Russian economic crisis fuels political tensions

Andrea Peters
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The Russian economy declined dramatically over the course of 2009. According to recently released data from the federal statistics service, the country's gross domestic product (GDP) fell by 7.9 percent.

While this was less than the 8.5 percent predicted by analysts, it was the worst of all the G-20 countries. Among the group of emerging economies known as BRIC (Brazil, Russia, India and China), Russia was the only one to experience negative growth in 2009. The decline in GDP was the sharpest the country has experienced in the last 15 years, outpacing even that of 1998, when the Russian economy defaulted.

Industrial production fell 10.8 percent in 2009, with the automotive and construction industries suffering the most. The number of cars and trucks produced last year dropped to less than half of what it was in 2008. The production of building materials fell by about 40 percent.

The sharp decline in both of these economic sectors is particularly significant because their expansion in previous years was bound up with a growth in consumer spending and the real estate market due to the emergence of a small but significant middle class. The economic position of this social layer, which was never particularly stable, has been undermined by the crisis.

While industrial production started to recover in the second half of last year, the gains have been less than expected and are largely attributable to the fact that the base level had dropped so steeply.

Based on fiscal data showing that the Russian economy returned to growth in the last two quarters of 2009, the Kremlin announced earlier this month that the recession is officially over. The global ratings agency Fitch recently changed the country's status to "stable" from "negative."

However, despite official insistence that the economy has turned the corner, there continue to be concerns about the health of Russian industry.

According to Andre Illarionov, head of the Institute of Economic Analysis, who previously predicted that Russia would quickly pass out of recession, "the boom that began in industry in March of last year, which reached its peak in August, September and October of last year, is rapidly declining."

Interviewed on the radio programme "Svoboda" in late January, Illarionov continued, "In its place will come either fading growth or possibly even stagnation. I do not think that there will be another wave of the crisis, like others are saying. Technically speaking, this cannot happen because the period of growth has gone on already for 6 months. If a new slump occurs…this will be a new crisis."

Private enterprise in Russia continues to be highly indebted. Prior to the onset of the global financial crisis, Russian companies engaged in heavy borrowing on world markets. Government bailouts last year failed to eliminate all of the bad debt on their books.

According to an article published on December 29 in *Nezavisimaia gazeta*, "High corporate debt creates an additional tension in the domestic economy." In 2010, Russian businesses are obligated to repay $200 billion to Western creditors, against anticipated profits of $70 billion.

The downturn of 2009 has also affected the character of economic life in other ways. According to an article published on *Gazeta.ru*, the shadow economy is rapidly growing in Russia, with official estimates placing it at 20-25 percent of GDP. Other analysts maintain that the so-called "unobserved economy" makes up at least 30 percent, and possibly as much as 49 percent, of the country's total economic output.

General economic uncertainty, which fuels businesses' desire to evade taxes, is driving many enterprises out of the official sphere. Thus, even as Russian President Dmitri Medvedev has been insisting that the economic crisis underscores the need to cleanse the country's economy of corruption and make it operate more in line with the rule of law, economic activity is increasingly moving outside the framework of governmental or juridical oversight.

The mood within the general population—62 percent of which described 2009 as the "most difficult" year of the decade, according to an article published in the newspaper *Vedomosti* in late December—has become increasingly dominated by "exhaustion, indifference, fear and bitterness."

The official unemployment rate in Russia now stands at 8.2 percent, an increase of about 2.5 percent from the onset

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of the economic crisis in 2008. Experts believe that the real numbers are higher, with some calculating that as many as 3 million people are out of work. The government's numbers are based on estimates of just over 2 million.

Despite the upturn in the Russian economy in late 2009, which was attributable to a rise in oil prices, the Kremlin recently announced a regime of fiscal austerity. In 2009, the federal government's budget ran an unprecedented deficit of 2.3 trillion rubles ($75.5 billion), or 5.9 percent of GDP. Another deficit is expected for the coming year.

Massive amounts of money were spent by the Kremlin bailing out banks and well-connected oligarchs in 2009. *Bloomberg* estimates the total size of the rescue package at $200 billion. While this yielded little improvement in the economy, with much of the money ending up in offshore accounts or used in currency speculation, it did take a large chunk of out the country's so-called stability fund.

In late January, Finance Minister Alexei Kudrin announced plans for a 10-year freeze on government expenditures, insisting that "excess appetites" accompanying the return of higher oil prices had to be kept in check.

This is a warning to the general population that nothing will be done to alleviate widespread poverty or improve the country's moribund public infrastructure. It appears that the Kremlin's promises over the course of the past few years to improve key areas of social life, in particular health and housing, through a series of "national projects" have remained largely unrealised, or have been implemented with little to no effect. An article published on December 29 in *Nezavisimaia gazeta*, entitled "The Forgotten National Projects," reports that these supposedly multibillion-dollar efforts have done very little to provide "accessible and decent-quality housing" or make much-needed improvements in health care.

Even as news of Russia's economic recovery has received great attention in the media, new data continues to come out about the deplorable state of social conditions in the country. According to a study by the British medical journal *Lancet*, Russia consumes more alcohol per year than any other country in the world, with men in particular suffering high death rates as a result.

The crisis of the past year has destabilised the Russian economy and political system. Even if the country returns to consistent growth in 2010, this will not change the fact that the speed and intensity of the downturn in 2009 exposed a widely known but unspoken truth—the boom years of the Putin era rested on extremely fragile foundations—little more than oil wealth and cheap global credit.

Kudrin's insistence that the return of higher oil prices should not spur "excess appetites" may have also been a warning to sections of Russian big business and the state bureaucracy that they have to exercise some modicum of restraint when feeding at the government's trough lest their actions begin to fundamentally jeopardise the stability of the Russian state.

The economic situation is fueling tensions within the Russian political establishment, as competing sections of the ruling elite draw the lessons of the crisis and utilise the experience to advance an agenda that wrests control of coveted resources and political influence from their rivals.

Most recently, a leading research institute with close ties to Medvedev issued a report advocating major reforms to the country's political system, including the introduction of certain democratic procedures into the election process and an avowedly pro-Western foreign policy. These reforms are generally at odds with the orientation promoted by Prime Minister Vladimir Putin, who was formerly head of state and is widely considered its *de facto* leader still.

The report by the Institute of Contemporary Development follows statements made by Medvedev last year calling for the modernisation of the economy, including the diversification of Russia's industrial base and a shift away from dependence on oil.

While it remains unclear how deep the differences are within the Kremlin or how they will develop in the coming period, the possibility of a split emerging within the Russian elite is being closely watched by the United States and, in some quarters, applauded. Ever since his election, but particularly over the past year, Medvedev has been increasingly presented as a progressive alternative to Putin in the US media. And while efforts to portray the Russian president as a genuine bourgeois liberal with real, if closeted, democratic sympathies are false, it is certainly possible that the US will seek to take advantage of the tensions developing within the Kremlin to try to advance its interests.

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