries, where there are no reliable statistics anyway) had higher murder rates—South Africa and Colombia—whereas in Brazil and Mexico, the figures are 50 per cent lower than Russia's. Even the US murder rate, the highest in the developed world—6–7 people per 100,000—pales in comparison with that of Russia.

When the murder rate reaches 40–50 people per 100,000, as it did in Colombia in the 1990s, the country faces a complete collapse of state authority and a decline into chaos and warlordism. The unprecedented increase in the crime rate in the 1990s, the shocking—but unpunished—murders of high-profile politicians, businessmen and journalists, left Russia's law enforcement agencies morally bankrupt and brought the state to the brink of losing its monopoly on violence.

The Russian rate of deaths from external causes (accidents, murders and suicides) had by the beginning of the twenty-first century skyrocketed to 245 per 100,000 inhabitants. This is higher than in any of the 187

FIGURE 14: *Mortality rate and average life expectancy, 1950–2006*TABLE 1: *Deaths from external causes per 100,000 inhabitants, 2002*

	Total	Accidents	Suicides	Murders	Other
<i>Russia</i>	245	158	41	33	11
<i>Sierra Leone</i>	215	148	10	50	7
<i>Burundi</i>	213	64	7	18	124
<i>Angola</i>	191	131	8	40	13
<i>Belarus</i>	172	120	38	13	0
<i>Estonia</i>	168	124	29	15	0
<i>Kazakhstan</i>	157	100	37	20	0
<i>Ukraine</i>	151	100	36	15	0
<i>Côte d'Ivoire</i>	148	86	11	27	24
<i>Colombia</i>	134	36	6	72	19
<i>Niger</i>	133	113	6	14	0

'Other' deaths are due to unidentified external causes, wars, police operations or executions. Totals may differ from the sum of columns due to rounding. Source: World Health Organization.

countries covered by WHO estimates in 2002 (see Table 1, opposite). It is equivalent to 2.45 deaths per 1,000 a year, or 159 per 1,000 over 65 years, which is the average life expectancy in Russia today. Put differently, if these rates continue to hold, 1 out of 6 Russians born in 2002 will have an 'unnatural' death. To be sure, in the 1980s murder, suicide and accidental death rates were quite high in Russia, Ukraine, Belarus, Latvia, Estonia, Moldova and Kazakhstan—several times higher than in other former Soviet republics and in East European countries. However, they were roughly comparable to those of other countries with the same level of development. In the 1990s these rates rapidly increased, far outstripping those in the rest of the world.

The most important achievement of recent years is the improvement in social trends brought about by economic growth and political stability: the number of murders reached a peak in 2002 and fell in 2003–06; the suicide rate decreased in 2001–06 (Figure 13, above); the mortality rate stopped growing in 2004 (Figure 14, opposite); after reaching a 50-year low in 1999, the birth rate started to grow, the marriage rate increased and the divorce rate fell. On the other hand, a nearly 60 per cent increase in the crime rate in 2002–06 is most likely a sign of better recording of crimes. True, the improvements are very marginal, and have only appeared in the last two or three years, but at least there is a ray of hope that was previously entirely absent.

### *Rebuilding the state?*

The victory of 'Yedinstvo', the 'party of power', in the parliamentary elections of 1999 was, among other things, a victory for the have-nots (subsidized regions) over the haves (donor regions), which had joined forces in the Primakov–Luzhkov bloc 'Otechestvo–Vsyā Rossiya'. Putin tried to limit the all-powerful regions by changing the principles of fiscal federalism, appointing presidential viceroys in seven amalgamated regions and reforming the Federation Council, the upper chamber of the Russian parliament, which represented the interests of all 89 regions. In 1999, Putin began a second war against Chechnya, refusing to negotiate with the separatists, who are today largely defeated. He launched court cases against the 'oligarchs'—remaining within the limits of the law. A series of tycoons were accused of tax evasion and financial machinations; some emigrated, some were arrested. The only non-governmental television channel, NTV, was shut down

(incidentally, also for totally legitimate reasons: the 'oligarch' Gusinsky had refused to pay his debt to the state-owned Gazprom, having seemingly decided that freedom of speech was not worth that much money). Oil company, Sibneft, was purchased on the open market by Gazprom, raising the state's share in the oil industry from less than 15 per cent in 2004 to over 30 per cent a year later.



But the improvement in social indicators has been the most important achievement of all. Economic growth and low inflation alone cannot prevent the disintegration of the country if social inequality and crime increase. Building the vertical of power and intensifying centralization may not prevent the collapse of the state, if they do not establish law and order more firmly and limit the extent of the shadow economy. In fact, Putin has been criticized precisely for taking ever more power into his own hands without greater order resulting. But it now seems that the first signs have appeared of a real, rather than an ephemeral, stabilization.

Putin's popularity can be explained primarily by his ability to stop the collapse of the state caused by the reforms of the 1990s. All other problems are dwarfed by the threat of social and national disintegration. The majority of Russian citizens are prepared to forgive Putin for his heavy-handed tactics in dealing with the 'oligarchs' and even with entrepreneurs of a lesser stature, for the 'purges' in Chechnya, and for the constraints placed on democracy and freedom of speech—all in the interests of strengthening law and order and curbing the boundless anarchy of the 1990s.

Polls conducted on the eve of the February 2004 elections asked Russians what they expected first and foremost of the new president. Fifty-eight per cent wanted him to restore Russia to its status as a great and respected power; 48 per cent to ensure a just distribution of income in the interests of ordinary people; 45 per cent to strengthen law and order; 43 per cent to put an end to the war in Chechnya; 41 per cent to return the money that ordinary people lost during the reforms; 39 per cent to strengthen the role of the state in the economy. Such priorities as 'keeping Russia on the road of reform' and 'continuing



the policy of closer ties with Western countries' garnered only 11 and 7 per cent respectively. 'Are you concerned that Putin could establish an iron-fisted dictatorship supported by the "power agencies"?' In January 2000, before Putin's first electoral victory, 34 per cent said yes to this question, while in January 2004, only 26 per cent held this view. Respectively, 57 and 67 per cent showed no concern.

### *Prospects*

Where is Russia headed? The future harbours many dangers. The current real exchange rate of the rouble (the ratio of domestic to world prices) is too high. It has been growing throughout the past five years and in 2006 exceeded the 1998 pre-crisis level. Therefore, a drop in world energy prices could easily provoke a new currency crisis and interrupt economic recovery, despite large currency reserves. Domestic fuel and energy prices remain many times lower than world levels, creating incentives for inefficient energy consumption; Russia has one of the highest ratios of energy use to GDP in the world. Unlike in Eastern European countries and many of the former Soviet republics, where the prices of fuel and energy have already reached or are approaching world levels, the restructuring of the Russian economy is still far from complete. What Russia should have done in recent years was to slowly devalue the rouble, and at the same time increase domestic prices for oil, gas and electricity, compensating producers for losses from the rising cost of energy with the stronger competitiveness that would result from the depreciating rouble. However, such a policy is not even on the drawing board at present.

A second danger is too rapid a decrease in taxes, which the government has already implemented (income tax, corporate tax and the unified social tax). Critics of such measures, including the IMF's Moscow office, justifiably point out that the current budget surpluses are based primarily on high prices for energy resources, and therefore, if these prices should fall, the government could once again find itself penniless. Moreover it is not the right time to reduce taxes when virtually all government services—health care, education, defence, law and order—are much worse off than the private-sector economy.

Other dangers remain: corruption, the inefficiency of the state apparatus, high levels of social inequity. But generally Russia is in better shape

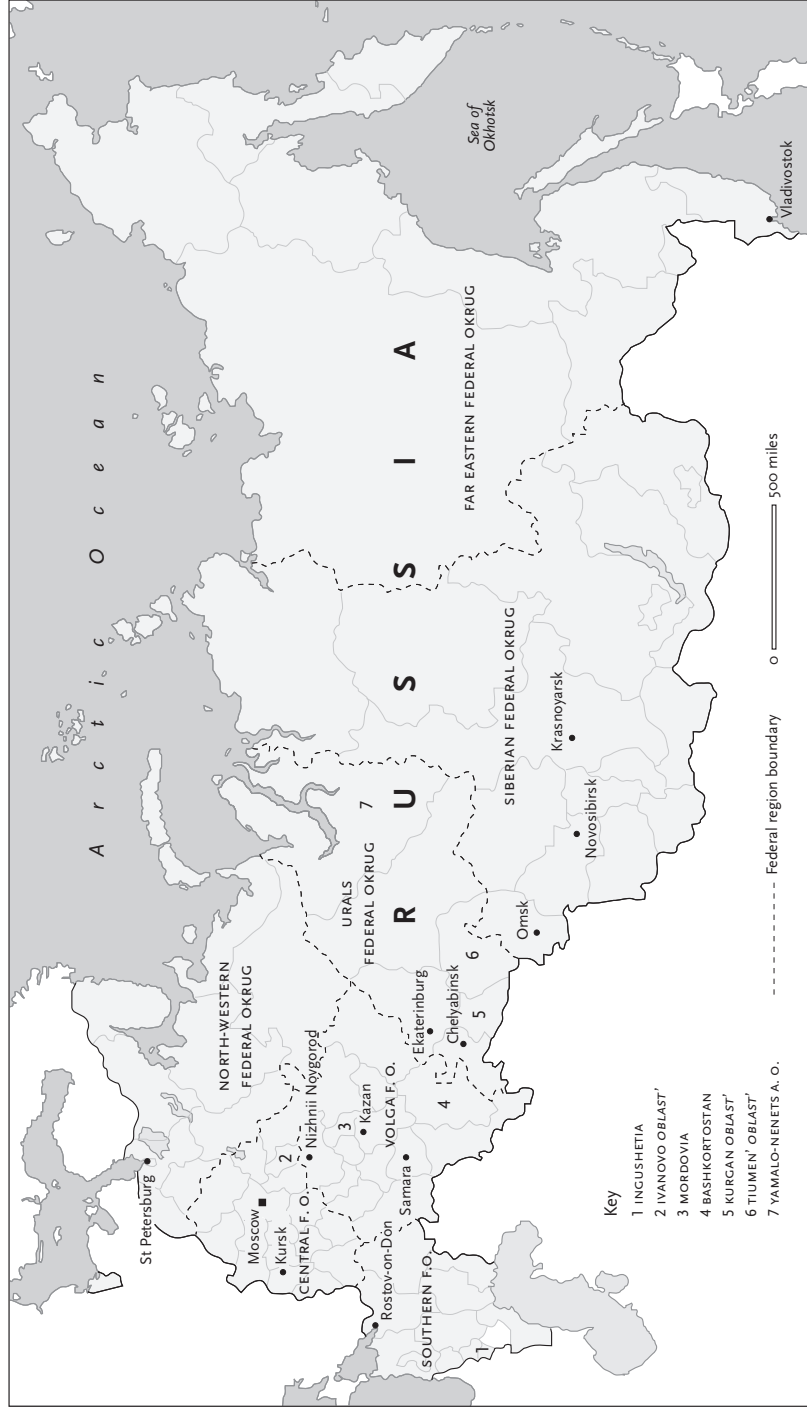
today than seven years ago, when Putin assumed power. Russia now needs more than anything to strengthen law and order and to restore the institutional capacity of the state. Democracy is also needed, but only later, when the rule of law has been established. There is, of course, a danger that the leadership will use political centralization to line everyone up along the 'vertical of power' and eliminate opposition in order to live in serene comfort at the citizens' expense—and perhaps also to embark on the occasional escapade. This has happened in Russia before. But one must choose the lesser of two evils. Strengthening law and order is only possible under a centralized system. Without centralization, there is no chance at all of it happening; unbounded chaos and lawlessness would rule. This seems to be the choice facing Russia today.

## CONTOURS OF THE PUTIN ERA

### *A response to Vladimir Popov*

**I**N 'RUSSIA REDUX?', Vladimir Popov has provided a lucid reckoning of the terrible economic, political and human costs of the shock-therapy era. If Russia is in slightly better shape now than seven years ago, it is still significantly worse off than it was twenty years ago. As one striking graph after another demonstrates, GDP, investment and life expectancy have yet to return to their 1989 levels. What Popov terms 'the recession' has few comparisons in world economic history. Nevertheless, it is heartening that he can present data which point to significant improvements in several areas. After the ceaseless turbulence and moral bankruptcy of the Yeltsin years, the two administrations of Vladimir Putin have been widely characterized as inaugurating a new era of stability in Russia: state power has been reasserted and, thanks to high oil prices, GDP has grown markedly, government finances are in the black, and much of the country's external debt has been paid down. There has also been good news in the social sphere: the birth rate has risen, while the suicide and mortality rates have declined.

However, as Popov warns, there are many dangers ahead. The rouble is overvalued, and the economy is overly dependent on the current commodities bonanza. Moreover, the government has not used the windfall from natural resources to fund spending on public goods, and has even opted to further shrink the tax base. Nonetheless, Popov concludes that 'Russia is in better shape today than seven years ago', and asserts that the priority is to 'restore the institutional capacity of the state'. The erosion of democratic prerogatives that has accompanied Putin's recentralization drive is the price that must be paid for continuing stability; the alternative is chaos.



Popov's empirical approach is a much-needed corrective to the liberal-capitalist mirages of 'transitology', and to the Kremlin shadow-puppetry of the mainstream Russian media. Above all, it provides a solid basis on which to advance discussion. What follows is an attempt to probe further into the trends Popov has outlined. This is in part a matter of more detailed quantification—differentiating the elements of the overall picture, in order to see more clearly the imbalances between them. But a closer examination of Russia today also has far-reaching qualitative implications, which in turn will determine how—or indeed if—the hazards Popov has identified are addressed.

### *Disequilibria*

The rate at which Russian GDP has grown since the rouble collapse of August 1998 is significant, reaching a high of 10 per cent in 2000, and averaging between 4 and 7 per cent over 2001–06. The rising economic tide has lifted the incomes of many: the national average reached 10,287 roubles (\$350) per month in November 2006, compared to 2,281 roubles (around \$80) in 2000, while the poverty rate declined from 29 per cent in 2000 to 17.6 per cent in 2004. The country's Gini coefficient, the standard aggregate measure of income distribution, rose from 0.3 in 1992 to almost 0.5 in 1998, but by 2000 had dropped to 0.4, indicating that at least some of the staggering inequalities of the 1990s had been smoothed out. However, the Gini figure has since then begun to creep upwards: from 0.397 in 2000 to 0.409 in 2004.<sup>1</sup>

Two further qualifications should be made to this picture, relating to the social and geographical distribution of Russia's new prosperity. Wealth remains highly concentrated: in 2002, the top 20 per cent of the population by income accounted for 46.6 per cent of total income, the bottom quintile for only 6.1 per cent. The latter were faring worse in relative terms by 2004, when they commanded 5.6 per cent of total income.<sup>2</sup> Contemporary Russian society is to a large extent stratified by chronology: among those buffeted by the hurricane winds of shock

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<sup>1</sup> Federal'naia sluzhba gosudarstvennoi statistiki (RosStat, [www.gks.ru](http://www.gks.ru)) and UN Human Development Reports, 2002 and 2006. The official poverty line in 2004 was 2,376 roubles per month (then around \$85).

<sup>2</sup> UN Human Development Report 2006; Economist Intelligence Unit, *Russia Country Profile 2006* (henceforth EIU), p. 45. The latter drily notes: 'since it is generally assumed that in Russia income and the ability to evade taxes are positively correlated, actual income distribution is probably more unequal still.'

therapy in the 1990s, the elderly and the retired were prominent, as already meagre pensions went largely unpaid during the Yeltsin years. Here again the country's improving fortunes have helped, and the sums paid have even increased. However, they remain low—2,395 roubles a month (\$85) in 2005—and the monetization of a string of benefits in 2004 has stretched pensioners' resources still further. Their standard of living has been eroded by having to pay for transport and utilities they previously received for free, and by inflation—formerly in double figures, now at 9.7 per cent, and still likely to outpace any increase in the standard pension.

Geography is a crucial variable in assessing Russia's present condition. Both population and resources have always been distributed extremely unevenly across the country's vast territory. Industry is concentrated in European Russia, the Urals and the Arctic Circle; as a result, the per capita gross regional product of the Central Federal District, for instance, is two and a half times higher than that of the Southern steppe and North Caucasus. The capital's gravitational pull on the country's economy is extraordinary: Moscow alone accounts for 20 per cent of GDP. If we factor in the wider Moscow region, St Petersburg and Tiumen', only 'four regions produce nearly half of Russia's output'.<sup>3</sup> The present reliance on exports of oil, gas and metals has exacerbated existing imbalances by dramatically raising the wealth of resource-rich regions: annual per capita gross regional product in Tiumen' *oblast'*, for instance, stood at 575,411 roubles in 2004 (\$19,800), compared to 12,583 roubles (\$430) in Ingushetia, the Russian Federation's poorest sub-unit.<sup>4</sup> Needless to say, this torrent of cash has largely flowed into the coffers of extractor companies as profits, rather than to employees as wages.

Regional aggregate figures conceal further disparities. There are significant differences not only between regions, but within them. In the Central Federal Region, for instance, annual GRP per capita stood at \$4,350 in 2004, and the average yearly income at the end of 2006 was \$6,120. But the gap between the region's maxima and minima is vast: where the average annual income in Moscow is \$13,440, in Ivanovo

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<sup>3</sup> EIU, p. 45. It should be noted, however, that many Russian companies have their headquarters in Moscow, which inflates the city's figure substantially; nevertheless, this statistical bulge itself illustrates the capital's dominant role in the national economy.

<sup>4</sup> Figures from RosStat website.

*oblast'* it is a mere \$1,860—a ratio of over 7 : 1. Lower, but nonetheless significant, ratios obtained elsewhere: in the Urals, the average income of the Yamalo-Nenets Autonomous *okrug* is nearly five times higher than that of Kurgan *oblast'*; inhabitants of Samara *oblast'* on the Volga earn two-and-a-half times as much, on average, as those of Mordovia.<sup>5</sup> Given the aforementioned concentration of industry, and corresponding focus of investment and employment opportunities, the distance between well-fed regions and lean zones seems set to widen in the years ahead. In such a context, the gradual increase in domestic fuel prices that Popov recommends in his conclusion would have vastly disparate impacts in different parts of the country and on diverse social sectors—reinforcing the dynamic of growing territorial and social inequality.

### *Stabilization and deceleration*

High global oil prices, coupled with the dominant role of natural resource extraction in the Russian economy, have resulted in a Slavic version of the 'Dutch disease'. Popov points to the consequent overvaluation of the real exchange rate as the principal reason for the effective slowdown in the rate of GDP growth since 2000. But a sequence of other, interconnected factors could be adduced, with significant longer-term implications.

Firstly, there is the matter of investment, both in terms of scale—relatively low, at less than 20 per cent of GDP—and character. The smashing of the planned economy in the 1990s led to large-scale de-industrialization in Russia, and what profits did accrue from surviving enterprises were largely funnelled out of the country into offshore accounts. The rouble collapse of 1998, in rendering exports more competitive, encouraged capitalists to repatriate some of this wealth. But as Simon Clarke notes, though investment has increased since the 1990s,

most of this . . . [has been] in piecemeal re-equipment and reconstruction of existing facilities to maintain or expand existing production capacity in a favourable market environment, rather than in the construction of new plants which will be able to produce to world cost and quality standards and actively expand the market.<sup>6</sup>

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<sup>5</sup> Figures from RosStat website.

<sup>6</sup> Simon Clarke, 'A Very Soviet Form of Capitalism? The Management of Holding Companies in Russia', *Post-Communist Economies*, vol. 16, no. 4 (2004), p. 420.

The direction of investment towards existing capacity, rather than towards diversifying the economy, may partly explain why the volume of imports increased by nearly 20 per cent in 2003–05: even in auspicious macroeconomic circumstances, domestic goods have been unable to compete with foreign-produced ones in many sectors.<sup>7</sup> This seeming unwillingness to devote funds to broadening the base of the Russian economy—and so the basis for future profits—suggests that the Russian business elite remains largely extractive in nature. Unless and until this orientation changes, GDP growth will continue to depend above all on the vagaries of global oil prices.

The reluctance to invest is not confined to the private sector. In 2004, the Russian government set up a Stabilization Fund in which the dizzying quantities of petroroubles would accumulate. Any revenues from sales of oil over a price of \$27 per barrel for Urals crude are now paid into the fund, the balance of which peaked in June 2006 at just under \$80bn.<sup>8</sup> Yet as Popov observes, the Putin administration has ‘failed to use windfall revenues from oil and gas exports . . . to repair badly damaged state institutions and to restore the provision of crucial public goods’.<sup>9</sup> Some of the ‘Stabfond’ booty has been used to pay down external debt and cover pension arrears; but since the summer of 2006, it has been almost exclusively spent on foreign currency—45 per cent on dollars, 45 per cent on euros, 10 per cent on sterling. Between July 2006 and the end of January 2007, cumulative spending on foreign currency from the Stabfond reached 2.4 trillion roubles, or \$91bn—on top of the \$250bn in foreign reserves the state already possessed by June 2006.<sup>10</sup>

In a country where ‘as many as one hospital in five still lacks hot water and sewerage facilities’, where ‘state funding pays for less than one-third of the operating costs of state universities’, a government awash with cash has nonetheless opted not to spend much of it on public goods.<sup>11</sup> Instead, it has poured its resources into global capital markets, to ‘finance oil importers’ bigger current-account deficits—in effect, lending the increase in fuel bills back to consumers’, and propping up their

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<sup>7</sup> EIU, p. 43.

<sup>8</sup> Elena Lebedinskaia, ‘Stabfond: segodnia, zavtra . . . navsegda?’, *Neprikosnovennyi zapas*, no. 50 (2006); figures from Ministerstvo Finansov, [www.minfin.ru](http://www.minfin.ru).

<sup>9</sup> Popov, ‘Russia Redux?’, NLR 44, March–April 2007, p. 43.

<sup>10</sup> *Financial Times*, 9 June 2006; figures from Ministerstvo Finansov and EIU, *Russia Country Report*, September 2006, p. 39.

<sup>11</sup> EIU, p. 24.



economies rather than redressing the imbalances of its own.<sup>12</sup> This, it should be stressed, is in addition to running a budget surplus of 7.7 per cent of GDP in 2005, and implementing a series of regressive changes to the tax regime since 2001—including a flat income-tax rate of 13 per cent and a cut in corporate tax from 35 to 24 per cent—that have systematically favoured corporate wealth at the expense of ordinary citizens.<sup>13</sup>

### *Who rules Russia?*

The Putin government's choice of spending priorities—bolstering the euro and the tumbling dollar rather than providing for the needs of its own people—and the reluctance of Russia's entrepreneurs to invest in expanding domestic markets, raise fundamental questions as to the overall strategy of Russia's current business and political elite. Before addressing these, however, we need first to tackle a more basic matter: who are Russia's new rulers?

Much has been written about the rise of representatives of the 'power structures' under Putin, one-time KGB Lieutenant Colonel and, prior to his elevation to the premiership and presidency, director of the FSB, successor agency to the KGB. Drawn from the ranks of the military and security services, *siloviki* are indeed prominent in the current Russian leadership: according to Olga Kryshtanovskaya and Stephen White, *siloviki* composed 58.3 per cent of the Security Council in 2003, compared to 33.3 per cent in 1993, and a mere 4.8 per cent in the Politburo of 1988. They have also increased as a proportion of the regional elite: of 88 heads of federal sub-units, 2.2 per cent were drawn from military or security circles in 1993, rising to 4.5 per cent in 1999, and then surging to 10.2 per cent in 2003.<sup>14</sup> Of most concern to those fearing an authoritarian restoration is the fact that many of these appointees remain within the 'active reserve' of their original ministry—from which they are effectively seconded, and for which they are supposed to prepare a monthly report on their activities.

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<sup>12</sup> *Economist*, 10 November 2005.

<sup>13</sup> EIU, pp. 66, 39.

<sup>14</sup> Olga Kryshtanovskaya and Stephen White, 'Putin's Militocracy', *Post-Soviet Affairs*, vol. 19, no. 4 (2003), pp. 289–306. I have cited the figures for the most tightly defined groups, rather than the much higher aggregate figure calculated by Kryshtanovskaya and White; for important methodological qualifications to their data, see Sharon Werning Rivera and David Rivera, 'The Russian Elite under Putin: Militocratic or Bourgeois?', *Post-Soviet Affairs*, vol. 22, no. 2 (2006), pp. 125–44.

The melding of security services and political power is a salient characteristic of Putin's Russia; a point to which I will return. Perhaps even more striking, however, has been the swelling presence of business in the state. The rouble collapse of 1998 profoundly altered the character and composition of the Russian business elite, virtually sweeping away Moscow-based banking and finance, while the sudden boost to domestic production resulting from default and devaluation led to a rise in the weight of the real sector—and a corresponding new prominence of industrial regions. Where the 1990s scene was dominated by a handful of 'oligarchs', at the turn of the century political influence and economic throw-weight was distributed across a larger, more geographically dispersed pool of individuals, with closer affiliations to the state apparatus than their tycoon predecessors. Indeed, an examination of the trajectories of the new business elite reveals that in 2001, 29 per cent had a *nomenklatura* background, up from 24 per cent in 1993; Kryshatanovskaya and White further observe that 'the main source of recruitment of the business elite is government ministries'.<sup>15</sup>

Conversely, business has been a significant source of state cadres. This applies at all levels: a whole section of Putin's Presidential Administration was drawn from the ranks of Al'fa Bank, while as Table 1 (opposite) shows, by 2003 some 20 per cent of the government was drawn from business, which provided almost the same proportion of Duma deputies. The representation of business in the upper house of the Russian Federal Assembly was still higher: in 2002, almost a third of Federation Council members came from private enterprises.<sup>16</sup> More than a dozen Russian regions, resource-rich ones prominent among them, are now headed by businessmen from major local companies.

The upshot of the 1998 rouble collapse, then, was a 'renegotiation, but not a dissolution, of the interpenetration of business and government that defines an oligarchy.'<sup>17</sup> Indeed, with Putin's successive appointments, since 2001, of key government figures and allies as chairmen of state companies, the relations between business and officialdom have become still closer. The two are now, in the words of the *Financial Times*,

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<sup>15</sup> Kryshatanovskaya and White, 'The rise of the Russian business elite', *Communist and Post-Communist Studies*, 38 (2005), p. 300.

<sup>16</sup> Andrew Barnes, 'Russia's New Business Groups and State Power', *Post-Soviet Affairs*, vol. 19, no. 2 (2003), p. 180.

<sup>17</sup> Kryshatanovskaya and White, 'Rise of the Russian business elite', p. 295.

TABLE 1: *Business representation in elite groups (percentages)*

	<i>Top leadership</i>	<i>Duma deputies</i>	<i>Government</i>	<i>Regional elite</i>	<i>Overall</i>
Yeltsin cohort (1993)	2.3	12.8	0	2.6	4.4
Putin cohort (2002)	15.7	17.3	4.2	8.1	9.3
Putin cohort (2003)	9.1	17.3	20	12.5	14.7

Source: Kryshnanovskaya and White, 'Rise of the Russian business elite', Table 4, p. 303.

'extraordinarily intertwined': Deputy Prime Minister Dmitri Medvedev is also chairman of Gazprom; Putin's deputy chief of staff, Igor Sechin, is also chairman of Rosneft. Taking the Presidential Administration as a whole, '11 members chaired 6 state companies and had 12 further state directorships; 15 senior government officials held 6 chairmanships and 24 other board seats.' Many members of the government are also rumoured to have significant, undisclosed business interests—such as the Communications Minister, Leonid Reiman, who allegedly still holds a stake in the phone company he co-founded, Telekominvest.<sup>18</sup>

The *Financial Times* has described Putin's immediate entourage as the 'quasi-board of what might be called Russia, Inc.' The broad extent to which state and business have merged, and the amphibious character of functionaries and executives, initially suggest that this would be an apt term for the country as a whole. The question arises, however, as to which of the Russian elite's two faces—business and state—predominates; which fractions set longer-term goals and priorities?

### *Elite orientations*

The reassertion of state control over strategic companies and sectors has been seen as a sign of stealth nationalization—the state using its

<sup>18</sup> *Financial Times*, 19 June 2006; and William Tompson, 'Putin and the "Oligarchs": A Two-Sided Commitment Problem', in Alex Pravda, ed., *Leading Russia: Putin in Perspective*, Oxford 2005, p. 193.

administrative powers to crush YUKOS and, more recently, even muscle aside multinational companies such as Shell. Western establishment analysts have diagnosed these developments as a case of 'resource nationalism', likening Putin's actions to those of Chávez or Morales, while the latest leitmotif of Russian political dis-course has been the idea of 'sovereign democracy'—essentially referring to Russia's ability and determination to pursue an independent course, no longer reliant on loans or approbation from the West.

Neither of these concepts is an adequate measure of the orientation and outlook of Russia's contemporary elite. As noted above, the Putin administration has not actively redistributed oil wealth to those dispossessed by the 'reforms' of the 1990s; indeed, its tax regime seeks precisely to benefit the wealthy still further, while the monetization of benefits and increased charges for utilities penalize the poor. Though the poverty rate is declining and wages rising, any significant drop in oil prices will likely reverse these trends, which will once again have the most severe impact on the lowest income strata. The decision to spend the oil windfall on euros and dollars, meanwhile, is ostensibly motivated by a desire to keep inflation in check; but in a context of continued infrastructural dysfunction, such prudence is a form of deferred suicide, starving the nation of the public goods that would secure its survival in the longer term.

Popov criticizes the decision not to spend oil revenues on public goods and infrastructure, but does not pose the question of why it was made. It is clear, however, that for all the nationalist rhetoric emanating from the Kremlin, it is not the livelihoods and prospects of its own citizens with which Russia's rulers are concerned. Rather, it is the continued flow of oil out and money in which they seek to secure, distributing largesse to the silent *narod* when electoral needs dictate, but otherwise focused on the twin prizes of profits and power.

The relationship between these is perhaps the structuring feature of Russia today: administrative power provides crucial tools for business success, while commercial considerations often dictate the allocation of state assets and offices. The convergence of state and business is in that sense far more than a coalition of the self-interested: it is a symbiosis rooted in the neo-patrimonial form assumed by capitalism in Russia. For the state has been the key structure through which the country's

capitalists have pursued their economic interests—using its officials to secure the outcome of privatizations; to facilitate hostile (often armed) takeovers, asset-stripping and money laundering; to defer or conceal tax debts; even to act as paid protection against organized crime. At a meeting with the country's most prominent tycoons in July 2000, Putin revealingly pointed to 'the fact that you have yourselves to a significant extent formed this state, through political and quasi-political structures under your control'—adding that 'perhaps what one should do least of all is blame the mirror.'<sup>19</sup>

In the twenty-first century, the state has become the indispensable guarantor of property acquired in the 1990s. Many have seen in Putin's selective persecution of the 'oligarchs' since 2000 a forceful reassertion of state prerogatives and authority over business. However, this is to overlook the extent to which a strengthening of state power serves precisely the interests of Russia's business elite. OECD economist William Tompson observes that 'for Russia's new rich, state-building and structural reform were intended to consolidate the victories they had won in the 1990s.'<sup>20</sup> In a context where state and business overlap so extensively, an expansion of state power has often simply meant an exponential increase in the coercive strategies available to business groups.<sup>21</sup> While the centralizing rhetoric of the national leadership has gained in stridency, business elites have shifted their attention to securing the services of the state apparatus at regional and local levels, where 'state resources . . . are rented to powerful and expanding business groups'.<sup>22</sup> The phenomenon of state 'capture' that characterized the 1990s has, then, been modified in form rather than substantively reduced.

The resulting formation could be described as one in which the state has little or no autonomy from the economic interests of Russia's elite. The fractions of this state-business alloy consist of both state actors and business groups, who combine according to common economic

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<sup>19</sup> Tompson, 'Putin and the "Oligarchs"', p. 182.

<sup>20</sup> Tompson, 'Putin and the "Oligarchs"', p. 188.

<sup>21</sup> Vadim Volkov has concluded that in the period since 2000, 'the major instruments of aggressive enterprise takeovers are corrupt state organizations that have judicial and coercive power.' Volkov, 'The Selective Use of State Capacity in Russia's Economy: Property Disputes and Enterprise Takeovers After 2000', *PONARS Policy Memo* no. 273, October 2002.

<sup>22</sup> Volkov, 'Selective Use of State Capacity'.

interests. Divisions on forward policy—such as the further liberalization and lowering of tariff barriers required for WTO entry—take place along sectoral lines, with many export-oriented manufacturers and still-fragile banks aligned with proponents of ‘sovereignty’, against liberal supporters of increased integration into the global economy. The influence of the two main tendencies fluctuates, with Putin hovering above the fray—and deliberately working to maintain the fragmentation of domains and interests that has thus far blocked the emergence of a unified capitalist class.

Putin enjoys considerable support among the general populace, but this has a shallow, plebiscitary character, and should not be mistaken for a broad social consensus on which the elite as a whole could depend. Indeed, Russia’s rulers have been unable to forge an ideology with any consistent appeal; the recent cultivation of nationalist sentiments has mostly taken the form of post-imperial spasms, rather than a coherent vision that would enable them to exert moral leadership. They instead hold sway over the atomized populace through a combination of electoral approval for Putin himself and various unformalized mechanisms of coercion. These play a more prominent role than Popov’s analysis—where crime, corruption and the informal sector appear as mere by-products of an unstable conjuncture—would suggest. Indeed, they are integral to the functioning of Putin’s Russia, and as such are critical to any understanding of its future course.

### *Symptoms of informality*

The principal administrative change wrought by Putin has been a formidable re-centralization; the ‘vertical of power’, in the President’s own phrase, has been firmly planted in the country’s soil. This has meant, on the one hand, increased efficiency in the basic functioning of the state—above all in the collection of taxes—and the assumption, to a higher degree than in the Soviet period, of civilian posts by military and security service personnel. On the other hand, increased centralization has had at least two other, less widely remarked consequences. Firstly, the federal centre has not done away with regional structures, but rather has simply created a new layer of state employees who usurp the functions of their counterparts, without displacing them altogether. Hence, in part, the phenomenal bureaucratization of the Russian state: there are now 1.3 million functionaries, more than twice as many as the USSR had

prior to its dissolution.<sup>23</sup> Secondly, it is not only authority that has been centralized: the shadow world of corruption has been similarly reorganized. According to research by the Russian think-tank INDEM, although the quantity of bribes decreased by 20 per cent over 2001–05, the average size of a bribe actually increased thirteen-fold.<sup>24</sup> The same study estimated the volume of business corruption at \$316bn, while the Russian deputy general procurator put it at \$214bn. Either way, as Leonid Kosals observes, ‘both figures exceed the scale of revenues of the Russian federal budget’—adding that the growth of corruption ‘is roughly tenfold, which is many times greater than the growth of the economy as a whole.’<sup>25</sup>

The scale of corruption in Russia stems above all from the continued prevalence of informal practices in all spheres of society—in turn a product of what Georgi Derluguian has called the ‘persistent under-institutionalization of Russian life’.<sup>26</sup> In political terms, the lack of institutions gives rise to widespread personalism, which at the very least sustains a ferment of cliques and factions—witness the number of St Petersburgers in Putin’s retinue. It also frequently clears the way for brazen nepotism. To cite only two of countless examples: between 1996 and 2000 the Kursk *oblast*’s oil concern, pharmacies, public security and cultural affairs were placed into the hands of his relatives by the then-governor Aleksandr Rutskoi; while much of Bashkortostan’s economic life today lies in the purview of president Murtaza Rakhimov’s family.

There are, of course, plenty of similarly egregious cases elsewhere in the world. But the personalism that facilitates such corruption is part of a whole complex of informal practices on which the post-Soviet order relies. As Alena Ledeneva has argued, ‘the informal component is an integral part of political power in Russia, which makes it both efficient and dependent on the unwritten rules, their non-transparency, and the selectivity of law-enforcement.’<sup>27</sup> Hence, for instance, the dismemberment of YUKOS did not aim solely to transfer prize assets to companies connected

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<sup>23</sup> EIU, p. 9.

<sup>24</sup> Cited in Leonid Kosals, ‘Klanovyi kapitalizm v Rossii’, *Neprikosnovennyi zapas*, 50 (2006), p. 196.

<sup>25</sup> Kosals, ‘Klanovyi kapitalizm’, p. 191.

<sup>26</sup> Georgi Derluguian, ‘Under Fond Western Eyes’, *NLR* 24, November–December 2003, p. 138.

<sup>27</sup> Alena Ledeneva, *How Russia Really Works: The Informal Practices that Shaped Post-Soviet Politics and Business*, Ithaca, NY 2006, p. 188.

to the government; it also deliberately sought to create uncertainty among investors as to the rules of the game—preserving the prerogative of state officials to uphold or overturn property rights, according to the interests of their own fractions.

The Russian economy has long possessed a sizeable shadow sector. In the Soviet period, it was above all a mechanism for coping with shortages; similarly, in the 1990s, when cash was in short supply and, as Popov records, ‘the payment system was on the brink of collapse’, barter deals made up 50 per cent of total transactions and the shadow economy accounted for between 40 and 50 per cent of GDP.<sup>28</sup> The commodities boom has ensured a substantial monetization of the economy, but Popov warns that barter and non-payment could surface once more, ‘if the authorities resort to tight monetary policy’. This somewhat understates the extent to which informal economic mechanisms are a permanent feature of Russia’s socio-economic landscape. Again, the favourable macroeconomic climate conceals the persistence of unofficial channels; where the latter ‘were used in the Soviet economy to protect enterprises from the exigencies of the plan’, present-day recourse to them ‘protects companies from the exigencies of the market.’<sup>29</sup>

### *Crime and colonial war*

According to Popov, ‘the scale and scope of criminality in Russian society remains vast’. The murder rate currently stands at over 20 per 1,000—three times as high as that of the US, and ten times that of Western and Eastern Europe, Canada, China and Japan. Still, this is lower than before. There has, however, been a 60 per cent increase in the overall crime rate over 2002–06. Popov contends that this is ‘most likely a sign of better recording of crimes’.<sup>30</sup> Many would not share his confidence. A higher degree of (real or perceived) official competence no doubt encourages people to report crimes; but enough to account for a 50 per cent rise, over an already high rate? The persistence of informal practices mentioned above, the continued and growing corruption, and the further entrenchment of income inequalities, all work to expand the social fractures in which crime thrives. The fact that the law is manifestly an instrument at

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<sup>28</sup> Popov, ‘Russia Redux?’, p. 44; Kosals, ‘Klanovyi kapitalizm’, p. 184.

<sup>29</sup> Ledeneva, *How Russia Really Works*, p. 118.

<sup>30</sup> Popov, ‘Russia Redux?’, pp. 46, 49.



the service of particular interests and factions has arguably done much to undermine respect for legality.

But it is Putin's continued use of force that has contributed most to the legitimization of violence in the country as a whole. The war in Chechnya, waged with even greater ferocity than that of 1994–96, propelled him to the presidency in 2000, and has played a vital role in his consolidation of an authoritarian system: crushing Chechen aspirations to independence was the militarized component of Putin's re-centralization drive, and his uncompromising stance underpinned much of his initial public appeal. Popov glides past the atrocities and ongoing occupation, noting only that 'today the separatists are largely defeated'. Russian military and government spokesmen have declared victory several times—starting with Putin himself as early as 2000—but with the war now in its eighth year, no end is in sight. The Russian army continues to suffer casualties at an average rate of around 3 per week, picked off by a small but highly mobile resistance; the puppet regime Moscow has set in place consistently kidnaps, tortures and kills its countrymen, and is bereft of all legitimacy. There is no viewpoint from which Putin's war on Chechnya could be considered a success. Popov himself provides indirect confirmation of its failure when he refers to the 43 per cent of the population who in early 2004 wished the president to end it; by late 2006, the proportion of those in favour of negotiations with the separatists stood at 64 per cent.<sup>31</sup>

The war is a catastrophe whose consequences stretch far beyond the North Caucasus. In Russian society as a whole, Putin's counter-insurgency in Chechnya has fostered an upsurge in xenophobia and unapologetic imperialism, the killing of tens of thousands of Chechens portrayed as essential to the survival of Russia as a state. It has had a more directly damaging impact on over a million Russians, ranging from raw conscripts to mercenaries to law enforcement officers, who have passed through Chechnya since 1994: all of them have either committed or witnessed acts of boundless brutality, and for all of them, unlimited force is an officially sanctioned mode of conduct. The psychological trauma inflicted on soldiers by the war has been termed 'Chechen syndrome'. But the insidious symptoms of aggression are not

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<sup>31</sup> Popov, 'Russia Redux?', p. 50; poll data from Levada Centre, [www.levada.ru](http://www.levada.ru).

confined to veterans' minds; they have become rooted in Russian public and political life.

*The lesser evil?*

Popov concludes by emphasizing the need to choose the lesser evil of centralization and potential authoritarianism over the inevitable unravelling and chaos that will accompany any other course. Stability is the prime consideration; democracy can wait until more favourable circumstances develop. The question that immediately arises is: stability for whom? From the foregoing analysis, it should be clear that Russia's rulers have little interest in the fortunes of the general populace; the current priority is rather to use the country's natural resources to leverage a greater role in global affairs, and so carve out further opportunities for the internationalization of Russian capital. Entry into the WTO will assist in the latter goal, though it will also bring with it a dismantling of the protections that have served Russian industry well, and undermine recent attempts to revive manufacturing in the automobile and aviation sectors. To the dangers Popov lists, then, we should add the exposure to international capitalist pressures and widening of existing inequalities that inevitably accompany WTO accession. These forms of destabilization will, of course, largely bypass the fractions of business and state most actively seeking them.

Finally, there is the matter of the lesser evil. Popov poses the alternatives in stark terms: the status quo or utter disaster. Such logic has long helped to rally critics of various kinds to otherwise unpalatable governments. But it is precisely the immunity from challenge or debate that enables crime, coercion and corruption to flourish; conversely, it is the availability of alternative proposals for future paths of development that constitutes the political health of a nation. Popov's analysis presents many points from which such a discussion could begin.