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Putin's Fourth Term: The Phantom Breakthrough

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Russian President Vladimir Putin promised a "decisive leap forward in development" in his fourth term (2018-2024), claiming that Russia will create a "modern system of effective governance." The prospects of a developmental breakthrough, however, are extremely slim. The economy remains sluggish and the political system is resistant to major institutional reforms. Over the last two decades, Putin has shown no appetite for creating new rules of the game that would rein in arbitrary state power, subject his close acquaintances and friends to fair business competition, or limit his own authority. Late Putinism is incompatible with good governance and highly compatible with economic and political stagnation.

Putin's Promises: The National Projects

Putin set out his fourth term goals in his annual address to parliament in March 2018, a few weeks before his re-election. His starting point was that during his rule the country had overcome many challenges and established stable foundations. This stability provides the necessary basis for the next step, a "decisive breakthrough" to improve the wellbeing of the population. Echoing previous Russian leaders, Putin highlighted "backwardness" as the "main threat" facing the country.

Putin's goals are ambitious. He stated that by 2025 Russia should become one of the world's five largest economies, achieve annual economic growth above the world average, and increase per capita Gross Domestic Product (GDP) by 1.5 times (which suggests a growth rate of around 6 percent per year). He also set out a series of specific goals in other spheres, such as reaching an average life expectancy of 80 years by 2030 (it was 72.5 in 2017) and increasing productivity by 5 percent per year. Other aspirations were stated in more general terms, such as improving the business climate and securing free competition and entrepreneurship.

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These general goals have now been given concrete form as a series of "national projects." These national projects identify twelve priority areas, such as science, demography, health care, education, ecology, and the digital economy. Government plans call for spending nearly $400 billion over six years on the projects.

Putin emphasized the importance of the national projects during his annual call-in show in June 2019, stating the need to restructure the economy and increase productivity in order to improve citizens' wellbeing. He claimed that people should be feeling the effects of the national projects already, including in their incomes. This message was somewhat undercut by his own press secretary, Dmitry Peskov, who admitted the day before the show that most Russians do not understand what the national projects are, and also when one of the call-in show moderators, state television journalist Pavel Zarubin, observed that "many ministers looked so sad" when the government cabinet discussed the national projects.

Prospects for a Breakthrough

Those sad ministerial faces reflect the general mood about the national projects among expert observers. Indeed, reportedly, government analysts already have concluded that most of the goals cannot be achieved, including important ones related to income growth, life expectancy, and poverty levels.

The primary problem is that the Russian economy has been in a rut for a long time. Over the last decade, Russian economic growth has averaged less than 1 percent per year, and less than 0.5 percent per year over the last five years. Both Russian and foreign economists, including the International Monetary Fund (IMF), forecast annual growth through 2024 of less than 2 percent per year. Given that the world economy is expected to grow at 3.5-4 percent per year over the next five years, Putin's goal of a Russian growth rate higher than the global average seems fanciful.

The people who write leadership speeches and government plans understand, at least conceptually, what is needed for Russia to achieve higher growth. These plans discuss the need to increase productivity and investment and, more generally, as Prime Minister Dmitry Medvedev put it, the importance of "institutional and structural modernization." Putin, in his March 2018 speech, referred explicitly to the need to improve the business climate, stimulate entrepreneurship, and decrease the state's role in the economy. He called for legal reforms to protect entrepreneurs and private property.

The problem is that all of these issues have been discussed for the last two decades with no meaningful improvements; arguably, things have only gotten worse. Russian economist Sergey Guriyev, who for the past three years has been the chief economist at the European Bank for Reconstruction and Development (EBRD), detailed the lack of progress in a January 2019 interview with *Vedomosti*. He noted that, with the exception of the stability of the financial markets, Russia had made no progress or had even regressed in such important EBRD indicators as the quality of state and corporate governance, development of competition, and integration into the world economy. Corruption and the poor investment climate, Guriyev remarked, is causing "investors to vote with their feet." He noted that increases in productivity and investment had been a key government goal in 2012 also, but that no progress had been made in either sphere. "The economy," he concluded, "is in exactly the same place it was six years ago, if not worse."

The investment news does indeed seem to have gone from bad to worse. For the years 2015-2018, foreign direct investment in Russia, leaving out reinvested earnings, was only 0.2 percent of GDP, according to a study by the Institute of International Finance. That was the absolute bottom of the Institute's list of 23 core emerging economies—lower than Venezuela, Ukraine, and Nigeria, for example. The February 2019 arrest of prominent American investor Michael Calvey was a stark illustration of the potential dangers of investing in Russia. In May 2019, Morgan Stanley announced that it was pulling out of Russia. The head of their Moscow office for fourteen years painted a dire picture of the investment climate, noting: "In order for a person to invest money in a business, he has to be sure that he won't be killed and his money won't be stolen." Investment risk in Russia, he asserted, "isn't just high, it's prohibitively high."

The poor investment climate is a product not only of domestic factors—weak property rights, corruption, poor rule of law, state domination of the economy—but also international ones. Specifically, U.S. and European sanctions discourage foreign investment in Russia, especially because of the possibility of falling under American secondary sanctions for transacting with sanctioned Russian firms. U.S. congressional proposals for further Russia sanctions would have even more wide-ranging effects. The prospect of more draconian measures, German economist Janis Kluge wrote earlier this year, represents a "sword of Damocles hanging over any business that wants to invest in Russia today."

Given the poor private investment climate, it seems that the only option for the Russian government in trying to fulfill the national projects is to draw on its own resources. State spending on infrastructure and other priorities is set to increase. Low government debt and a budget surplus, as well as accumulating oil profits in the country's National Welfare Fund, do provide a considerable cushion of cash to plow into the projects. However, the influential head of the Central Bank, Elvira Nabiullina, is worried that such a strategy would stimulate inflation, which had been successfully brought down from nearly 13 percent in 2015 to slightly over 4 percent in 2018.

A related concern is that state-led investment will lead to inefficient and wasteful spending, given Russia's high level of corruption and a tendency toward insider dealing in awarding state contracts. Russian Kremlinologists believe that the national projects have become a key battleground over resources between different clans, with the heads of large state-controlled firms (Sergey Chemezov of Rostec, Igor Sechin of Rosneft) or nominally private firms that depend on large state contracts (Gennady Timchenko's Volga Group, Arkady Rotenberg's Stroygazmontazh construction) strengthening their influence in Putin's fourth term.

Same Game, Same Players

Ultimately, Russia's economic problems are not so much economic as political. Indeed, whether Medvedev understands it or not, his call for "institutional modernization" is fundamentally political. Institutional reform involves strengthening property rights, the quality of governance, and the rule of law, which are political steps necessary to create the conditions for attracting investment and increasing productivity. Russia's arbitrary and despotic state is not only the subject but also must be the object of meaningful reforms.

Some Russian officials may believe that technocratic reforms offer the promise of improving the quality of governance without changing the larger political system. The emphasis on a new digital economy in the national projects is consistent with this vision of an apolitical transformation of the Russian bureaucracy and economy to meet 21st century standards. And, to be fair, Russia's eGovernance reforms launched in 2010 led to improved infrastructure and some progress in service delivery, although less than the reformers had hoped. However, as European University at St. Petersburg professor Vladimir Gel'man pointed out in a policy memo last year, the notion that major reforms can be insulated from politics is an illusion, because powerful bureaucratic and economic actors stand ready to block major changes that threaten their interests.

In Putin's Russia, some key interests are very well entrenched indeed. Take, for example, the security and law enforcement organs, which have a significant impact on the legal environment for small and medium-sized businesses. The heads of the Federal Security Service (FSB), the Investigative Committee, and the Security Council have all been in their positions for more than a decade; they also are all long-time Putin associates from St. Petersburg whose careers began in either the KGB or the Soviet police. The head of the national police has been in his position more than seven years and the chief of the prosecutor's office for more than a dozen years. The head of *Rosgvardiya*, the national guard created in 2016, is led by Putin's former chief bodyguard, who also hails from St. Petersburg. Last year he challenged Russian opposition politician Aleksey Navalny to a duel, threatening to pound him into mincemeat, because of Navalny's reporting on corruption in his agency.

Similar stasis is evident at the top of Russia's largest companies, many of them state-controlled. This includes top energy firms Gazprom, Rosneft, and Transneft, the state military-industrial conglomerate Rostec, and the largest state bank, Sberbank, all headed for many years by Putin's long-time associates from either St. Petersburg or the KGB. Key economic actors that are "cronies" of Putin, such as Chemezov, Yuriy Kovalchuk

(National Media Group), and Rotenberg, are playing an increasing role in sustaining informal relations between Putin and both state officials and big business. They also are seeking to further increase their influence as part of the new national projects.

Given the longevity of many of the top political and economic players in Moscow, starting of course with Putin himself, the latest set of grand speeches and ambitious policy documents are like déjà vu all over again. There is little reason to think that Putin, whose penchant for state control and what he once called "manual steering" is long-standing, will suddenly take the hard steps to create modern economic and political institutions. Fighting corruption, solidifying the rule of law, protecting property rights—all of these reforms generally require a more open political system in which other branches of power and non-state actors (the media, civil society, political parties) are significantly more empowered relative to the executive than they are in today's Russia. The fight for political influence and economic gain will continue to be a closed game of special deals played by insider networks, rather than one based on transparent rules of the game for all actors. And that means no decisive breakthrough to rapid development and modern public administration will take place.

There are two final reasons for skepticism about the likelihood of a decisive leap forward. First, the confrontation with the West works against modernization. Russia has sought to protect itself from sanctions' effects through a partial withdrawal from international trade and financial markets. "The Kremlin," observed Janis Kluge at the German Institute for International and Security Affairs, "has sacrificed future economic development for sanctions resilience today." Long-time Putin ally and Accounts Chamber head Aleksey Kudrin has argued that Russia needs rapprochement with the West and greater integration into the world economy to make higher economic growth possible, but "systemic liberals" like Kudrin have little influence on broader political issues, and certainly not on matters of foreign policy.

Second, ultimately, the Kremlin's top priority this term is not domestic modernization and institutional reform. In addition to foreign and security policy, which Putin finds considerably more interesting than reforming education or health care, he has to figure out some kind of solution to the "2024 problem." Constitutional term limits prevent the president from being re-elected in 2024. Insiders have already begun to maneuver for influence on the decision about how to keep Putin in power or, if he decides to step aside, who will be his designated successor. The outcome of this battle matters much more to leading elites than the national projects.

Return to Stagnation

Russians conventionally refer to the period of Soviet history from the late-1960s to the mid-1980s as the era of stagnation: economic growth faltered, the political leadership became sclerotic, and social disaffection slowly spread. It is no surprise that the current period is being compared to that previous era. Putin already has served longer than Leonid Brezhnev's eighteen years, and the past decade of 1 percent annual economic growth is worse than the 2 percent per year recorded by the Soviet Union from 1976-1985. The recent wager on digitalization to drive economic modernization, without fundamental change to the underlying institutions, is reminiscent of the Brezhnev leadership's hope that the so-called "scientific-technological revolution" would transform the country, even though signs of serious problems in the Soviet developmental model were increasingly evident.

Columbia University professor Seweryn Bialer in 1986 highlighted the paradox evident in the Soviet Union's growing global footprint, from Afghanistan to southern Africa, at a time of domestic stagnation, using the phrase "external expansion, internal decline." This also seems an apt descriptor of late Putinism, which combines an ambitious foreign policy with domestic degeneration. A crucial issue for Putin's fourth term is whether the likely failure of an economic and governance breakthrough, combined with Putin's lame-duck status in the run up to 2024, will lead not just to economic stagnation but political breakdown. As his ratings dip and popular demand for change increases, which are evident both from public opinion polls and growing protests over the last year, Putin's fourth term is shaping up to be his most difficult yet.