

A Putin policy without Putin after 2008?

Vladimir Popov, Professor, New Economic School

On October 1, 2007, two months before the parliamentary elections (December 2, 2007) and less than half a year before the presidential elections (March 9, 2008) President Putin agreed to put his name on the electoral ballot sheet of the largest Russian party “United Russia” that always supported him, although he was never a member. He did not exclude the possibility that he will accept the post of the prime minister. Thus, Putin made it clear he is going to stay in politics even after his second presidential term comes to an end.

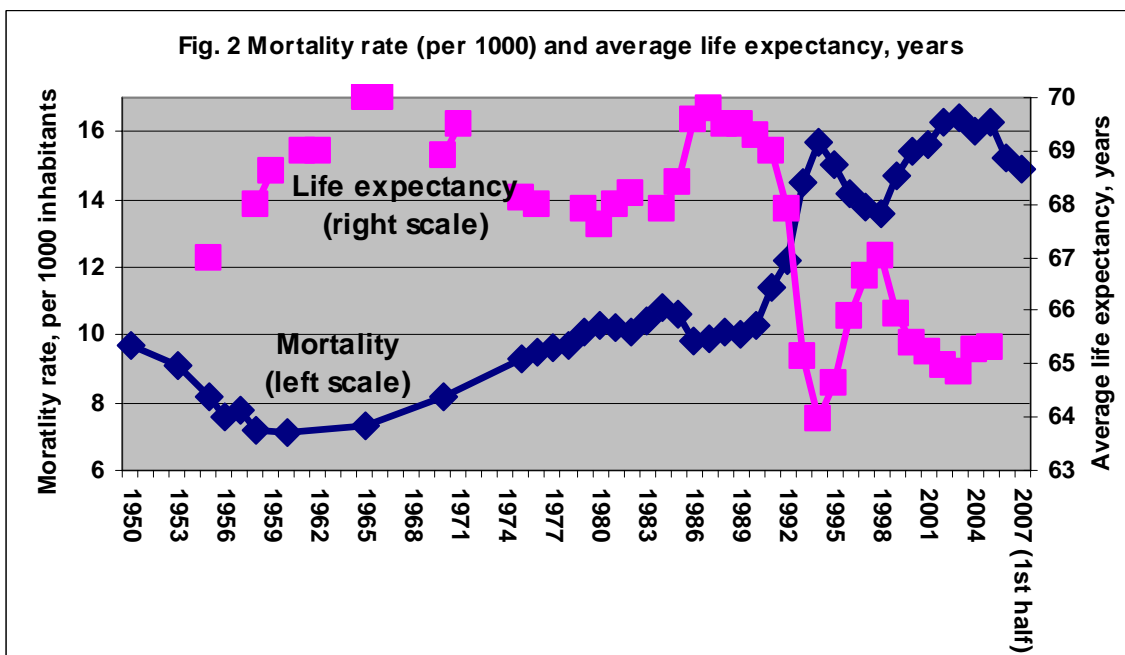
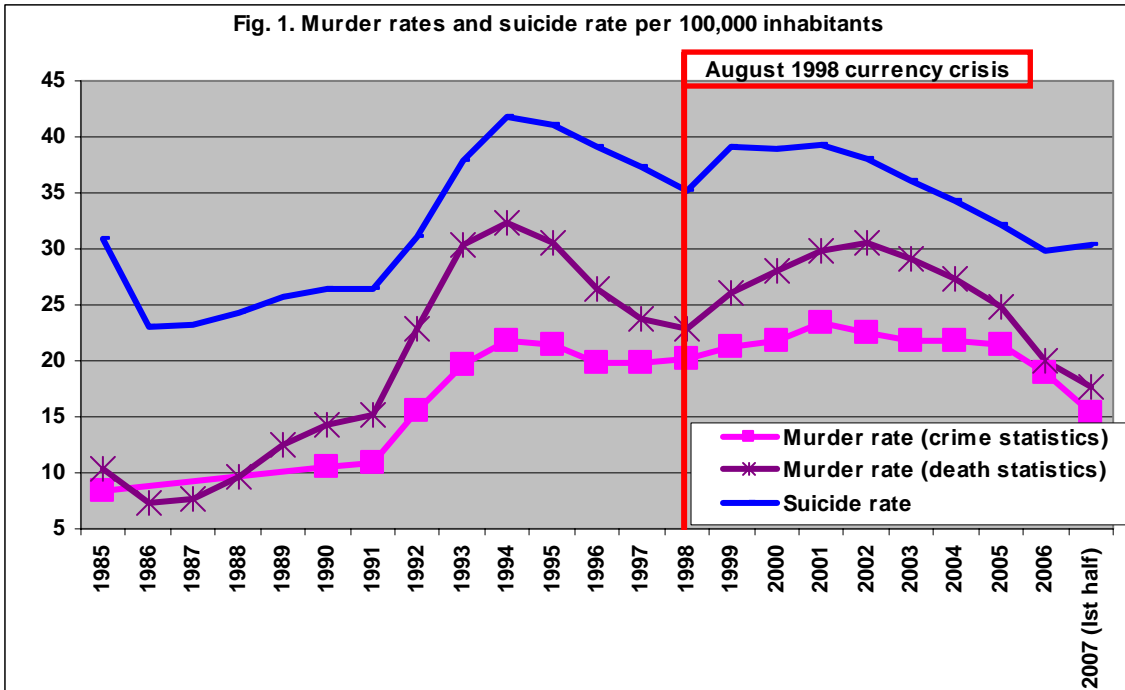
Putin’s desire to remain in politics is quite understandable: he is prohibited to run for the third presidential term by the Constitution, but he remains extremely popular – 53% voted for Putin in 2000, 71% - in 2004, and over 60% said they would vote for him in September 2007, even though he is not going to run. The secret of his high popularity is simple – he is leaving the country in a better shape than 8 years ago, when he came to power.

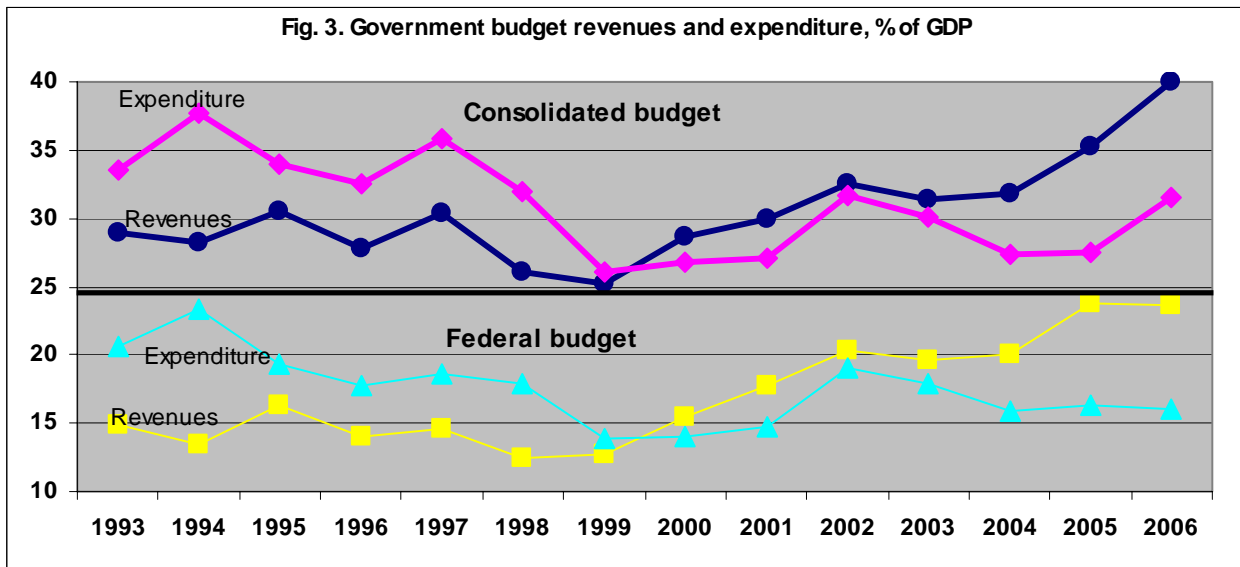
Putin’s legacy: achievements

The stabilization of the past 8 years is especially impressive, if compared to the period of disarray of “the rocky 1990s”. Russian economy lost 45% of output during transformational recession of 1989-98, income inequalities increased greatly, crime rate doubled, life expectancy went down from 70 to 65 years. The short-lived stabilization of the 1995-98 (when the ruble was pegged to the dollar and inflation subsided) ended up in the spectacular currency crisis of August 1998 – the ruble then lost over 60% of its value in several months, inflation got out of hand again, crime, suicides, mortality increased once more (fig. 1).

However, after the 1998 currency crisis Russian economy started to grow – the average annual growth rate totaled about 7% in 1999-2007 (fig. 2), so now the GDP gradually approaches the pre-recession level of 1989. Real incomes and personal consumption increased even faster – they more than doubled in 1999-2007 – and have already surpassed the pre-recession level of the late 1980s. Economic growth and high world fuel prices helped the government to collect more tax revenues, so the government budget moved from a deficit to surplus, and government spending as a proportion of GDP increased since 1999 (fig. 3), allowing to restore partially the institutional capacity of the state that was lost in the 1990s. Moreover, high oil and gas prices in the world

markets allowed Russia to enjoy high foreign trade surpluses and to accumulate foreign exchange reserves – they increased from less than \$15 billion right after the 1998 currency crisis to over \$400 billion by the end of the 2007.





What is most important, the economic growth and gradual restoration of government's ability to provide public goods led to the improvement in the social sphere – since 2002-03 the murder rate, suicide rate and mortality rate started to fall, albeit very slowly, birth rate and marriage rate increased, the decline of the Russian population (it fell from 148,5 million in 1990 to below 143 million in 2007) slowed down.

Putin also managed to strengthen the unity of the Russian Federation – the separatists in the break away republic of Chechnya were largely defeated and the regionalist trends in other regions were suppressed. Financial tycoons that gained strength during the 1990s and wanted to supplement their wealth with political power by “privatizing the state” got a clear signal from the government that they should stay away from politics: Mr. Khodorkovsky, the owner of the major oil company “Yukos” with open ambitions to replace Mr. Putin as a president, was arrested for financial fraud in 2003.

No wonder, Russian citizens appreciate the new stability of recent years and are not interested in seeing the new leadership and changes in the current course. The opinion polls conducted in September 2007 showed that over 60% of Russians were willing to see Putin as a next president (even though he does not have the right to run and said many times he will not run), whereas the majority is apparently willing to vote for any candidate that would be supported by Putin.

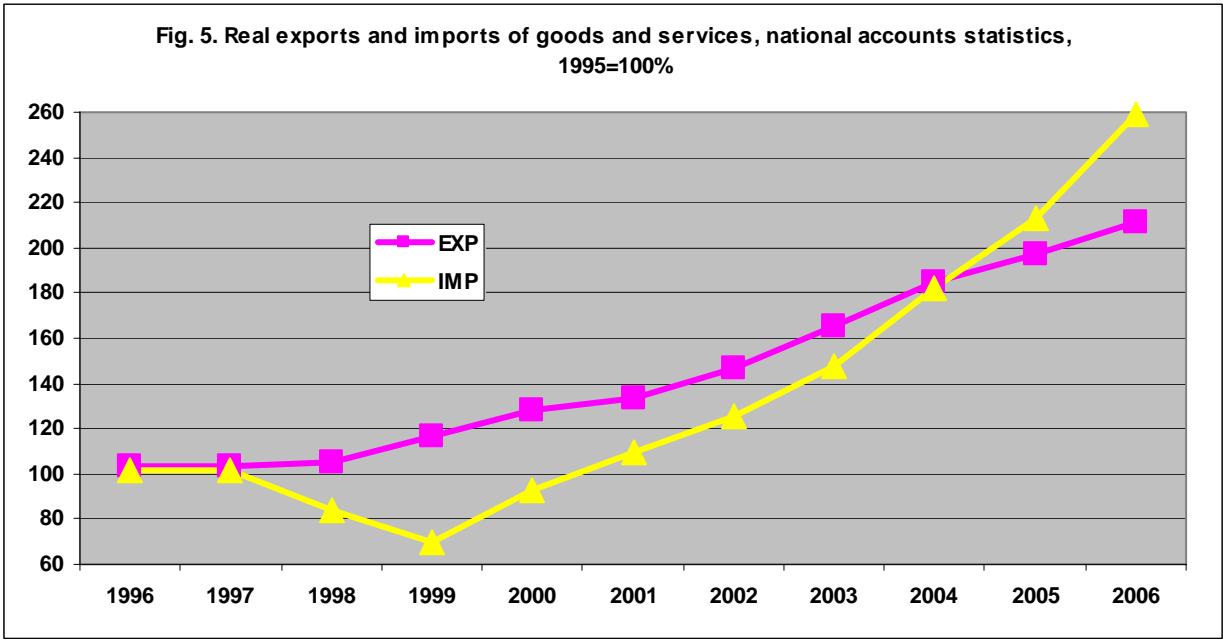
]

Putin's legacy: problems

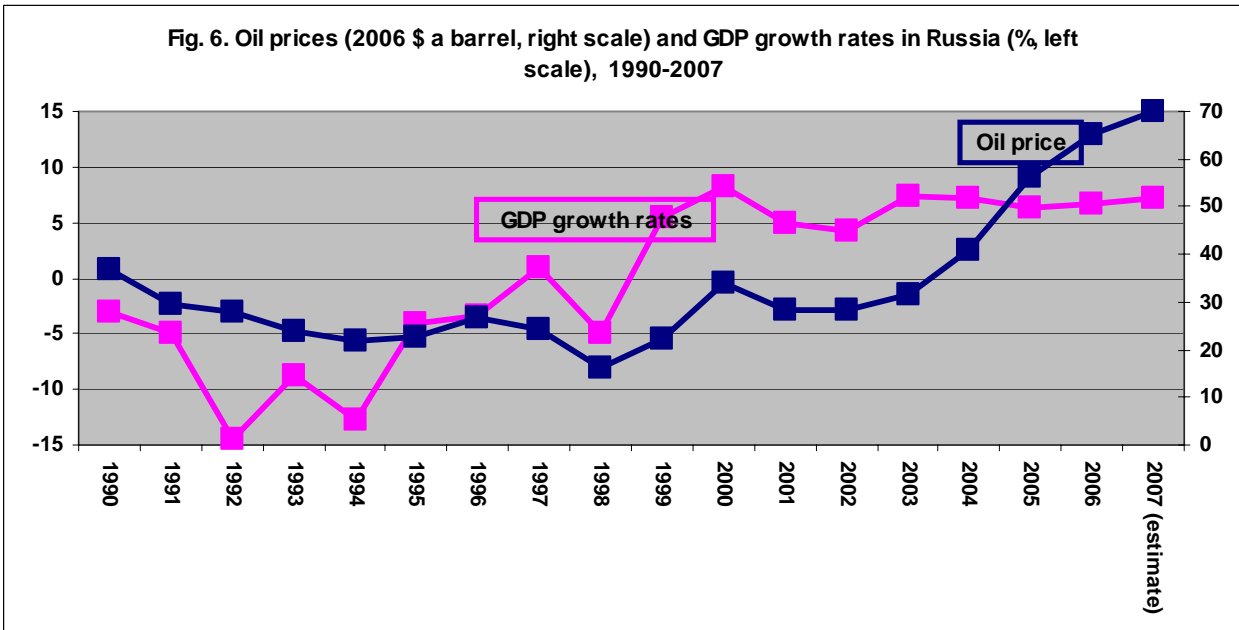
Russian achievements of recent years may be impressive, but unfortunately they are based on weak foundations. The economy is too dependent on oil and gas export that accounts for $\frac{1}{2}$ to $\frac{2}{3}$ (depending on world fuel prices) of total Russian export. And the prosperity of recent years was mostly based on growing world fuel prices. The simple calculation shows the importance of the windfall oil revenues. Russian GDP at the official exchange rate was about \$1 trillion in 2006, whereas the production of oil and gas sector that employs less than 1 million workers is valued at about \$500 billion at world prices of \$80 per barrel of oil. When oil was priced at \$15 a barrel in 1999, Russian oil and gas output was valued at less than \$100 billion. The difference, \$400 billion, is the fuel windfall profit that literally fell on Russia from the skies.

Russia was unable to properly cope with the growing stream of petrodollars. In recent years it developed a typical “Dutch disease” – Russian growth was concentrated in resource industries and non-tradables (services). Increased fuel revenues were mostly used not for investment, but for personal consumption that more than doubled since 1999. Due to the appreciation of the real exchange rate of the ruble (growing ratio of Russian prices to foreign prices) Russian non-fuel industries became non-competitive as compared to foreign goods, so imports in real terms grew faster than anything else in the national economy. As fig. 4 and 5 suggest, the growing trade surplus of recent years is mostly due to constantly increasing fuel prices, whereas the growth of the physical volume of imports (nearly fourfold in real terms in 1999-2006) greatly outpaced the growth of exports in real terms.





Russian growth rates in 1999-2007 were high (7%), but still lower than in other fuel exporters in the former Soviet Union region, like Azerbaijan, Kazakhstan and Turkmenistan (over 10% in 1999-2007). Even some fuel importers, like Armenia and Belarus showed higher growth rates than Russia. In fact, the right question to ask about the recent performance of the Russian economy is why Russian growth rates lagged behind the growth rates of other countries and did not increase in 1999-2007 despite the threefold rise in average annual oil prices (see fig. 6). The answer may be disappointing, but is hardly disputable – Russia did not manage to use its growing resource rent in the best possible way.



If oil prices fall...

It is very likely that with lower oil prices Russia would not be able to maintain the relatively high growth rates of the past several years. Russian economy is often likened to the drug addict who needs larger and larger injections of drugs just to stay out of depression. Even if fuel prices would just stop growing and would stabilize at the current high level, Russian economy would run into a problem of shrinking current account surplus and possible outflow of capital. With currently high foreign exchange reserves consumption could be maintained at the existing level for several years, but production growth rates would start falling unless the economy would undergo a structural adjustment through the devaluation of the ruble and greater emphasis on non-fuel industries.

Both options – slowing down of growth and structural adjustment – would have political implications. Whether Mr. Putin can become Russian Deng Xiaoping – a “grey cardinal” retaining overwhelming control even without formally holding the top post of the president – depends to a large extent on economic prospects, which in turn are linked to the dynamics of fuel prices. If the latter would fall or stop growing, Russian economic situation would worsen and Putin’s successor would face a temptation to put the blame on his predecessor. At the same time, Mr. Putin, on his part, may be willing to distant himself from his “unlucky” successor presiding over the deteriorating economy, in order to have a “clean record” to run in 2012 presidential elections.