The State of the Russian Economy: Balancing Political and Economic Priorities

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A strong and vibrant economy that addresses the interests and concerns of the entire population is a fundamental national interest of all countries. Russia is no exception. Unfortunately, the Russian economy is in a state of decline and stagnation. Moscow's policies is in work together to optimize each other's potential and to strive to achieve the best possible results for the national economy.

In this essay, I will examine the state of the Russian economy and the challenges the Russian government and private sector face in building an economy that meets the needs of the national interest and the international community.

Today's Popular View of the Russian Economy in Two Memes

"We have no money, but you have to think. Best defined Overall Take-Level" These two infamous memes are distributed by Anna Prima Donna (@Anna_Prima_Donna) during the Crimea on May 20, 2016, in response to questions from a crowd of pensioners complaining about their pitiful pensions and the government's failure to pay them. The first meme, "Crying, yes dimitrovs-kitchen," ("yes hang in there" / "have good cheer") is a popular phrase used to characterize the Russian government's inefficiency to the needs of ordinary citizens, particularly those in the country's vast provinces.

The second popular meme is an image of a large, gilded "rubber duck" floating on a dark pond, surrounded by a crowd of ducks. The caption reads, "Ducks, ducks, ducks, and a rubber duck." Russian political analyst Andrei Pertsev explains that the ubiquitous "rubber duck" is a reference to the Russian government's "Tsarevna" project, which is a pun on Russian society between the "Tsarevna" and the "have-nots," and the blatant inefficiency of the Russian economy. The "have-nots" represent the diverse and potential cause of future unrest in Russian society today.

Russia is not the only country with sharp societal divisions based on differences in economic and ethnicity. The problem arises when these divisions are used as a tool. For Russia, it is exacerbated by a period of mounting political uncertainty as Vladimir Putin's rule enters its twilight years. Moreover, the Russian economy is in a state of decline and is on a way to fall into a cul-power 1990 economic energy as the economic decline and stagnation are ensure a smooth transition of power.[1] Or will Putinism be unleashed in Russian society, which is a "Tsarevna" and a "have-not" society? Will the Russian government implement a social structure of the country? Or will the Russian government implement a social structure of the country? Or will the Russian government implement a social structure of the country? Or

Russians are very worried about the state of the economy. The independent Russian polling agency, Levada Center, reports that 77 percent of Russians say they, among about rising prices, 52 percent cited growing impoverishment, and 48 percent say one of the biggest problems is the growing gap between the rich and the poor. Russians see the bottom rungs of the economic ladder and have spread well into the middle class. As the economy stagnates and the purchasing power of the Russian consumers decreases, growing socio-economic discontent threatens to increase instability, and the risk of popular demonstrations against the Putin regime, something that has been occurring with increasing frequency since 2011. Yet, Putin's ability to quell popular discontent by increasing spending, improving social welfare, and Russian society. According to recent Russian Public Opinion Research Center surveys, "88 percent of the population say that antagonism between the rich and poor has become the main problem today. Society is fragmented, primarily due to economic inequality."

The response of the Russian government to the growing dissatisfaction with the economic crisis has been predictable. Putin has blamed the West for economic sanctions and seeks pressure when needed, and suppress—often with increased violence—popular demonstrations against deteriorating economic conditions. Most glaring, however, is the government's overall disregard for the plight of its low-income citizens. Recently, a new anchor in Russia's eastern region of Kamchatka burst out laughing as she was reading a report about how people living on the equivalent of $100 a month in the region. Recipients will get a little more than 1,000 rubles ($18) per month in welfare payments for medicines, health resort packages, and "international travel" to the resorts. It is no wonder that there is so much cynicism among the population about the government's interest in their needs.

Yale's Miller cites a Russian narrative that illustrates the quandary both the Russian consumer and the authorities face. Miller says that,

> the population is in a tug of war between their refrigerators and their televisions. The fridge is empty, but the television says everything is great. And for those who don't believe the television, there is the police baton. [T]o long as Russians sit at home, the Kremlin has no reason to keep their fridges full.

Despite Russia's more successful macroeconomic indicators, the ramifications at the microeconomic level of a stagnant economy for the consumer and the population, in general, pose a serious challenge to the future of the Russian economy and its political system. The promise of reform, which has been repeated ad nauseam over the years, as the panacea for Russia's ills, contains within it an inherent threat to the political system that has ruled since the collapse of communism. Will the Putin regime, for example, be able to continue its stumble along without significant changes? Will the implementation of reform be inevitable? Decisions made in the next few years may well determine the fate of the Russian economy.

The Imperative for Reform

There is little doubt that Russia cannot continue along its current path and widen in economic stagnation if it is to regain its status as a great power, become a stronger player on the world economic stage, and provide a better life for its people. Russia must modernize and institute meaningful reforms to move forward. Without change, the Kremlin risks growing social unrest and further degradation of living standards.

President Putin acknowledged this challenge in his State of the Nation Address to the Federal Assembly on January 15, 2020, in which he said that raising the income level of Russian citizens is ", the most important task of the government, and of the entire state." He stressed that "we need structural changes in the national economy and an increase in efficiency." He also promised that GDP growth would be increased investment in the economy. Such promises are well and good, but without sustained, aggressive government programs and private entrepreneurial initiatives, these are just empty words.

Russia's most prominent liberal economist and former Minister of Finance Kudrin has expressed concern over the direction of the Russian economy. In 2019, he issued the following assessment: "For the past six years, the country has not taken advantage of the opportunity to move forward. We are in a state of economic stagnation. Our economy is uncompetitive and efficient. We are in a state of economic stagnation. We that doesn't lend itself to optimism." He added that there is a "decline in real income. And when so many young people have been the prime by (2019), this worries me, and many people could begin expressing their concerns." By this, he means there is a greater chance now that young people will take to the streets and protest despite the risks of repression and suppression of violence. Frustration is mounting, but a satisfactory course correction is not imminent.

Impediments to reform are formidable. The largest impediment is the state itself. The state and its top officials benefit from corruption and the status quo. Reform would threaten their ability to keep the status quo and continue to plunder the coffers of the state. Officials may exercise over the economy. They have a vested interest in maintaining these controls and the rightful distribution among these power centers from which they derive their sustenance and strength. Therefore, they will continue to rely on state-sponsored projects, natural resource exploitation, and restrictive regulations to maintain their dominance and to impede competition and initiative from below. Consequently, such impediments to reform, as Yale's Miller points out, are not just "technical" but personal financial, fear and ideological in nature. Reform of the rule of law is independent judiciary, and an effective and persistent war against corruption are eschewed as anathema to sustaining the current political and economic order.

Because of oppressive governance and growing economic stagnation, which are increasingly impending some of the worst features of the Brezhnev regime of the 1970s–1980s, there is a decreasing capacity for the economy to diversify and grow. Putin periodically talks boldly about change, raising living standards, and reducing the worst abuses of his corrupt regime, as well as undertaking meaningful reform and investing in human capital and the next generation of leaders. Such steps, however, if pursued, could threaten to dismantle the very structure of control on which his authority is built. The result could be chaos.

Are the "National Projects" the Hope for Economic Prosperity?

Frustration is not just an emotion shared by a large segment of the general population; it is also a sentiment increasingly expressed by the technocrats and even some government officials who would like to see Russia pursue a different course. They are frustrated that their voices are not heard, that they are not able to effectuate positive changes and make a real difference in the lives of their compatriots. Many keep trying, but others can longer tolerate the inequities of the system and the lack of opportunity for professional development. They just instead to hone their knowledge and skills to develop their careers outside of Russia. Although the outside world benefits from these talented young men and women, Russia loses, the future of Russia loses.

In the meantime, the Putin regime continues to look for ways out of its economic maze without surrendering the levers of control that it so ardently guards. One glimmer hope for building a "bright future"[5] is the so-called "national projects."

The 12 "national projects" program, which the Kremlin initiated in 2018, is an attempt to create a new economic model based on supply-side investment. The program focuses on massive infrastructure development, major housing construction, transport and large-scale economic modernization over six years at a cost of $400 billion, one third of which is to come from private sector. This program includes major road-, bridge-, rail- and airport-building projects, substantial rehabilitation of urban housing, expansion and modernization of the country's telecommunications infrastructure, developing the "Northern Passage" Arctic sea route between the Far East and Europe.

Criticism of the national projects is widespread, not only among the general population but also among many economists. They argue that the program is overly ambitious and will fail to lift the economy because it does not focus on the real needs of the Russian consumer. The Economic Development Ministry claims that investments in the national projects will result in an 80 percent increase in the rate of growth over six years. But economist Regina Stephens of Oxford Economics argues that "the National Projects are no breakthrough for Russia's growth model, as long as institutions continue to constrain investment, the economy will underperform, regardless of how much cash is thrown at the wrong sectors." Russian economist Sergei Guriev points out that, in the case of projects, he claims that they will cost the Russian taxpayers trillions of rubles, but they will increase Russian GDP according to the International Monetary Fund, an average of only 1.4 percent through 2023, which, Guriev points out, will bring Russia back to the level it stood at in 2008.

Guriyev summarizes the criticism of the national projects this way:

> It is not surprising that experts and investors have little faith in the effectiveness of large-scale public investment in a country notorious for corruption. The solution to Russia's problems lies in precisely the opposite direction—in implementing the long-promised reforms protecting property rights, respecting the rule of law and competition, reducing the state's role in the economy, fighting corruption, reintegrating Russia into the world economy and investing in human capital.

Other critics recognize the problems of the national projects and admit that they will most likely fail to deliver results as promised, but they argue that these projects should be viewed not just in economic terms but also through a political lens. Even if only limited results are achieved, they argue, the projects will help the Putin regime maintain control over Russia for everyone. With elections coming up—both for the State Duma and 2024 for president—this can be a powerful tool for the politicians.

Technology and Reform

One of the major challenges Russia faces is insufficient diversification of its economy. The economy has grown over the years has come from the exploitation and export of its natural resources, primarily oil and natural gas. The Kremlin recognizes this challenge, acknowledges the need to increase investment in technology and digitalization of the economy, but struggles with implementing the measures to meet this challenge. Former Prime Minister Medvedev was known for his fascination with technology, and he was the driving force behind the establishment of the Skolkovo Innovation Center, a great admirer of Silicon Valley and sought to replicate its development of innovative technology by building the Skolkovo Innovation Center. The new prime minister, Mikhail Mishustin, is an economist and is known for promoting digital technologies in the workplace. There is hope that Mishustin will be a more successful promoter than Medvedev in expanding Russian development of innovative technology.

Unfortunately, advanced technology and digitalization, and its commercialization, face the same problems and roadblocks as most other aspects of the economy. The predatory practices of the government, the lack of rule of law, the stifling of initiative, arbitrary government regulations, and a poor investment climate have a chilling effect, particularly on private Russian companies that have the talent but not the resources to overcome the obstacles to innovation and commercialization. Many of these problems are rooted in the state changes its traditional concept that the people are for the state to one that empowers the people and provides the economic and political resources to pursue initiatives that benefit society and the state. Russia will remain far behind the world's leading countries in the areas of technology development and innovation. According to Russian President Vladimir Putin, whoever "rules artificial intelligence will rule the world." Kudrin's argument that "engineers are the most important people" is right, but incomplete. Not. What is clear, however, is that his policies for nearly 20 years now have for the most part hurt rather than helped Russia's technological competitiveness and prospects for long-term sustainable economic growth.[6]

Prospects for Meaningful Reform

Putin has made several attempts at reform during his 20 years in power. Most of those attempts have failed. Is there any expectation that implementation of the national projects, a change in government leadership under a new prime minister, or the anticipation of upcoming elections will bring about sufficient policy changes that could lead to a reform program that serves the interests not just of the elite but of the ordinary citizens as well.

Most experts take a pessimistic view. At a minimum, they argue that because of the upcoming elections the authorities will not attempt to make any drastic changes that could hurt either their constituents or jeopardize their power. Kudrin, who is 70-year-long regin has been maintaining a fragile political balance among the various factions of the elite and the Putin regime, is not optimistic that he will be able to pursue his reform agenda. Kudrin's "The Russian president would rather sit on his hands than risk disturbing the fragile political balance that ensures his power."

Bershidsky, further explains why reforms pose a threat to the Kremlin, Reforms, Bershidsky argues, that reduce

> the state footprint would undermine the most important pillar of the Putin regime. The employees of various branches of government and state companies and Putin's more reliable support base. Putin's billionaire friends have gotten rich from state procurement., and it remains the only source of their continued prosperity. Putin needs to keep these cronies happy if he wants to avoid a slash in the back. Given the regime's political foundation, Putin can't allow the kind of economic freedom that would attract foreign investment—property rights, courts, and a frightening assortment of unwritten debt.

In his book *The Putin System*, Grigory Yavlinsky, a veteran liberal political leader and economist, argues that "the prospects [for economic reform] are grim, inability to reform the economic system, the lack of independent institutions and slow collapse." "The only solution," Yavlinsky says, "is to elevate enough citizens so that when the rent 'fork is the road' comes, they can change the system."

That rent "fork in the road" may come in 2024 with the presidential election, or it might come earlier if Putin decides his future is already safely secured. A change in the system could mean little also, a new economic model and policies for Russia. This could come about if the Kremlin decides that it must do so in order to maintain its control over power, shift through the international sanctions and enforcement mechanisms to attract more investors, and encourage rather than discourage initiative from below.

As we have seen in the past, the Kremlin and its allies see such changes as a threat to their power and to the stability of the state. Yavlinsky, Kudrin, and Bershidsky are well-known and respected throughout the international community when, in February 2019, it arrested on dubious charges a major American investor in Russia, Michael Calvey. After months in prison, Calvey was remanded to house arrest where he still awaits trial because of his fate. That decision will not only determine the fate of Calvey; it may also impact the fate of future foreign investment and the course of the Russian economy.

It will take a long time for the negative clouds that hang over the Russian economy to dissipate, even if Russia seeks a different direction at a future "fork in the road." Until then, it appears that the Kremlin will continue to hunker down and avoid any steps that could threaten the status quo of the power elite, their ponderous Russian economy, and the system that sustains them.

What Do Leading Experts Predict for the Russian Economy?

The future direction of the Russian economy is unclear, and predictions among experts differ greatly. They range from the mildly optimistic (the view of some Russian government officials) to the Most analysts see continued stagnation at the minimum level, with some small improvement in the standard of living, depending on how serious the government is about implementing reform. Others see a worst-case scenario in which the power elite will surrender their right hold on the economic levers of control and choose.

Some take a more radical view and predict a potential socio-economic apocalypse if radical political reform is not set in motion in 2024 when Putin's term as president ends and a new president is elected. Most experts argue against such views, insisting that Russians are historically much more tolerant of authoritarian rule and are willing to accept a lower standard of living as they are left alone to manage their daily lives in a reasonably acceptable manner.

Instead of a predictive conclusion due to the uncertain path of the Russian economy, I offer a sampling of views of prominent experts on what to expect from the Russian economy over the coming years.

Trenin, the Director of the Carnegie Moscow Center and an astute observer and analyst of the Russian scene, frames the issue in a broad political-economic context. He wrote on Twitter on January 21, 2020, the following: "In 1990, Putin inherited near-chaos; over the following 20 years, he managed to turn it into a conditionally stable authoritarian and personalistic political regime. His ambition now is to convert the regime into a stable, Hard pile."

Following the appointment of Mishustin as Russia's new Prime Minister on January 16, 2020, Kirill Dmitriev, CEO of the Russia Direct Investment Fund sovereign wealth fund, offered an unsurprisingly positive assessment. He said that he expects the Mishustin government to be able to "deliver on the ambitious goals of the national projects and the pace of implementation of national projects." Dmitriev, who is reportedly a close ally of President in his Federal Assembly address,[7] Dmitriev opined that these measures should help increase economic growth to 3 percent in 2021. He ignore that Russia has not seen in quite a few years.

In an interview on August 8, 2019, with the popular newspaper Moskovsky Komsomolets, Igor Nikolaev, an economist and professor at Moscow's prestigious Higher School of Economics, offered a blunter assessment. He predicted that Russia faces a new economic crisis and explained why:

> There are four reasons why a new crisis is coming. Sanctions and counter-sanctions, the redistribution of budget funds, the deterioration of trends in oil prices, and slowing world economic development.... The crisis will definitely occur... Most likely, it will come in 2020. At least, it may delay until 2021... Should the sanctions be more severe, then the route will immediately lead, by dropping... [This will] the ruble exchange rate to collapse, consequently, inflation will rise."

To avert such a crisis, he urged three measures that need to be taken ", decreasing taxes, renouncing counterpressures, and establishing true freedom for entrepreneurs. However, our government, in any case, has so far acted in exactly the opposite way."

Picking up on the threat a weak economy poses to Russian domestic and foreign policies, Stratfor, a prominent American geopolitical intelligence platform, published the following assessment on January 21, 2020: "While a weak economy will probably hobble Russia's economic challenges not only will contribute to internal political and social instability, but they also will continue limiting Moscow's ability to project power internationally." They note that "economic weakness restricts the resources available to Russia to pursue its interests abroad, and it's also driving Russia to emphasize exporting and mineral resource extraction that can help drive the economy at home."

Yale's Miller offers the most widely accepted view of the future of the Russian economy. "Expect more corrosion from the state," Miller tells us,

> [B]ut don't expect much to change. The Kremlin's style of rule at home and confrontation with the West abroad have proved it. Over the next five years, Russia's economy will continue to stagnate, and the regime will continue to rely on state-sponsored projects in the absence of a new foreign crisis to rally around. Russians will probably judge the Kremlin's policies to be state. But state can be stable, even if Putin's approval rating slips further.... Russians are sadly used to economic stagnation and suffering under sanctions, and they are unlikely to be offered an alternative anything soon.

I conclude with the assessment of Jade Cordell, a business and economics reporter for the *Moscow Times*, who focuses primarily on macroeconomic issues, which on the surface present a more positive picture. In a piece for the Moscow Times on January 25, 2020, Cordell wrote:

> 2019 was an impressive year in the Russian business world. The Russian stock market was one of the best performing anywhere in the world—up more than 40% in dollar terms and setting new record highs in the process. Corporate profits soared—rising 12% and on track to pass the landmark 10 million ruble mark ($360 billion). As a share of GDP Russia's corporate profits come in second to China—more than twice the level it had compared with 8.5% in the United States. Businesses are expecting more of the same in 2020. Optimism among Russian CEOs is at a record high, and companies are betting on growth against a not insignificant set of challenges. There are a lot of reasons to be optimistic, they argue, and it isn't sure about their futures. The risk of a decline in domestic demand continues to wane business—most of that is undoubtedly connected with the economic slowdown, the VAT increase, increase in the retirement age, the trade embargo [sanctions], and other factors. But companies are betting that Russia's economic growth will continue despite these problems—including government interference in private companies and government lack of protections for investors—also lingers over the business community. "As the 2020s approach, Russia is caught between needing to find new growth drivers for your moribund economic growth, and a political economy set to protect the vested interests of established players," said the British global risk and strategic consulting firm, Maplecroft's [Sergei] McDowell. More restrictive conditions for the Russian internet and technology sector are on the horizon, and the risk of further international sanctions remains are still raising the kind of concerns that were prevalent at the start of 2020—[illegible] criminalization of corporate disputes, bloated bureaucracy, government interference, outdated regulations, weak investor protection, a politicized judiciary—those that change is a slow process in Russia. Surveys also reveal strong dissatisfaction with the modern business environment. Nearly half of respondents to a Russian Chamber of Commerce survey found SEM of business owners that it was easier to do business in Western 1990s than it is today. Stuart Lawson, a veteran British banker who came to Russia in the 1990s, said: "When it comes to Russia, I will be the last person to say that it is time to go and go you hope."

"It's never as bad as it feels, but never as good as you hope." These words ring true for so many, things in Russia, not just the economy. They also bring to mind the astute observation of Victor Chernomyrdin, President Boris Yeltsin's longest-serving prime minister who lamented: "We wanted the best, but it always turned out the same way." For the sake of the Russian people and their future, let's hope that the new memes chief at the beginning of this essay are eventually replaced by a more positive and promising meme, one that reflects the hope that the Russian people have promised since the Soviet days and has been so elusive, actually becomes a reality.

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[1] Shock therapy is a strategy to switch over to a market economy as quickly as possible. The strategy relies on price liberalization, budget stabilization, ending subsidies, and privatizing industry.

[2] In an effort to retaliate against sanctions imposed by the West, Russia enacted its own countersanctions, which amounted mainly to a ban on the importation of many Western foodstuffs and products. The ban on imported foodstuffs was a boon to the agriculture sector the Russian people felt the countersanctions even more. Not only were they deprived of their favorite food items, but they had to witness absurd scenes of destruction of Western goods that remained in Russia after the imposition of the countersanctions or were smuggled into the country. Piles of quality products were bulldozed, set on fire or destroyed by other means. Although this may have instilled a certain degree of patriotism among a certain class of Russians, it evoked disgust, anger and frustration among many others.

[3] A "bright future," or in Russian *yeetlaya budashchaya*, was a term used extensively by Soviet officials to rally the nation to the causes of communism and all the wonderful benefits awaiting the Soviet people. Over time, it became a term of derision among Soviet citizens and is still viewed that way today.

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