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POLITICAL RISK & STRATEGY

SMOKE AND MIRRORS: WHY A HIGH-PROFILE NEW APPOINTMENT IN RUSSIA DOES NOT HERALD REFORM

By Christopher Peters

At the end of April Russian president Vladimir Putin announced that he had appointed former finance minister Alexei Kudrin, a respected reformist, as deputy head of the President's Economic Council. At the same time Kudrin became chair of the Center for Strategic Research, a think tank closely affiliated with the Kremlin, and among his primary tasks will be drafting a strategy for the country's development after 2018 (a strong indication that Putin intends to run for a fourth term). But his appointment should not be taken as a sign that Putin is leaning towards the modernizers or that Russia is entering a period of liberal reform, and investors should remain circumspect in their dealings with the country.

KUDRIN'S LEGACY OF MODERNIZATION, 2000-2011

Kudrin was a finance minister and deputy prime minister from 2000 to 2011, known for prudent fiscal management and creating a more hospitable environment for private business and foreign investors in Russia. Under his leadership, the Stabilization Fund of the Russian Federation was established to invest surplus income from oil-and-gas exports while oil prices were high. He resisted strong pressure from inside and outside the government to put this money to other uses, and the fund, which during his tenure peaked at over US\$600 billion, is widely credited with helping Russia survive not just the global financial crisis but also the more recent low-oil-price period and the sanctions leveled against Russia for its policies toward Ukraine.

In September 2011, Kudrin was fired by then-President Dmitri Medvedev for insubordination, but his influence helped key figures retain their hold on the levers of national economic policy, including Elvira Nabiullina (minister for economic development, and later head of the Central Bank); Igor Shuvalov (deputy prime minister responsible for the federal budget and economic policy); and German Gref (CEO of the state savings bank Sberbank).

Since leaving office, Kudrin has taken positions in academia and think tanks, and has consistently shown a rare independence of mind: he has criticized the isolationist path taken by Russia since 2014, acknowledged the damage done to Russia's economy and standing by the Yukos affair, and spoken of the need for root-and-branch reform of powerful state bodies, such as the police. At the same time, he has never criticized Putin directly, and Putin is known to hold him in high regard.

NEW ROLE, LIMITED SIGNIFICANCE

The general public, heavily influenced by government propaganda, has accepted that Russia is set to go through difficult times to meet the perceived “aggressive” economic and political challenges from “the West.” But Russians are unlikely to back wholesale liberal reform: in the public mind, such reform is associated with the turbulent 1990s, with the decimation of pensions and savings, a near-breakdown in public order, and the rise of a much-resented super-wealthy class. Putin knows that any perception that he would risk a return to those times would ruin him, and his third term, since returning to the presidency in 2012, has been defined by appealing instead to nationalist and statist instincts.

A DELICATE BALANCE

Historically there have been two main factions within Russia’s ruling elite: those who favor modernization, reform, and close cooperation with the West, and those who favor statism, take a conservative and nationalist view of society, and believe that Russia must remain independent of, or even opposed to, the West. Putin’s government is no exception, but as with previous Russian leaders, he has found it necessary to balance the two factions, and works hard to ensure that appointees to state ministries and corporations satisfy both camps. However, he has leaned toward the conservatives since the start of his third term, in 2012, and Kudrin’s elevation should be viewed accordingly.

Shortly before Kudrin’s appointment, there was a re-ordering of Russia’s security agencies that greatly favored conservatives, many of whom come from the military and security services. A new agency, the National Guard of Russia, has been placed under the command of Viktor Zolotov, a long-serving head of presidential security, and the National Guard will be drawn almost entirely from the Interior Ministry. These forces, numbering nearly 400,000, will comprise an armed structure separate from the country’s Armed Forces, and under Zolotov, will answer directly to the presidency. They include the feared OMON (riot police) as well as other agencies that can wield physical and even lethal force. The structure also more closely fits the “power vertical” that Putin believes is best suited to running the Russian state, a view strongly shared by many conservatives.

This development also reveals the limits of Kudrin’s influence: while out of government, Kudrin authored a detailed analysis of the Russian police force, an institution universally viewed as deeply corrupt and ineffective, and made proposals for its reform. The new National Guard is the exact opposite of what Kudrin had proposed.

CAUSE FOR CAUTION

Kudrin has repeatedly made it clear that he will not work with or for Prime Minister Dmitri Medvedev, and it is rumored that he covets Medvedev’s job. Putin himself is said to have seriously entertained this idea, in part because a Kudrin premiership would indeed benefit both private business and foreign investors in Russia: he has the force of personality and, more importantly, Putin’s backing to create conditions for both to flourish.

However, Russia is heading into parliamentary and presidential elections (September 2016 and March 2018, respectively), and while there is some likelihood that the unpopular Medvedev will eventually be



sacrificed, his immediate replacement would almost certainly hail from the conservative camp, as this would be more in tune with the public mood – important at election time. After the 2018 elections, meanwhile, Putin will feel less constrained by public opinion, looking instead to his legacy, and a Kudrin premiership may become more likely at that time.

But in the short to medium term, while Nabiullina, Shuvalov, and other reformists maintain sufficient influence to prevent imprudent economic policies, the trend of isolationism and antagonism toward the West will continue, and the systemic reforms needed to encourage private enterprise and the return of foreign investors will not be countenanced.

And, because Russia and its economy will continue to be anchored more to the president than to institutions, and the rule of law will remain fluid, foreign investors would be wise to approach any dealings in the country with caution.