

BTI 2010 | Russia Country Report

Status Index	1-10	5.70	# 65 of 128	
Democracy	1-10	5.25	# 73 of 128	➔
Market Economy	1-10	6.14	# 54 of 128	➔
Management Index	1-10	3.45	# 106 of 128	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Transformation Index (BTI) 2010. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 128 transformation and developing countries are evaluated.

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Key Indicators

Population	mn.	142.1	HDI	0.82	GDP p.c.	\$	14690
Pop. growth	% p.a.	-0.3	HDI rank of 182	71	Gini Index		37.5
Life expectancy	years	68	UN Education Index	0.93	Poverty ²	%	<2
Urban population	%	72.9	Gender equality ¹	0.54	Aid per capita	\$	-

Sources: UNDP, Human Development Report 2009 | The World Bank, World Development Indicators 2009.

Footnotes: (1) Gender Empowerment Measure (GEM). (2) Percentage of population living on less than \$2 a day.

Executive Summary

The political and economic development of Russia has been highly influenced by the policies of Vladimir Putin, who served two terms as president from 2000 until 2008 and then became prime minister. In terms of the country's democratic transformation, no material progress was achieved during the period under study. To consolidate its power, the political elite that surrounds Putin routinely employs measures that conflict with democratic standards; this includes the marginalization of political actors outside the federal executive, the control over national mass media, the harassment of politically relevant NGOs as well as massive human rights violations committed during the government's fight against Chechen rebels in the Northern Caucasus.

In 2007 and 2008, such tendencies were brought into starker relief by the campaigns for the parliamentary and presidential elections. Though President Putin resigned at the end of his second term as the constitution demands, he reappeared on the political scene as prime minister, and his hand-picked candidate, Dmitri Medvedev, became his successor as president. Media coverage of both election campaigns was highly biased toward Kremlin favorites. Public demonstrations and gatherings of democratic as well as radical anti-Putin opposition groups were on many occasions ended through police violence. NGOs and journalists critical of the government were regularly subject to pressure from state organs. After the OSCE, which included the election campaigns in their monitoring, had declared the parliamentary elections "not fair," OSCE election observers were then discriminated against by the Russian authorities, so that as a result the observers decided not to monitor the presidential elections.

It is clear that the political leadership that surrounds Putin and Medvedev does not consider a qualitative enhancement of the process of democratic transformation one of the government's key tasks. Nevertheless, President Putin had stabilized the overall political system and instituted some basic democratic rules, such as free and fair elections (though not free and fair election campaigns), which are now by and large guaranteed. This situation has not changed under his successor, who however works in close cooperation with the now Prime Minister Putin.

In the transformation toward a market economy, there was progress in Putin's first term (2000-2004). The macroeconomic situation was stabilized. Regulation of some important policy fields was completely reformed. However, implementation has been rather inefficient because of bureaucratization, corruption and political interference.

In Putin's second term, the focus of economic policy shifted to embracing state-promoted industrial policy and large-scale projects in the social sphere. This policy was supported by a long-lasting economic boom, with GDP rising by about 70% during the eight years of the Putin presidency. The international financial and economic crisis, which reached Russia in the fall of 2008, marked the end of that boom. As a result, the state is now spending much of its funds saved during the boom to ease the economic and social consequences of the crisis.

It should be pointed out that the transformation strategy of Russia's political leadership aims primarily to preserve a stable political system and foster considerable economic growth. Violations of some fundamental democratic rights or market principles are apparently considered acceptable. Measured on such terms, then, Russia's political leadership has been quite successful. Measured by the normative standards of a market-based democracy, however, there are considerable and persistent deficiencies in the political sector and increasingly in the economic sector, too.

Within its conceptual framework, the Russian government behaves consistently in international politics. However, Russia has become very self-confident in recent years. Invitations to join high-level organizations and positive remarks about the state regarding its democracy are taken for granted and do not lead to any further efforts on the Russian side. Clear refusals and outright criticism are interpreted as a lack of understanding for the specific Russian situation. In combination with Putin's arrogant, aggressive and sometimes vulgar rhetoric, this has led to the impression of unpredictability among many foreign observers and governments. Though President Medvedev employs a softer style, he has not diverted substantially from Putin's policy course, and he is seen by many as still being de facto dependent on Putin's support.

History and Characteristics of Transformation

The economic and political transformation process in Russia began in the second half of the 1980s, with the reforms of Soviet General Secretary Mikhail Gorbachev. But the defining influences for post-Soviet Russia were the reform measures of Russian President Boris Yeltsin. The Russian constitution was approved by a referendum of the Russian people in December 1993. Parliamentary elections were held at the same time as the referendum. Outspokenly anti-democratic parties won 43% of the vote. Until 1999, there was no significant change in this balance of power. While the Russian constitution expressly provides for the democratic rule of law, constitutional realities under President Yeltsin were characterized by significant democratic deficiencies. These resulted not only from anti-democratic forces that stalemated reform projects

in parliament and ignored democratic requirements at the regional level, but also from executive policies of the Yeltsin administration, characterized by political manipulation and pressure on the mass media. In this context, actors without democratic legitimacy, like the so-called oligarchs, gained considerable influence in political decision-making.

The first milestone in Russia's transformation toward a market economy was the reform package that took effect in 1992. Its core components were the liberalization of prices and mass privatization. But instead of the anticipated economic upswing, Russia found itself facing a prolonged economic crisis. GDP had declined by more than 60% until 1998. Russia was competitive on the world market only as an exporter of raw materials. Imported goods dominated many sectors of the domestic market. Capital spending shrank dramatically, while capital flight remained high. Core economic reforms, including a new tax code and land code, were stalemated in the legislative process. The protracted economic crisis also adversely affected the population's standard of living, and social inequality increased considerably.

The situation substantially changed under Yeltsin's successor, Vladimir Putin. Putin has earned permanent approval from significantly more than half of the population. One of the core reasons for this was his decisive action to combat the country's "state of emergency." Here he won especially great approval for his military campaign against separatists and terrorists in the Northern Caucasus and for tough government measures against business tycoons, the so-called oligarchs. Politically under Putin new constraints were imposed on democratic principles, especially through interventions against press freedom and NGOs and through extensive human rights violations in the Chechen war. The political reforms of 2004 increased central control over Russia's regions in such a way that put the federal principle, outlined in the constitution, into question.

Whereas authoritarian tendencies could be observed in the political sphere from the beginning of Putin's first term, economic policy was for some time dominated by liberal ideas. An economic boom started in 1999 also contributed to Putin's popularity. Until 2008, Russia's GDP rose by more than 70%. In Putin's second term, economic policy increasingly focused on industrial policy, state control over "strategic" sectors of the economy and large-scale projects in the social sphere. However, widespread corruption, an extensive shadow economy, and the manipulation of the judiciary by the executive branch remained serious obstacles for economic and social development.

At the end of his second term in April 2008, Putin accepted the constitutional limit on presidential terms and did not seek re-election. Instead, his hand-picked and strongly supported candidate, Vice Prime Minister Dmitri Medvedev, won the presidential election with a margin that mirrored Putin's previous electoral successes. Medvedev, in turn, appointed Putin as prime minister, an action which promoted the impression that Putin is still in charge of Russian politics.

Transformation Status

I. Democracy

1 | Stateness

Russia's stateness is seriously questioned only in regard to the situation in Chechnya. Since the second Chechen war, which began in September 1999, the Russian army has been unable to achieve full control of the region. Chechen rebels regularly attack representatives of Russia's central power throughout the region, and they have committed several terrorist acts in the Northern Caucasus and in the Russian capital. Apart from the Chechen case, there are no serious limitations on the state's monopoly on the use of force.

Monopoly on the use of force

Apart from the separatist conflict in Chechnya, defining citizenship and who qualifies for it is not a politically relevant issue. The majority of the population defines the Russian state as based on the nations that historically have lived on its territory, with a dominant role ascribed to the Russian nation. Xenophobia is rather widespread and directed primarily at individuals from the Caucasus, Central Asia and Africa. Racial violence has led to several deaths. There are also many cases of discrimination by representatives of state agencies against Russian citizens who belong to ethnic minorities from the Northern Caucasus region.

State identity

Church and state are separate in Russian politics, and the general political process is secularized. However, the Russian Orthodox Church holds a privileged status and other religious groups, including the Roman Catholic Church and Islamic groups, have occasionally complained about discrimination. At the same time the Russian government has adopted an explicitly pro-Islamic stance on several occasions, and former President Putin has repeatedly pointed out that in absolute terms Russia has one of the biggest Muslim populations in the world.

No interference of religious dogmas

Apart from some regions of the Northern Caucasus, the state maintains a basic infrastructure (such as administrative institutions, fundamental administration of justice and apparatuses to implement political decisions) throughout the country; but bureaucratization, corruption and a lack of funds have made its performance erratic.

Basic administration

2 | Political Participation

At the national level, there are no serious restrictions on free elections, but some issues do exist in terms of election fairness. There have been instances of minor manipulations in some regions. As an exceptional case, elections in the Northern Caucasus (including national elections) have not met any level of democratic standards. Electoral fairness is limited. Election campaigns are regularly manipulated by the state administration throughout the country. This includes heavily biased media coverage, the use of state resources in support of specific parties or candidates, administrative discrimination of opposition candidates sometimes leading to questionable exclusions of such candidates from the ballot and bans on public demonstrations or assemblies by opposition parties. As a result of manipulated election campaigns, the election result can be seen as unfair despite a voting process which is by and large free yet, less so, fair (outside the Northern Caucasus).

Free and fair elections

In formal political decision-making, elected representatives have full power to govern. At the national level, informal influences by non-state actors, namely the oligarchs, but also influential lobbies from the agriculture or coal-mining sectors, have been successfully reduced under President Vladimir Putin. In some regions these actors still remain powerful. However, it is generally assumed that representatives of secret services and the military (combined under the Russian label of “siloviki”) have gained broad political influence. This influence is mostly formalized through appointments to official positions in government agencies and state-owned companies. Concerns about democracy in Russia thus focus on the behavior of elected or legitimately appointed representatives and not, however, on the influence of other veto powers.

Effective power to govern

There are considerable restrictions on citizens’ rights to organize and communicate political thoughts. NGOs critical of the national or regional governments have on many occasions been subject to harassment by state agencies. Since the run-up to the 2007 parliamentary elections, liberal parties have systematically been discriminated against by state administration and the media. Several demonstrations and public assemblies by opposition parties and movements have been banned or have been prevented to gather under administrative pretexts. Protests against specific state policies, such as social welfare reform, the demolition of houses or higher import tariffs on foreign cars, have also been broken up violently by police. In a special appendix to his 2007 annual report, the Russian Ombudsman for Human Rights has documented cases of what he calls the “at best highly subjective understanding” of citizens’ constitutional assembly rights by the police forces and the Ministry of the Interior. The Moscow Helsinki Group in 2008 published a report on the problems concerning a citizen’s right of association, declaring the issue to be one of the most pressing of Russian society.

Association / assembly rights

Mass media are subject to influence from the executive branch. During President Vladimir Putin's first term, private media with a nationwide reach have systematically been brought under (at least indirect) state control. In his annual report, the Russian Ombudsman for Human Rights stated in February 2006 that, "The main mass media, and first of all the leading electronic media, accounting for 90% of the information segment of the country and forming public opinion, are under the very strict control of state organs." This situation has not changed since then. Media coverage of elections is systematically manipulated. There are extensive restrictions on freedom of the press in covering the war in Chechnya. As a result, opinions critical of the government are on many occasions restricted to a handful of newspapers and radio stations with a very limited reach, which first of all aim reporting at the political and business elite, and to the Internet. Critical journalists and media outlets are often the subject of administrative harassment by the state, in the form of extensive fines for libel or intensive investigations by state organs, such as the tax administration.

Freedom of
expression

3 | Rule of Law

Serious deficiencies exist in checks and balances among the executive, legislative and judicial branches. As the president maintains a stable majority in parliament, the legislature exercises its review function only to a very limited degree. The judiciary is fundamentally independent, but lower-court decisions in particular are often influenced by corruption and political pressure. In specific high-profile cases, such as the Yukos affair, which saw Mikhail Khodorkovsky again on trial in 2009, principles of equal treatment and formal court proceedings have been violated in the interest of the national government.

Separation of
powers

Political interference as well as corruption leads to manipulation in the application of the law. In surveys, businesspeople regularly state that court cases against state agencies are more likely to be unfair than cases against rival businesses. In his first state of the nation address, President Dmitri Medvedev himself named corrupt and inefficient courts as a major obstacle to Russia's progress toward a modern society. The fact that about one-fifth of cases being heard at the European Court of Human Rights are from Russia might also indicate that Russian citizens consider their domestic courts to be biased. There is a differentiated organization of the judiciary and a formally adequate education and appointment system for judges. However, their professionalism suffers from the legacy of the Soviet era, from lingering corruption and from state interference. When an independent jury acquitted the accused in the murder case of journalist Anna Politkovskaya in spring 2009, the state reacted with a reform which limits the assignment of independent juries to minor cases.

Independent
judiciary

Russian leadership, including Vladimir Putin and Dmitri Medvedev, repeatedly names corruption as one of its main challenges. However, most anti-corruption efforts have been merely symbolic. Official accusations of corruption are still perceived as public relations campaigns inspired by political power struggles. The judicial prosecution of corruption charges has improved neither in quantitative nor in qualitative terms. Accordingly, there are no indications that corruption in Russia has been reduced in recent years. The Russian parliament is at present working on new legislation that would strengthen the prosecutions of abuse of political office.

Prosecution of
office abuse

Russia's political leadership often sacrifices certain democratic standards, such as the freedom of press and assembly, the right to a fair trial and the rule of law, to strengthen its own grip on political power, which is seen in turn as a precondition for providing stability. Lower courts are often biased in favor of local politicians or as a result of corruption and do not, therefore, offer efficient civil rights protections. In the fight against terrorism and the situation in the Northern Caucasus, security forces have decided at least implicitly that "stability" trumps the local population's basic human rights. This view is supported by the fact that human rights violations by Russian security forces are rarely investigated and hardly ever punished.

Civil rights

The state prosecution has also initiated biased and selective investigations against a considerable number of independent journalists and NGOs, most recently directed at the human rights organization Memorial, which saw its St. Petersburg offices raided by police and all computer hard disks confiscated. However, observers agree that there is no systematic purge and no clear pattern of general pressure on independent NGOs. Instead, bureaucratic harassment is sporadic and voluntary. The aim of such harassment seems to be to frighten off potential protests through show cases. An exception to this pattern has been public demonstrations by the political opposition. Such demonstrations were regularly banned by the authorities, and demonstrators regularly beaten up by the police or arrested. While such actions do not represent a systematic purge of oppositional political actors, in the sense that all gatherings are banned, these measures still ensure that opposition forces are not able to enter the public sphere.

4 | Stability of Democratic Institutions

Although subject to limitations on the rule of law, including political interference and corruption, democratic institutions are stable. However, the bureaucracy's implementation of legislated provisions often remains a serious problem, due to inefficiency. Another obstacle to the adequate performance of democratic institutions is a weak party system, which is dominated by the so-called party of power, United Russia.

Performance of
democratic
institutions

Most relevant actors view the institutions of the democratic state as legitimate. There is no serious opposition to the political system as it was reshaped by President Vladimir Putin and now continues to be molded by the Prime Minister Putin/President Dmitri Medvedev team. However, specific democratic institutions have on several occasions been ignored when the Putin administration perceived them as obstructing the realization of concrete political goals. In summary, the acceptance of democratic institutions is for most actors more a question of pragmatic consideration than of principle.

Commitment to democratic institutions

5 | Political and Social Integration

So far, Russia has been unable to establish an organizationally stable, socially rooted party system. The relevant political parties are predominantly associations based on personality. The Communist Party is the only party with an organized mass base; a state of affairs, however, that is not helpful to democratic consolidation. The party with the biggest faction in parliament, United Russia, was founded in 2001 through a merger of the two main rival parties from prior elections, both which had been founded in 1999. Of the nine factions formed in the parliament elected in 1999, only three were represented in the parliament elected in 2003. As a result of weak political parties and of the election victory of the pro-presidential United Russia, parliament has ceased to function as an efficient check on executive power. In the parliaments elected in 2003 and in 2007, the political opposition has been permanently marginalized. Due to changes in the party law and also due to discrimination, smaller parties, including the famous Yabloko party, are threatened with extinction. At the same time, United Russia has established an efficient election machine at the national level and in many regions. The population is highly skeptical of political parties, indicated by the fact that the share of the population claiming to trust them never exceeds 10%.

Party system

The ecology of interest groups related to the political sphere is sparse. Important social interests are underrepresented. The political leadership's reaction to work by interest groups has essentially been no more than symbolic. Prime Minister Vladimir Putin has stressed the need for a strong civil society in several well-publicized speeches, but at the same time he has blamed Russian NGOs for accepting support from foreign donors. NGOs critical of the government have been excluded from the dialogue between the state executive and civil society, and groups have on several occasions been harassed by state agencies. As a result of several years of harassment (or efforts to tame enthusiasm), the strength and variety of interest groups has been further reduced. Although President Dmitri Medvedev has adopted softer rhetoric, state policy has not changed.

Interest groups

The population's approval of democracy per se as voiced in representative polls is moderate to high, depending on the wording of the question. However, about a third of the Russian population is not able to give any meaningful definition of

Consent to democratic norms

democracy. Moreover, when asked about specific democratic principles, including democratic elections, accountability and civil rights, the majority of the Russian population does not consider any of these principles to be important, as polls by institutes such as the Russian Public Opinion Foundation (FOM) or the Levada Center regularly indicate.

In summary, about a quarter of the population is openly opposed to democracy, whereas barely more than 10% can be considered strong democrats. Accordingly, the vast majority of the Russian population has no strong opinion on the idea of democracy. This implies a sort of silent consent to democratic norms, but represents no principal opposition to undemocratic norms.

Self-organization in civil society encounters strong barriers, namely the burden of a Soviet past in which NGOs did not exist, and harassment by the state executive. Accordingly, NGOs are unevenly distributed across the country, flourishing mainly in the mega-cities of Moscow and St. Petersburg, and are often spontaneously organized and temporary. Many Russian NGOs owe their existence only to the engagement of international organizations and sponsors.

Associational
activities

II. Market Economy

6 | Level of Socioeconomic Development

The key indicators show a relatively high level of socioeconomic development for Russia. Measured in terms of HDI, the country's level of development permits adequate freedom of choice for almost all citizens. There is no indication of fundamental social exclusion on the basis of poverty, education or gender discrimination. The economic boom, which started in 1999 and led to a rise in GDP of more than 70% up until 2008, has been accompanied by an eightfold rise of average wages during Vladimir Putin's two terms as president (from \$80 per month to \$600). An important contribution to the income of the rural population comes from household plots used for agricultural production. Most of the output here does not reach the market as it is consumed domestically. The dimensions of this subsistence economy are hard to estimate; yet according to Russian statistics, its share in Russian agricultural production has risen to more than 40%.

Socioeconomic
barriers

However, at the same time social inequality as indicated by the Gini coefficient increased markedly in the 1990s and has since then remained largely unchanged. Reasons for this are long-term unemployment, an insufficient pension system and a

flat income tax rate. There are considerable regional differences in levels of socioeconomic development within Russia. Financial readjustments among regions do not materially reduce these discrepancies. The international financial crisis, which reached Russia in the fall of 2008, did not have a substantial impact on the social situation until spring 2009, as such indicators generally appear with a time lag after an economic downturn and also because the Russian state heavily increased spending to soften economic and social consequences.

Economic indicators		2004	2005	2006	2007
GDP	\$ mn.	591742.5	764531.1	990576.9	1290082.1
Growth of GDP	%	7.1	6.4	7.4	8.1
Inflation (CPI)	%	10.9	12.7	9.7	9.0
Unemployment	%	7.8	7.2	7.2	6.1
Foreign direct investment	% of GDP	2.6	1.7	3.0	4.3
Export growth	%	11.8	6.5	7.3	6.4
Import growth	%	23.3	16.6	21.9	27.3
Current account balance	\$ mn.	59511.7	84602.2	94686.4	77011.8
Public debt	\$ mn.	103403.7	76827.0	56427.3	70396.4
External debt	\$ mn.	196783.0	229910.9	250479.7	370172.5
Total debt service	% of GNI	3.6	5.6	5.2	3.2
Cash surplus or deficit	% of GDP	-	9.9	8.0	6.2
Tax Revenue	% of GDP	-	16.6	16.6	16.7
Government consumption	% of GDP	16.7	16.6	17.0	17.6
Public expnd. on edu.	% of GDP	3.5	3.8	3.9	3.1
Public expnd. on health	% of GDP	3.1	3.2	3.3	-
R&D expenditure	% of GDP	1.1	1.1	1.1	1.1
Military expenditure	% of GDP	3.8	3.7	3.6	3.5

Sources: The World Bank, World Development Indicators 2009 | UNESCO Institute for Statistics | International Labour Organization, Key Indicators of the Labour Market Database | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security.

7 | Organization of the Market and Competition

The foundations of market-based competition are assured by the country's institutional framework. Prices on the domestic market were freed in 1992. By now, price regulation by the state is restricted to utilities. The state also subsidizes prices for agricultural products. The national currency became freely convertible in summer 2006. Foreign trade was liberalized and currently the remaining restrictions are no more extensive than those in OECD countries.

Market-based competition

However, state economic policy remains skewed in favor of politically influential large corporations, especially state-owned ones. The state has increased its ownership in the economy and has in a number of economic sectors which are deemed to be of strategic relevance discriminated against private, and especially foreign, investors. The drive toward state ownership may be further strengthened by programs to tackle the international financial and economic crisis, which reached Russia in fall 2008. The informal sector amounted to 30% to 50% of GDP in the late 1990s. According to the Russian government, its size has been reduced considerably with the economic reforms under President Vladimir Putin. However, independent empirical studies are not available.

Although the recent economic boom led to a net capital inflow until mid-2008, red tape also presents a serious obstacle to running a small or medium-sized business. According to the World Bank study "Obstacles to Doing Business" for 2007/2008, Russia ranks 120th in a worldwide comparison, slightly ahead of India and Brazil, but below China. Russia ranks better for setting up a business, coming 65th in the worldwide comparison. As a result of unattractive conditions for business, investments are far from sufficient to satisfy the modernization needs of the Russian economy.

Broad sectors of the economy, defined as significant to national security, are shielded from competitive pressure. The "natural" monopolies in the natural gas and transportation industries have not yet been substantially reformed despite year-long debates over the issue. However, reform of the electricity sector was concluded in summer 2008, improving competition. In general the anti-monopoly agency functions rather efficiently for the liberalized part of the economy with exceptions on the regional level, where some administrations have blocked competition.

Anti-monopoly policy

Foreign trade has been liberalized in principle, but substantial regulatory exceptions remain, such as on imports of agro-food products or cars, and on exports of some metals, which has resulted in regular trade disputes especially with the European Union. In addition, Russia imposed new protective import tariffs on some agricultural products and on cars in late 2008 in reaction to the international economic crisis. Though Russia has reached bilateral agreements on WTO

Liberalization of foreign trade

membership with most relevant parties, its membership talks remain stuck. Major obstacles at the beginning of 2009 were Russian subsidies for agriculture, the role of state trading associations and Georgian opposition to Russian entry.

Though the liquidity of the Russian banking sector has improved remarkably since the financial crisis of 1998, it remains severely underdeveloped and is still not able to perform its economic function as a financial intermediary. Russian banks are not yet able to compete internationally. Moreover, the banking sector is dominated by state-owned banks. At the same time, differentiation of the Russian banking sector is increasing and seems to be working. State regulation of the banking sector has some deficits, but seems by and large to be adequate. Banks have been forced to adopt international standards, though at a slower pace than originally planned. However, the international financial crisis, which reached Russia in fall 2008, put a heavy strain on the small Russian banking sector. The Russian state guaranteed liquidity of the banking system and thus prevented a breakdown. However, assets and credit business are both likely to decline.

Banking system

8 | Currency and Price Stability

After the 1998 financial crisis, which caused significant inflationary pressure as the ruble lost around 70% of its value against the dollar, the government and the independent central bank were able to bring inflation under control and stabilize the exchange rate through a consistent budgetary and monetary policy. The national currency became fully convertible in summer 2006. Like in many countries, inflation accelerated in 2008 because of rising prices for raw materials (especially oil, gas and metals) and agricultural products. The financial crisis then put the exchange rate under pressure. In fall 2008 alone the Central Bank invested more than \$100 billion to stabilize the currency.

Anti-inflation /
forex policy

Under President Vladimir Putin, the country has adhered to a consistent austerity policy that regularly leads to budget surpluses, which made possible a significant reduction of foreign debt. The fact that monetary policy is integrated into general economic policy is also indicated by the stability fund, which was introduced to save the state budget's windfall profits from high oil prices for the future. This fund has successfully been defended against demands for increased state subsidies. Saving windfall profits during Putin's presidency then, in fall 2008, offered the Russian government the chance to react to the international financial and economic crisis with extensive liquidity support and stabilization programs.

Macrostability

9 | Private Property

Property rights and the regulation of the acquisition of property are defined formally in law. With the exception of the sale of farmland, the legal provisions are practical.

Property rights

They are not, however, consistently implemented nor adequately safeguarded by law, especially against state intervention. For example, high-level state officials have repeatedly cast doubt on the validity of the privatization auctions conducted in the 1990s. In “strategic sectors” such as the oil industry, the state seems to systematically reduce the share of private owners through administrative pressures, which leads either to confiscations or to negotiated sales. Some property rights, especially copyrights, are regularly ignored.

Private enterprise is the backbone of the economy, accounting for about two-thirds of the economy. However, for the first time since the end of the Soviet Union, the share of private enterprise overall considerably decreased in 2005. This seems to be a result of the Russian government’s attempts to bring “strategic” enterprises back under state control. The prime example for this is the oil industry, where the share of state companies in production has risen from about 15% in 2004 to about 40% in 2008. There are also market concentrations tolerated by the state, especially in the “natural” monopolies, such as natural gas and railroads.

Private enterprise

10 | Welfare Regime

Parts of the social security system (especially health care) are relatively well-developed in Russia, but they do not cover all risks for the entire population. Moreover, efficiency and availability to social aid is reduced by widespread corruption. There is almost no state support for the unemployed. Though pension payouts have been increased considerably in recent years, they are still insufficient to survive on. Without additional income, such as a job in the shadow economy, private farming or family support, pensioners are at risk of slipping into poverty. The bigger cities have large numbers of homeless people whom state social facilities completely fail to reach.

Social safety nets

Economic improvements since 1999 have mitigated the country’s social problems, as wages and employment rates have risen and poverty has been reduced. But improvement in the state’s social insurance systems has been limited. Under President Vladimir Putin, the reform of the state’s social welfare system aimed at liberalization. However, most Russians lack the financial means to purchase private insurance and especially in the pension system, private companies are underdeveloped. Special government programs to improve health care and fight rural poverty have had only a very limited impact, mainly due to the size of the problem and the inefficiency of the state bureaucracy. For example, as the state health care sector employs 700,000 doctors and an additional 1.5 million trained medical personnel, even a rise of salaries to the average level for respective educational qualifications was impossible. Another problem with the special state programs is that they did not establish meaningful accounting mechanisms for the use of funds.

Equality of opportunity is not fully assured. There are substantial differences from one region to another. Members of non-Russian ethnic groups, especially those from the Caucasus, suffer systematic discrimination in the educational system and on the job market. In Moscow, for example, citizens from the Caucasus region have been banned from working at public markets. Social exclusion extends to people living in the Northern Caucasus, where in some regions living standards are far below the Russian average, a quarter of the population is unemployed and wages are far below the national average. There are sizeable communities of homeless people in the bigger Russian cities. Throughout the country, women have equal access to education but are underrepresented in the political system and in business management.

Equal opportunity

11 | Economic Performance

After the dramatic deterioration in macroeconomic fundamentals caused by the 1998 financial crisis, an improved economic environment, characterized by an undervalued ruble, rising prices for Russian exports of raw materials in the world market, and low real wages, laid the foundations for significant economic improvement. During the eight years of Vladimir Putin's presidency, Russia's economy grew by about 70%. At the same time, all key macroeconomic indicators improved considerably. In 2007, Russia's GDP grew by 8%, the CPI inflation rate stood at 12% (compared to 20% in 2000), unemployment was down to 6% (from 10% in 2000) and the state budget ran a surplus equal to 5% of GDP. However, the international financial and economic crisis, which reached Russia in fall 2008, put a heavy strain on the economy. In the fourth quarter of 2008, Russia's industrial production contracted by about 10% and unemployment increased for the first time since the 1990s.

Output strength

12 | Sustainability

Russian economic policy is focused on medium-term economic growth. Ecological concerns are entirely subordinated to growth efforts, despite a considerable legacy of environmental damage from the Soviet era. Accordingly, environmental concerns are only on the political agenda when they promise to deliver clear material short-term advantages (as they can be used to put pressure on unwanted investors).

Environmental policy

The long-term political effort to reduce economic dependence on raw material production would also reduce negative environmental effects. But again, environmental concerns are hardly ever mentioned as a reason for this strategy. Administrative reforms under Vladimir Putin have weakened further the limited institutional base for environmental protection, in both state and NGO settings. When the focus of economic policy shifted increasingly to direct state control, and

when additionally the international economic crisis put an end to the country's economic boom, environmental concerns became even more sidelined.

Russia inherited from the Soviet Union an educational system with comparatively high standards, able to compete on a world scale in some segments. Under post-Soviet conditions, however, the country has been unable to put this educational potential to good economic use. Rather, Russia has faced mass emigration of top personnel. Funding shortages greatly reduced the quality of the state educational system. The private educational sector has not developed far enough to make up this deficiency. Research and development is still up to world standards in some areas, for example in space technology, but in general Russia is below the level of OECD countries in quantitative as well as qualitative terms.

The Russian government reacted to this by declaring education a top priority as one of the four national projects which receive considerable additional funding. The government has also designed programs to improve research and development as well as academic tuition. Russia has joined the Bologna process which aims to create a common European academic education system. Government spending on education is now slightly below 5% of GDP and spending on research and development stands at slightly below 2%.

Education policy /
R&D

Transformation Management

I. Level of Difficulty

The structural constraints on governance in Russia are moderate as key indicators show a relatively high level of socioeconomic development. The country has an educated workforce. There are no serious geographic or infrastructural deficiencies which could not be overcome by good political management. However, the production of raw material in northern regions poses a real challenge. Also, a decline in health care standards and alcoholism are causing a serious demographic problem. Russia's population has declined from 147 million people in 2000 to 142 million in 2008.

Structural
constraints

Throughout most of Russia's history, civil society was heavily suppressed. Independent NGOs started to develop only in the late 1980s. The only older tradition NGO members can refer to is that of the dissidents and human rights activists of the Soviet period. Trust in institutions and general social trust are extremely low in Russia. A civic culture of moderate participation in public life has not yet been developed.

Civil society
traditions

In the Northern Caucasus, ethnic conflicts have the character of a civil war and are associated with terrorist acts. They also have a religious dimension. Apart from this, visible divisions of Russian society have not yet transformed into conflicts. The non-Caucasian ethnic communities traditionally living on Russian territory have been accommodated within the federal system. The same applies to religious communities. However, xenophobia and anti-Semitism are widespread among the population. Several people were killed in racist attacks in recent years, especially in the big conurbations of Moscow and St. Petersburg.

Conflict intensity

II. Management Performance

14 | Steering Capability

While Russian policies under President Boris Yeltsin (1993-1999) presented a largely desolate picture of incompetence and short-term power grabs, after President Vladimir Putin took office in 2000 he immediately defined clear, long-term priorities that have dominated the policies of his administration and were adopted by his successor, Dmitri Medvedev, when he took office in 2008. However, these long-term priorities are inconsistent with the goal of transformation toward a market-based democracy. On the political side, the main aim is executive control over the legislative process and the implementation of policy measures. On the economic side, the state aims to promote economic growth through direct intervention. The state increasingly aims at direct ownership of enterprises in sectors of “national strategic relevance.”

Prioritization

This policy is rather consistently transformed into legislation, as the state executive has a huge majority in parliament. However, implementation suffers from administrative weaknesses. As a result, policies which can be implemented by a small group of competent administrators, like monetary policy and the management of the stabilization fund, or to a certain degree competition policy, have a high chance of successful implementation, while most of the reforms, like national projects, social or education reforms, rely on larger bureaucracies and are therefore prone to corruption, lack of accountability and bureaucratic inertia.

Implementation

In response to administrative and political resistance to reform, the government has increasingly resorted to heavy-handed control or pressure tactics. At the same time, criticism over reforms is met with increasing arrogance on behalf of the government. As a result, independent decision makers, advisory bodies and civil society organizations are increasingly brought under Kremlin control and oppositional voices are repressed or ridiculed.

Policy learning

A prime example for the underlying ignorance toward criticism is the failure of the Kremlin to acknowledge the concerns of the European Union during the gas conflict with Ukraine in January 2009. Although Russia’s gas company, Gazprom, and not Ukraine as a transit country is legally responsible for gas supplies to the European Union, Russia simply put the blame on Ukraine instead of doing everything possible to restore supplies. When the European Union later agreed with Ukraine to modernize the country’s gas transit pipeline network, the Russian energy

minister ostentatiously left negotiations. While overall Gazprom showed more concern with public relations than during its prior gas conflict with Ukraine in 2006, the Russian side was not able to adequately react to EU concerns. Instead, the Russian leadership simply blamed Ukraine and felt offended when the European Union demanded a reaction not only from Ukraine but also from Russia.

15 | Resource Efficiency

Although reforms under President Vladimir Putin have improved resource efficiency considerably, Russia is still far from achieving an effective use of resources. While a stringent austerity policy has yielded significant progress in the use of government funds, the effective use of staffing and organizational resources continues to languish because of the problems of an oversized, often corrupt and only modestly competent administrative apparatus.

Efficient use of
assets

The state budget has been consolidated and has shown a surplus since the beginning of Putin's presidency. The level of state debt has been considerably reduced, leading to regular upgrades in the investment ratings of Russia's sovereign debt. The processes of budget planning and spending discipline have been improved considerably. However, there is no effective audit and reports by the parliament's audit chamber have on most occasions been ignored.

With a share of 2% in total employment, the bureaucracy of the Russian state executive is not oversized when compared internationally. However, its organizational structure and code of behavior often leads to considerable inefficiencies. Although Putin and President Dmitri Medvedev regularly stress the need for administrative reform, regular re-organizations have not led to structural improvements as they are not able to efficiently tackle the problems of corruption, inefficiency and conflicts over competencies. As a result, what starts off as coherent strategy and legislation on the leadership level is regularly being distorted at the implementation level.

There is a serious division of the Russian government into two ideologically opposed camps. Liberal reformers who were initially in charge of economic policy under President Vladimir Putin have increasingly been sidelined by politicians with a secret service or law education background. Some of the liberals' major projects, aimed at reforming companies close to the state, have been delayed. However, some major policy areas, like financial policy or electricity sector reform, are still dominated by liberal policymakers. In the second term of Putin's presidency, the state executive was increasingly marked by conflicts between different government camps over competencies and especially control over state-owned enterprises. In addition, many policies are not implemented properly due to bureaucratic inefficiency and corruption.

Policy
coordination

Corruption is widespread in Russia. This impression is shared not only by independent experts (including international expert opinion as measured in the CPI of Transparency International) but also by top state representatives, including the president, who regularly name corruption as a key problem.

Anti-corruption
policy

This situation can be explained with the nearly complete lack of functioning integrity mechanisms. State auditors are often competent, but auditors lack enforcement powers. Rules to hold politicians or bureaucrats accountable are underdeveloped and not enforced in practice. Procurement is still open to manipulation, although regulation has been improved. Corruption is not systematically prosecuted and courts themselves are highly corrupt. Civil society is too weak to have a real impact on the situation and NGOs are systematically discouraged from engagement in corruption and public integrity issues.

16 | Consensus-Building

The elite consensus developed under President Vladimir Putin is not primarily oriented to creating a market-based democracy. The major political actors agree on the Putin model of a “controlled democracy” and a limited market economy. That means they accept the existing political and economic system, including democratic elections as the main way of transferring political power, but they do not agree on a market economy and democracy as strategic long-term aims and do not object to violations of democratic standards, as in the case of biased election campaigns. Actors in favor of a market-based democracy, like the political parties Yabloko and Union of Right Forces or other public democratic movements, have been increasingly marginalized in recent years and are no longer granted free access to public discourse.

Consensus on goals

There are no relevant pro-democratic reformers represented in the ruling elite. Representatives of genuinely democratic movements have been marginalized in Russian politics.

Anti-democratic
veto actors

Vladimir Putin has achieved considerable progress in consensus-building compared with his predecessor, Boris Yeltsin. The notion of the “Putin majority” has now become a fixture in the country’s political vocabulary. Parliamentary opponents of reform have been successfully marginalized. Putin’s opponents in the regions have also seen their position weakened. President Dmitri Medvedev continues this policy in tandem with now Prime Minister Putin and has thus been able to profit from Putin’s popularity. A large majority of the population supports the Putin/Medvedev team. The appeal for broad-based collaboration to overcome the “state of emergency” is a core component of their political rhetoric. In this respect the international financial and economic crisis, which reached Russia in fall 2008, might even help them to justify a continuation of their policies. Thus the political leadership has managed political cleavages in a way which makes escalation highly unlikely.

Cleavage /
conflict
management

Officially the state executive aims at a dialogue with civil society. For this purpose President Vladimir Putin signed the law on the Public Chamber in April 2005. The Chamber, consisting of citizen representatives and civil society organizations, is intended to advise political decision makers on a wide range of public issues. Independent NGOs have criticized the makeup of the Chamber as being heavily influenced by the political leadership. As a result the Chamber has so far had no significant influence on political decisions or public debates.

Civil society participation

Both civil society and the mass media risk serious harassment from state organs when they engage in unwelcome criticism of the state. Most mass media have been brought under state control, and the creation of the Public Chamber in combination with the more restrictive new NGO law seems to be an attempt to bring civil society under control, too. Those remaining outside state control are often oppressed or ridiculed.

Dealing with past injustices is no major topic in Russia's public debate. Attempts by civil society organizations to initiate a public debate on Soviet human rights abuses are hampered by a government policy which wants to celebrate Soviet successes and forget Soviet repressions. In a popular show of state television channel "Rossiya," former Soviet General Secretary Joseph Stalin came third in a vote of Russia's most important heroes. Opinion polls indicate that Mikhail Gorbachev and Boris Yeltsin are much more unpopular than any Soviet leader.

Reconciliation

17 | International Cooperation

While Russia under Boris Yeltsin cooperated with international partners like the World Bank or the IMF, the state government often used international aid for inappropriate purposes and applied only a very limited amount toward improving policies. President Vladimir Putin, by contrast, rejects international aid. He has criticized NGOs receiving support from abroad as acting as agents of foreign powers. His public explanation is that Russia does not need foreign help to develop. It can arrange the necessary measures on its own. Rhetorically, Putin has defended the Russian "way of (or to) democracy" with increasing self-confidence as being in line with Russian traditions and has denied the moral right of foreign actors to make judgments concerning Russia's political system and human rights record.

Effective use of support

Within its conceptual framework, the Russian government behaves consistently in international politics. However, tensions have been rising for three reasons. First, Russia increasingly assumes the attitude of a great power, using its permanent seat at the United Nations Security Council and its good relations with some states under considerable international pressure (like Iran or Uzbekistan) to hamper international conflict resolution. Second, there have been serious conflicts about Russian energy exports which have led to supply interruptions in the European

Credibility

markets and have caused worries, especially in the European Union. Third, Russia treats the CIS region as its sphere of influence and reacts to conflicts with increasing assertiveness. This led to an escalation with the South Ossetian war, where Russia reacted disproportionately to Georgian provocations by occupying large parts of the country and later recognizing the two breakaway republics of South Ossetia and Abkhazia as independent states (contrary to the argument it had used against the independence of Kosovo).

In combination with Vladimir Putin's arrogant, aggressive and sometimes vulgar rhetoric, this has led to the impression of unpredictability among many foreign observers and governments, with the U.S government under President George W. Bush opting for a strategy of containment. Some foreign governments in the West, notably Germany and Italy, stress however the reliability and consistency of Russian foreign policy.

In relations with neighboring countries, Russia still applies a foreign policy concept based on ideas of regional hegemony. However, Russia has been unable to transform the CIS into its own "backyard." Whereas some CIS countries, like Kazakhstan or Belarus, have accepted Russian dominance in return for preferential economic treatment, and others, like Turkmenistan or Uzbekistan, have opted for pragmatic cooperation with Russia but refrain from closer integration, other CIS countries are in open opposition to Russian foreign policy. In dealing with neighboring countries critical of its foreign policy, Russia regularly provokes the escalation of single-issue conflicts into broader state affairs. Most notably, the year-long conflict with Georgia escalated into a war in August 2008. In January 2009, the conflict over natural gas deliveries and transit between Russia and Ukraine escalated, when both sides took an uncompromising stance.

Regional
cooperation

Strategic Outlook

As President Vladimir Putin has successfully managed the re-arrangement of the division of power after the end of his second presidential term and has ensured that he can continue to coordinate Russian politics as prime minister in close cooperation with his hand-picked successor as president, Dmitri Medvedev, any major changes in Russia's political and economic policy are unlikely in the near future. The international financial and economic crisis, which reached Russia in fall 2008, will however pose a serious challenge for economic policy.

In the political sphere, the Putin/Medvedev team is able to realize most reform projects unchallenged. The political opposition remains marginalized and political pressure on mass media and politically active NGOs persists. The armed conflict in the Northern Caucasus, combined with terrorist attacks and massive human rights abuses by Russian military and law enforcement bodies, continues.

As the aims of the Putin/Medvedev team are clear and as they have proven unwilling to change their position in reaction to criticism from abroad and as Russia is strong enough to ignore foreign policy pressure, external supporters of Russia's development to a market-based democracy can either opt to accept Russia's conditions and find a niche for specific support programs or decide to withdraw from relations with Russia.

In the economic sphere, the state executive focuses on increased control over strategically important enterprises. The formation of state-controlled holding companies in sectors of the economy deemed to be of strategic importance continues. Structural reforms or genuine improvements in the efficiency of the state bureaucracy (including advances in the fight against corruption) are not on the agenda. However, the government will probably no longer benefit from windfall profits caused by high oil prices. In financial policy Russia will be able to reap the fruits of its consistent austerity policy. However, like many governments the Russian one, too, is most likely to fight the crisis with direct state intervention into the economy through subsidies, protective tariffs and company takeovers. As a result Russia will move further away from a market-based economy. Integration into international organizations like the WTO or into concerted efforts to fight the effects of the economic crisis might help to improve Russian economic policy, if there are any meaningful international policy initiatives.

Russia has become very self-confident in recent years. Invitations to join high-level organizations and positive remarks about the state of its democracy are taken for granted and do not lead to any efforts from Moscow for improvement. However, clear refusals and outright criticism are interpreted as a lack of understanding for the specific Russian situation and are met with insults and aggression. This poses a heavy burden on international attempts to mitigate conflicts in the CIS region, as has been shown by the South Ossetian war in August 2008 and the Russian-Ukrainian gas conflict in January 2009. With the present Russian leadership it is hard to introduce international mechanisms of peaceful, rule-based and transparent conflict regulation. Nevertheless, this seems to be the only option available.