



RUSSIA in GLOBAL AFFAIRS

Vol. 5 · No. 1 · JANUARY – MARCH · 2007

Contents

On the Eve of Change *Fyodor Lukyanov* 5

The Hydrocarbon Challenge

The Evolution of the Global Energy Market 8

The main task facing Russia in the next decade will be to provide conditions to minimize expected losses, first, from its declining presence on world oil and gas markets, and second, from falling world energy prices.

Are the Energy Majors in Decline? *Vladimir Feygin* 25

The Shtokman project may be a forerunner of critical changes in the global energy sector. The older-generation majors are heading for very tough competition. The governments of the resource-rich countries, and national companies enjoying governmental support are interested in reducing the role of transnational corporations to that of ordinary contractors.

Energy Partnership – A Dialog in Different Languages
Tatyana Romanova 32

The difference in approaches and the need to search for a compromise between diametric views de facto predetermines the structure of any future agreement between Russia and the EU. This can only be a general strategic partnership agreement and a number of sector-specific agreements, which will be used as a platform for a complex compromise between two visions.

Global Agenda

- Security Services, Police, and Human Rights *Valery Zorkin* 48
States should take inventory of the laws that regulate the limitations on human rights in the course of implementation of security measures. Most importantly, they should ensure various controls over security services and police by parliamentary and governmental bodies.
- Self-Determination: Between Law and Politics *Alexander Aksenyonok* 55
Can Kosovo's imminent independence be seen as a precedent in resolving other internal state conflicts, including in the former Soviet republics? This problem has gone from being a subject of academic dispute to an explosive element of Realpolitik.
- East Asia and Russia's Development Strategy 70
Although Russia has stepped up its military and political presence in East Asia, it has not yet gained the required levers of influence in the region. It fails to take into account the geopolitical changes there, while it views the changing situation in a simplified, outdated way: through the prism of its rivalry with the United States.
- The 21st Century Mafia: Made in China *Vladimir Ovchinsky* 84
As China continues to consolidate its leading positions in the global economy, Chinese organized crime is expected to broaden its presence in global criminal links. This is of tremendous concern for Russia and the world.

Russia on the Rise

- Strengths and Weaknesses of the Russian Economy *Vladimir Mau* 98
Russia entered its postindustrial transformation much later than the West. In fact, we must choose an effective model of a postindustrial market and produce a set of state policy instruments that will ensure its proper functioning.
- Russia Against the Background of Major Economies *Valentin Kudrov* 117
In the long term, Russia will inevitably be a strong state economically and will rank first in Europe and fifth or sixth in the world in terms of GDP. But the situation is different from the political, social or civilizational points of view: unless Russia makes a final choice in favor of globalization and Europeanization, anything can happen to this country.
- A Development Strategy for Russia's Largest Cities *Olga Vendina* 129
Proponents of globalization believe that Russia's largest cities must follow in the footsteps of the 'global cities' and compete for command positions in the global economy, using the geopolitical and geo-economic advantages of their Eurasian location and Soviet-era heritage. This does not seem very realistic.

Around Russia

- Europe as the “Center,” and Its “Outskirts” 148
Vladislav Inozemtsev
Europe is gradually turning into a kind of a community of personalities, whereas the United States and Russia are consolidating a society of citizens (or even subjects). The cohesiveness of the Europeans is built on natural social solidarity, whereas the cohesiveness of the Russians and Americans is based on extolling their not entirely indisputable values, as well as on the mobilization of efforts to attain some equally dubious goals.
- An Audit of Russia’s Foreign Policy *Ivan Safranchuk* 167
A country seeking to return to the global stage as a major actor must find a well-planned solution to the problem of providing its foreign policy with sufficient resources. The volatility of foreign policy spending reveals the main problem: political decisions in Russia are poorly translated into budgetary categories and specific plans with a particular price tag.
- Historical Struggle for the Black Sea Fleet *Yuri Dubinin* 177
Some forces in Kiev, under various pretexts, are again calling into question the agreement that settled the fleet conflict between Russia and Ukraine. It would be helpful to recollect exactly how the unprecedented diplomatic marathon, which was full of dramatic twists and turns, helped to untie one of the most complicated knots between the two states.
- Russia Must Regain the Initiative in Moldova *Zurab Todua* 196
Russia’s position in the Transdnestr settlement, which can be described as “defense on the Dniestr,” has no chances for success, as political resources for preserving the status quo are limited. Preservation of the status quo, sought only by Tiraspol and to some extent by Moscow, is against the plans of all the other interested parties.



BOARD OF TRUSTEES

Vladimir POTANIN
(Chairman)
Interros Holding Company

Sergei GENERALOV
*Association for the Protection
of Investors' Rights*

Andrei KUZUYAEV
LUKoil Overseas Holding Ltd.

Boris KUZUYK
*New Concepts and Programs
Holding Industrial Company*

Valery OKULOV
Aeroflot JSC

Ruben VARDANYAN
Troika-Dialog Group

Simon VAYNSHTOK
Transneft JSC

Victor VEKSELBERG
SUAL-Holding

Vladimir YEVTUSHENKOV
Sistema JSFC

PUBLISHED BY
FOREIGN POLICY RESEARCH
FOUNDATION

RUSSIAN EDITION
IS PUBLISHED
WITH PARTICIPATION OF



FOREIGN AFFAIRS

Editorial Office:
11 Mokhovaya St., Bldg. 3B,
Moscow 103873, Russia
tel.: +7 (495) 980-7353
fax: +7 (495) 937-7611
e-mail: info@globalaffairs.ru
<http://www.globalaffairs.ru>

Registered with
THE MINISTRY
OF THE RUSSIAN FEDERATION
FOR PRESS, TV AND RADIO
BROADCASTING AND MEANS
OF MASS COMMUNICATION
PI No. 77-12900
3 June 2002

Printed by
Kaluzhskaya Tipografia Standartov
Order No. 86
Circulation: 3,000 copies

EDITORIAL BOARD

Sergei KARAGANOV, *Chairman*

Martti AHTISAARI
(Finland)

Graham ALLISON (U.S.A.)

Alexei ARBATOV

Lev BELOUSOV
(Deputy Chairman)

C. Fred BERGSTEN (U.S.A.)

Carl BILDT
(Sweden)

Vladimir GRIGORYEV
(in a personal capacity)

James HOGUE (U.S.A.)

Igor IVANOV
(in a personal capacity)

Karl KAISER (Germany)

Irina KHAKAMADA

Helmut KOHL (Germany)

Andrei KOKOSHIN

Mikhail KOMISSAR

Vyacheslav KOPIEV

Mikhail KOZHOKIN

Yaroslav KUZMINOV

Sergei LAVROV
(in a personal capacity)

Alexander LIVSHITS

Vladimir LUKIN

Fyodor LUKYANOV
(Editor-in-Chief)

Vladimir MAU

Thierry de MONTBRIAL
(France)

Vyacheslav NIKONOV
(Deputy Chairman)

Vladimir OVCHINSKY

Vladimir POZNER

Sergei PRIKHODKO
(in a personal capacity)

Yevgeny PRIMAKOV

Vladimir RYZHKOV

Horst TELTSCHIK
(Germany)

Anatoly TORKUNOV

Lord William WALLACE
(Great Britain)

Sergei YASTRZHEMSKY
(in a personal capacity)

Igor YURGENS

Alexander ZHUKOV

Sergei ZVEREV

BOARD OF ADVISORS

Anatoly ADAMISHIN

Olga BUTORINA

Vladimir ENTIN

Leonid GRIGORIEV

Alexander LOMANOV

Georgy MIRSKY

Mark SHKUNDIN

Anatoly VISHNEVSKY

INFORMATIONAL PARTNERS

- Newspapers: *Izvestia*, *Moscow News*, *Rossiyskaya Gazeta*, *Sovershenno Sekretno*, *Trud*, *Vremya Novostey*
- News Agencies: *Interfax*, *RIA Novosti*, *Rosbalt*
- Radio Station *Echo of Moscow*

LEGAL
CONSULTANCY

KLISHIN & PARTNERS
Attorneys at Law

PR PARTNER

KROS Public Relations
Company

Editor-in-Chief Fyodor Lukyanov

Deputies Editor-in-Chief Natalya Kostromskaya, Timofei Bordachev

Director Executive
Irina Palekhova

Copy Editors
Robert Bridge
Rinat Yakubov

Proof-Reader
Lyudmila Kupchenko

Assistant to Editor-in-Chief
Yelena Nikitina

Web Editor
Pavel Zhitnyuk
pavel@globalaffairs.ru

*Assistant to Chairman
of the Editorial Board*
Yelena Blinnikova

Computer Makeup
Natalia Zablotskite

Design and Layout
Konstantin Radchenko

Circulation
Andrei Yevdokimov
tel.: 7 (495) 937-7611
op@globalaffairs.ru

Russian Edition

Copy Editors
Alexander Kuzyakov
Lyubov Ryklina

Proof-Reader
Arnold Kun

Photos contributed
by Fotobank Agency

The views of the authors do not necessarily coincide with the opinions of the Editors.
The responsibility for the authenticity and accuracy of the facts in the published articles rests with the authors.

© FOREIGN POLICY RESEARCH FOUNDATION 2007

All rights reserved. Reproduction in part or whole is allowed only with the explicit authorization of the publisher.

On the Eve of Change

Fyodor Lukyanov, Editor-in-Chief

Russia is entering a momentous election season. In December, Russian voters will elect a new parliament, while in March 2008 they will vote for a new president. Thus, the prospects for changes will be a prominent subject in our journal throughout the year, especially since the change of power in Russia traditionally has an impact on all spheres of politics, including in the realm of foreign policy. Experts differ in their forecasts about the future, yet they agree that the next presidential term will be particularly important. Russia's transitional period is coming to an end, and the country will have to choose a long-term strategy for its development.

What will the global conditions be like during the next decade for Russia's development? One group of experts, who participated in a study entitled, *The World Around Russia: 2017*, presented a comprehensive picture of the shape of the future. The study marked 15 years since the

establishment of the Council on Foreign and Defense Policy, the most representative and influential non-governmental organization in Russia in this sphere. The study will be presented in full at the Council's anniversary assembly in March and will later be published on our journal's web site.

This issue carries two sections from this study that are devoted to subjects of particular importance to Russia: the **prospects of East Asia**, a neighboring region that plays an increasing role in Russia's policy and economy, as well as a **forecast on global energy development** and Russia's role in it.

Energy problems are also the focus of two more articles in this issue.

Vladimir Feygin comments on Gazprom's decision not to set up an international consortium for developing the rich Shtokman gas field. He views this decision as a manifestation of a new global tendency.

Tatyana Romanova analyzes why Russia and the European Union fail

to achieve mutual understanding in the energy sphere.

Vladislav Inozemtsev offers an unorthodox view on relations with Europe: he argues that Russia and the United States are very much alike, as both are nothing more than the “outskirts” of the European “center.”

Ivan Safranchuk makes an attempt to determine the real priorities of Russia’s foreign policy by analyzing the budget allocations to this governmental sector. Some of his conclusions are rather unexpected. For example, Moscow’s policy toward the Commonwealth of Independent States is not an overwhelming priority, he argues, as it is officially stated. Several other articles focus on Russia’s relations with its neighbors. Russian veteran diplomat **Yuri Dubinin** offers his reminiscences about the difficult negotiations with Ukraine over the status of the Black Sea Fleet.

Zurab Todua weighs Russia’s chances of restoring normal relations with Moldova. **Alexander Aksenyonok** discusses a hot topic: Will the future status of Kosovo become a precedent for solving the problem of breakaway territories in

Georgia? **Vladimir Ovchinsky** writes about the activities of the “Chinese mafia” in Russia.

Russia’s ongoing economic development is a perennial topic for our contributors. **Vladimir Mau** analyzes various modernization experiences across the world and proposes models for Russia’s economic strategy.

Valentin Kudrov argues that if Russia continues with market reforms, it will have an opportunity to gain leading global positions in the next few decades. **Olga Vendina** discusses various scenarios for the development of major Russian cities, which are set to become epicenters of economic growth.

Finally, the Chairman of Russia’s Constitutional Court, **Valery Zorkin**, broaches a difficult international subject: how to ensure the observance of human rights amidst the global counterterrorism struggle and the broadened powers of the security services?

In our next issue, we will return to our primary topic: the role and place of Russia in the system of influential international institutions – the G8, the European Union, NATO, and the Shanghai Cooperation Organization.

The Hydrocarbon Challenge



“Despite its leading positions in the production and shipment of hydrocarbons, Russia lags noticeably behind in the implementation of advanced technologies. The country’s leadership puts the main emphasis on oil, natural gas and coal as the principal instruments that allow Russia to attain and retain the status of a great energy power. Meanwhile, the world’s changing energy structure will by 2030-50 substantially reduce Russia’s competitiveness.”

The Evolution of the Global Energy Market

8

Are the Energy Majors in Decline? *Vladimir Feygin*

25

Energy Partnership – A Dialog in Different Languages

Tatyana Romanova

32

The Evolution of the Global Energy Market

The global energy market is going through large-scale changes, some of which may reach their final phase by 2017. There are increasing signs that the traditional code of relations between energy producers and consumers, established in the last quarter of the 20th century, is becoming a thing of history. Mechanisms for regulating the global energy market no longer work. Competition between consumers, fueled by the emergence of new powerful players, like China and India, is obviously increasing.

Oil fields that are situated close to the developed countries, where oil price-hikes in the 1970s-1980s prompted oil production, are now near exhaustion. Today, large-scale investment is required in new oil-bearing areas in West Africa, Central Asia, the Caspian region and Russia in order to replace depleting oil fields. A new energy reality is taking shape in the world.

This material was prepared as part of the project *The World Around Russia: 2017*. The project is being implemented by a group of experts, headed by Sergei Karaganov, from the Council on Foreign and Defense Policy, the Department of International Economics and International Politics of the Higher School of Economics, the Institute of Strategic Studies and Analysis (ISSA), the Institute of Europe and other organizations, with the support of Rio-Center. The main authors of this material are **Vagif Guseinov**, ISSA Director; **Alexei Denisov**, ISSA Deputy Director; and **Alexander Goncharenko**, expert with the Socio-Economic Information Bureau.

GENERAL SITUATION

The world's key energy players include:

- The United States – the world's largest oil consumer (24.6%). It imports more than one half of the oil that it consumes. The United States is also the world's leading importer of natural gas (16% of global imports);

- The Middle East accounts for 61% of global oil and 40.1% of natural gas reserves, which makes it a crucial regional factor in the energy strategies of the world's largest consumers;

- The largest oil producers in the Middle East are Saudi Arabia (22% of global proven oil reserves, 13.5% of global oil output), Iran (14.9% of proven natural gas reserves, 11.5 of proven oil reserves), Iraq (9.6% of proven oil reserves), and Qatar (14.3% of proven natural gas reserves);

- Russia possesses 26.6% of global natural gas reserves, 6.2% to 13% (according to different estimates) of global proven oil reserves, and about 20% of known coal reserves. The country is the world's leading pipeline gas supplier and the world's No. 1 oil exporter (together with Saudi Arabia). More than 90% of Russian energy exports today go to European countries;

- China, the world's fastest growing energy consumer, accounts for 31% of global oil consumption growth in 2004. In the past 40 years, oil consumption in China has grown more than 25 times over and is now at 8.55% of global consumption;

- The EU, which accounts for only 3.5% of global proven gas and less than 2% of proven oil reserves (mostly in Norway and the UK). At the same time, oil and gas deposits in Europe are exploited far more intensively than in other parts of the world, which leads to the rapid depletion of reserves. Western Europe consumes 22% of the world's oil supplies, while Germany is the world's second largest gas importer (14%). The main problem for the EU is its growing dependence on energy imports: by 2030, oil imports to the EU will grow from 76% to 90%, gas imports from 40% to 70%, and coal imports from 50% to over 70%.

Today, the situation on the global energy market is characterized by the following factors:

- oil is a global source of energy, and natural gas is primarily a regional source, while coal is a local source of energy;
- while consumption of hydrocarbons is growing rapidly, there will not be alternative energy sources in the foreseeable future;
- a rapidly rising need for energy resources in the emerging Asian economies amidst their ongoing economic development, rapid population growth, and the extremely high energy usage of national economies;
- the widening gap between the volume of hydrocarbon consumption (growth) and production (decline) in developed countries;
- limited production growth opportunities increase market destabilization risks;
- the global economy is experiencing a shortage of oil and natural gas;
- a shortage (temporary) of oil refining and transport facilities, together with a lack of additional oil production capacities;
- large industrial consumers are showing a marked interest in alternative energy sources;
- the growing importance of liquefied natural gas production and delivery projects;
- interest in nuclear energy is reviving in some countries;
- in the past few years mergers have been occurring exclusively within the limits of one country or a common geopolitical space as assets available for mergers and acquisitions are decreasing; and
- growing political risks in hydrocarbons-rich regions.¹

The global energy situation is marked by a deepening of contradictions that will remain throughout the period under review.

The conflict potential inherent in the distribution of oil resources in the world is the primary cause of geopolitical tensions. While the main consumers of oil are highly developed coun-

¹The growth of prices for hydrocarbons has shown consistency since 2000, when a new Arab-Israeli conflict broke out. Since then, periods of high oil prices have always echoed increases in tensions in this region: the U.S. intervention of Iraq, the worsening of the situation involving Iran's nuclear program, the thirty-day war in Lebanon, etc.

tries or emerging giants, the bulk of global hydrocarbon reserves is concentrated in a relatively small group of developing countries or transitional economies. This contradiction is a basic factor in the behavior of key market players. Such large consumers as the U.S., the EU and China are concentrating both economic and political resources on expanding on the same market, which leads to competition between them. The fact that the majority of resource-rich countries are politically unstable sets the stage for future upheavals on the world energy market, while opening some opportunities for Russian expansion.

The world's main hydrocarbon resources are controlled by national state companies. Meanwhile, downstream capacities, logistic and transport schemes, as well as distribution of hydrocarbons, are under the control of multinational corporations. This accounts for the differences in market players' behavior. Large multinationals are striving to strengthen their resource base while state controlled companies, which have the main resources, are striving to expand downstream operations and obtain an equity share in transport and sales structures. This contradiction is a growing trend that will likely continue in the next decade.

There are fewer regions today where hydrocarbon production can be raised sharply without the use of modern technology or production methods that demand many billions of dollars in infrastructure investment. As a result, there are fewer opportunities for maneuver by key consumers on the market, especially after 2013-17. Geostrategic confrontation is developing mainly between China and the United States, and by 2030, China will be importing as much oil as the U.S. At the same time the Chinese leadership is very well aware that further economic growth will be impossible without securing reliable energy sources. This is why energy security and the search for new markets is becoming a matter of survival for one of the world economic leaders. For its part, the U.S. is not interested in China strengthening its positions on the hydrocarbons market and is ready to use political and economic leverage to keep Chinese oil and gas companies off these markets.

MAIN VECTORS OF DEVELOPMENT
IN 2007-2017

The main trends in the global energy sphere will generally continue in the next decade. The share of fossil energy resources (oil, natural gas and coal) will remain at the 2003-05 level, i.e., about 80% of the aggregate consumption of primary energy sources. Until 2017, oil will be by far the most important source of energy in the world (interest in oil may only be expected to decline starting in 2030).

Within the next decade, oil will remain the leading source of energy, accounting for approximately 40% of energy consumption, followed by natural gas (28%), coal (20%), renewable sources of energy (7%), and nuclear energy (5%). The share of natural gas and oil will continue to increase whereas the share of coal and nuclear energy will decline. Possibly, by the end of the decade, the share of nuclear energy will stabilize and alternative energy sources will start to increase, but their growth will not affect global trends for at least the next 15-25 years.

In the longer term (by 2067), the world energy balance structure may change according to two basic scenarios. The first one sees a gradual shift from oil to natural gas, similar to the way coal was earlier replaced by oil. This will be followed by a shift toward renewable sources of energy and possibly to nuclear energy. At the same time, oil will retain its positions as an important energy source at least until the mid-21st century. In the second scenario, if considerable progress is made in hydrogen technology within the next decade and hydrogen fuel cells start replacing gasoline-powered engines, oil production will begin to decline much earlier, perhaps some time around 2025, but thus far this scenario seems unlikely.

While the huge energy demand of the global economy will gradually decline (mostly in developed countries), the dependence between GDP growth and energy consumption will remain. The continuing growth of the global economy will drive energy demand for some time yet, but energy consumption growth is slowing, and falling increasingly behind GDP growth. This means that world economies are beginning to adapt to the use of alternative and renewable energy sources. The share of energy in the GDP of

Western powers will continue to fall. This makes it impossible to rely on energy sources as the foundation of national economic development even in the medium term (particularly for Russia).

In the next decade, energy consumption will grow the most rapidly in 2006-12, on average 1.6-2% a year, after which growth will begin to slow, but the main trends in the energy sector will generally remain. On the regional level, energy consumption growth will be the largest in the Asia-Pacific region. Attempts by China and India to solve their energy security problems with internal resources will most likely prove unsuccessful. Oil, natural gas, and coal consumption in the developing countries will exceed that in the industrialized nations.

Global oil consumption growth will be driven mainly by increasing consumption in the Asia-Pacific region (on average 2.8% a year), primarily in China (4.5%) and India (3.5%), as well as in North America (1.4%), Latin America (2.6%) and the Middle East (2.1%).

In the next decade, natural gas consumption will increase the most rapidly around the Pacific Rim (on average 3.6% a year), Central and South America (3.2%), the Middle East (3.1%) and in Africa (4.1%). Natural gas consumption will grow as natural gas (including LNG) transportation and utilization technology systems become cheaper and more advanced. Gas supplies will increase as a number of major production projects are implemented in a number of countries, including Russia (Yamal Peninsula, East Siberia, the Far East, the Kara Sea shelf), Iran, Qatar (North and South Pars), Saudi Arabia, the United Arab Emirates, Kuwait, Algeria, Libya, Azerbaijan, Kazakhstan, Turkmenistan (Caspian Sea shelf), and other countries.

Due to an expected drop in oil production, industrialized states may substantially increase the volume of their oil imports, primarily from politically and economically unstable countries in the Persian Gulf. In general, this scenario makes diversification of oil supply a pressing problem. Hence the interest that major energy consumer nations and international corporations take in the energy resources of non-OPEC countries, including Russia and other post-Soviet countries.

Growing hydrocarbon consumption in the world will further aggravate the basic contradictions within the global fuel and energy

system. In the future, energy markets will be affected by coordinated terrorist attacks against elements of the oil infrastructure, most likely in Iraq, Iran, Saudi Arabia, Latin America, and African countries, with resulting disruptions in deliveries. Growing hydrocarbon consumption in the world will substantially increase political risks and could cause new regional conflicts. At the same time, oil crises, like those in the 1970s-80s, are unlikely to appear in the next decade.

China will likely do its utmost to strengthen its influence and economic presence in the Middle East, Africa, Latin America and Central Asia. The United States will remain China's main competitor with respect to geographic expansion. It cannot be ruled out that China will form temporary alliances with India and possibly with Russia in order to expand its presence in the global energy system.

The main source of production growth in Latin America will be around Brazil's deep-water shelf. U.S. corporations will apparently develop this region in order to lessen U.S. dependence on suppliers from the Middle East with Brazilian hydrocarbons. At the same time, the formation of the Chavez-supported Venezuela-Cuba-Bolivia union could attract other Latin American countries. Thus, high oil prices may cause substantial amounts of South American oil to be re-routed from North America to Asia Pacific. Chavez will most likely retain his position or transfer power to a successor. At the same time, faced with the danger of the complete termination of oil supplies or the formation of a political opposition in Latin America, the United States could take more decisive measures with a view to changing the political regime in Venezuela.

The share of energy sources in the Black Continent in the global energy system is expected to grow considerably. Energy production in the region should be expected to peak by 2020, and then gradually decline. Apart from the existing production projects in North and West Africa (Nigeria, Algeria, Egypt, and Libya), international energy companies will begin to actively invest in geological prospecting and production in East and Southeast Africa (Sudan, Tanzania, and Angola). Oil production should also grow in Chad, Congo, and Equatorial Guinea. Priority will be given to shelf projects. Angola, where deep-water deposits discovered in recent

years will reach full capacity, will become the growth leader in Africa. The main competitors in African oil and natural gas projects are the United States and China. The U.S. was the first country to start working in this area, but China is now rapidly expanding its presence in Africa. From every indication, the U.S. will strive to use its political leverage in the majority of African countries to impede Chinese entry into the African fuel and energy complex.

In the Caspian region, oil production will continue to steadily rise. Until 2015, the regional leader will be Azerbaijan, where oil will be produced at the Azeri-Chirag-Gyuneshli fields, while natural gas will be produced at the Shakh-Deniz field. After 2015, the main oil field will be the Kashagan deposits in Kazakhstan. As for natural gas, by 2017 the main suppliers will still be Turkmenistan and Kazakhstan, while Azerbaijan's shares will fall.

The geopolitical lineup in the Caspian region is generally developing in favor of the West. The Baku-Tbilisi-Ceyhan (BTC) oil pipeline bypasses Russia and Turkish straits; the Baku-Tbilisi-Erzurum (BTE) natural gas pipeline will be put into operation in 2007. Before 2015, a gas pipeline will likely be built from Turkey (subsequently transporting Iranian, Kazakh and Turkmen gas) to Europe (Nabucco project). In this context, the U.S. and the EU will intensify their pressure on Turkmenistan to re-route the gas flow to this pipeline project. At the same time, Kazakhstan and Turkmenistan will implement pipeline projects to carry oil and natural gas to China. Russia's influence in the Caspian region will be minimized. Russia's positions will most likely remain at their present level – as a transit country for small volumes of Caspian oil along the Caspian Pipeline Project (CPC). Oil shipments along the Baku-Novorossiisk pipeline will likely stop flowing once the Baku-Tbilisi-Ceyhan oil pipeline reaches full capacity.

The Broader Middle East will generally remain under U.S. strategic control. In terms of energy security, Saudi Arabia will remain the main energy source until 2017. By 2010, it will put new production capacities into operation. As a result, Saudi Arabia's share of the world oil market will remain unchanged, despite the fact that substantial U.S., Chinese, EU, and Japanese resources will

be spent to reduce dependence on Middle East oil. The majority of countries in the region will largely continue the policy of maneuvering between the principal consumers – the U.S. and China.

With continuing military-political instability in the Broader Middle East, no breakthroughs should be expected with regard to Iraqi oil and Iranian gas supplies to the world market before 2015. One likely scenario in the next decade is that the U.S. will attempt to establish control over strategically important oil and gas regions at minimum financial and political cost. With respect to Iraq, it is the “controlled breakup” of the country into three parts, as a result of which the oil rich north will, as the U.S. hopes, pass under the control of a U.S.-Kurdish administration. Then the Kirkuk-Ceyhan oil export system would expand accordingly.

With respect to Iran, the U.S. will apparently continue to work toward the “democratization” of the country’s political life amid “mild” economic sanctions. One possible U.S.-Iran scenario could be separate agreements and the relinquishment of a number of claims in exchange for long-term fuel and energy projects. Given the long-term nature of these measures, as well as the growing political instability in the region throughout the period under consideration, neither Iran nor Iraq will be able to fully realize their energy production potential before 2017. For the U.S., the Broader Middle East will remain a “reserve” source of hydrocarbons for the long term. Meanwhile, in the next decade the U.S. will be actively developing oil production programs in Latin America, Africa, Canada and the Caspian.

Iran’s role in the world – both in its political and energy dimensions – will continue to grow as Tehran continues with its efforts to expand the geographic base of its energy exports. There are three directions in Iran’s regional gas strategy – western (Turkey, Europe), northern (Transcaucasia and Central Asia) and eastern (Pakistan, India, China, and Southeast Asian countries). The western vector of Iran’s gas policy (the Iran-Turkey gas pipeline with the prospect of moving into European markets) is in the zone of high political risks. Nevertheless, Iran’s reserves are a key to the EU’s independence from Russia. From this perspective, the United States is interested in resolving the “Iranian problem” as soon as possible. Thus, it will

be able to use Iran's energy potential to deal with its own geopolitical problems, specifically, as already mentioned, reducing the EU's dependence on Russian energy. Even so, projects that may bring Iranian hydrocarbons to the European market can only materialize after Iran's nuclear problem has been resolved "in a peaceful way." As long as this ominous problem exists, Tehran will continue to target primarily the markets of the Pacific Rim.

In the next decade, developed consumer countries will give high priority to alternative and renewable sources of energy. Today, this is one of the most dynamic segments of the energy sector. These include wind and hydroelectric power, as well as ethanol, Brazil being its largest producer. Large-scale bio-fuel projects will begin to surface. Investment in alternative types of energy is expected to come mainly from the United States, China and Japan, as well as from the world's oil and gas majors – BP, ExxonMobil, Royal Dutch/Shell, and others.

New technology will help make energy consumption more effective, but alternative energy sources will hardly be able to meet the world's growing energy needs: their share in the energy balance will only increase modestly. For renewable sources of energy to meet at least one-half of the required energy growth, their capacity would have to increase 63 times. Such growth is impossible to achieve within a space of 10 years. During this period (until 2017) it will also be virtually impossible to mobilize production of "alternative" oil (super-heavy oil, tar sand, blacks, etc.) or to develop fields and deposits in hard-to-access areas.

The liquefied natural gas (LNG) market is becoming a global market. The main growth in demand for LNG is expected to derive from the United States and the Pacific Rim countries. The U.S., which is already a major LNG importer, will continue to increase its LNG imports (there are 55 new projects for LNG terminals, including LNG re-gasification plants). Japan is likely to remain the LNG market leader until 2020, after which the U.S. will become the No. 1 consumer. Nevertheless, the main volume of natural gas by 2017 will still be delivered to consumers through pipelines. Implementation of LNG projects will be unable to reverse the trend in the next decade.

The share of nuclear energy will fall to 5.3% as developed countries pursue a policy to enhance the technological security and environmental safety of their energy systems. The use of nuclear energy in the world will decrease amid its reduction in Europe (-1.1% a year) and stabilization in North America. The steady reduction in the number of nuclear power plants in Europe (except France) will be offset by the construction of new facilities in Pacific Rim (China, India, Pakistan, South Korea, etc.), as well as in Russia, Iran, and Brazil. Consumption of nuclear energy in North America, Japan, and France will increase to some degree in the next few years, after which it will stabilize. ***Russia has a unique chance of increasing its share on the global nuclear energy market. But that rare window of opportunity will remain open for a brief period – about 10 to 20 years.***

The risk of a major drop of world prices in the medium term is very high. Contributing factors here include sufficient supplies of oil and natural gas, declining interest of developed countries in traditional [fossil] fuels, and the construction of new energy capacities in the Caspian, Africa, and other parts of the world, as well as the policy of consumer countries (above all the U.S.) toward steadily increasing their interest rates. As a result, a considerable number of investors are moving away from the raw materials market, which narrows opportunities for speculative growth in hydrocarbon prices.

In the foreseeable future, Iran will play a major role concerning prices on the hydrocarbon market. The course of events in and around Iran is likely to follow one of three possible scenarios.

Scenario 1 (the more likely): further confrontation between Washington and Tehran, which, however, will not lead to an armed conflict. In this case, the world energy market will see a downward trend with oil prices falling to \$40-50 per barrel and fluctuations within the range of \$5-10.

Scenario 2: reaching agreement and resolving the conflict by peaceful means, which will lead to a sharp fall in oil prices within a year. But the chances for the realization of this scenario are rather slim.

Scenario 3: an armed conflict. In this scenario, oil prices will exceed \$100 per barrel. Subsequently, if the armed conflict

becomes protracted, the price could rise to \$130-150 per barrel, which would force the U.S. to exert unprecedented pressure on the OPEC to increase production. As a result, competition in non-OPEC production areas will grow considerably. But if the military confrontation in Iran follows the “Iraqi model,” the market will gradually adjust itself and stabilize by 2015-17.

OUTLOOK FOR THE RUSSIAN OIL AND GAS SECTOR

Russia has a large potential on the world energy market. By now, more than 3,000 hydrocarbon deposits have been discovered and prospected in Russia. About one-half of them are being developed. Over 50% of Russian oil production and more than 90% of natural gas production is concentrated in the Urals and West Siberia. Most of the deposits in this region are marked by a high rate of depletion, so while it remains the country's main hydrocarbons base, it is also necessary to develop alternative energy production areas.

According to Russia's Energy Strategy for the Period Until 2020, by 2015, oil production in Russia could hit 530 million metric tons with oil exports at 310 million metric tons. The West-Siberian oil and gas province will remain the country's main oil base. New oil production centers will emerge in East Siberia and the Republic of Sakha (Yakutia) – up to 50 mln metric tons by 2015; on the Sakhalin shelf (25-26 mln metric tons), in the Barents Sea and the Russian sector of the Caspian Sea. Oil production will also increase in the Timano-Pechora Province.

The capacity of main oil pipelines and sea terminals for the export and transit of oil from Russia beyond the CIS could increase 50% by 2015. This will enable Russia by 2015 to export to non-CIS countries about 70 mln metric tons along the western and northwestern lines, about 130 mln metric tons along the Black Sea-Caspian line, about 80 mln metric tons along the eastern line, and up to 25 mln metric tons along the northern line.

By 2015, natural gas production in Russia could reach 740 billion cubic meters, with gas export hitting 290 bln cu m. Gas production in West Siberia during this period will stabilize, therefore,

most of the increase will be ensured by putting into operation new fields in East Siberia and Russia's Far East, as well as the northern and Far East sea shelf. Substantial natural gas reserves in East Siberia and Russia's Far East make it possible to form new gas production centers in this region.

At the same time, the existing trends in the development of the Russian fuel and energy sector suggest that in the next decade Russia will not be able to strengthen its positions on the world energy market, converting its energy potential into political dividends.

The main impediments to oil production growth in Russia are:

- the critical condition of the existing oil export infrastructure;
- mineral and raw materials reproduction problems;
- political restrictions with respect to construction of private pipelines and access for foreign companies to the Russian market;
- the low investment activity of oil companies; and
- the shrinking resource base of Russian oil companies (production has been exceeding reserve growth potential for many years).

The main factor in Russia's weakening positions on the oil refining market is the obsolescence and general poor condition of most of Russia's oil refineries. Thus, although some companies have modernized their refineries in the past few years, the general quality of Russia's oil refining infrastructure is considerably below international standards.

The main impediments to natural gas production growth in Russia are:

- the policy of Gazprom, which finds it unprofitable to develop the domestic market with the current domestic gas tariffs;
- the gap between the growth of gas production and consumption;
- the need to invest substantial resources in development of new deposits;
- the preference that is given to the purchase of Central Asian gas over investment in production projects;
- the state policy of barring foreign companies from developing the most promising fields (Yamal, Shtokman) as project operators;
- the critical condition of the existing gas export infrastructure, and
- the monopolistic nature of Russia's natural gas sector.

The upshot of all this is that the existing oil production growth potential will only last for a few more years. Because of a confusing, poorly regulated tax system, and a lack of investment incentives for prospecting work, raw materials companies will be unable to prospect and develop new large deposits. The rate of oil production growth that Russia showed in 2000-04 is unlikely to be maintained in the future. By 2017, Russia will reach the maximum production level of 10-11 million barrels a day (530-550 million metric tons a year) by the end of the second decade, and that level will eventually stabilize. By 2010, Russia will account for about 15% of the world oil market, and this share will fall to around 10% by 2030. Therefore, factoring in global consumption growth, Russia's share on the world oil market will tend to decline.

By 2010, natural gas production in Russia will stabilize, and by 2010, given domestic demand and export levels, Russia could have a natural gas shortage of 75-150 billion cubic meters.

To maintain or increase energy production and exports, Russia needs to start developing new areas – above all in Siberia and the Northern shelf. This requires a political decision to attract investment (including foreign investment). No drastic changes in this sector are expected before 2010 – or even by 2017.

Despite its leading positions in the production and shipment of hydrocarbons, Russia lags noticeably behind in the implementation of advanced technologies. The country's leadership puts the main emphasis on oil, natural gas and coal as the principal instruments that allow Russia to attain and retain the status of a great energy power. Meanwhile, the world's changing energy structure will by 2030-50 substantially reduce Russia's competitiveness.

Russia's technological lag, especially in the medium term, also concerns the production and transportation of liquefied natural gas (LNG). By now, about one-quarter of global gas exports come in liquefied form, with the LNG market expanding rapidly. It is not ruled out that by 2017 LNG will become a viable competitor to gas supplies that are transported via pipeline.

Concerning the implementation of large-scale LNG projects in Russia, the outlook is rather pessimistic. Virtually the entire

LNG volume within the Sakhalin-2 project (the only Russian LNG project that could be completed within the next five years) has been contracted. As to the situation around other LNG plants, their future is uncertain. For example, it was decided to re-route natural gas from the Shtokman field (the most promising deposit for LNG deliveries to the U.S.) to Europe, to be shipped by pipeline. The LNG project in Ust-Lug, even if it is carried out before 2017, will not be enough to turn Russia into a great gas supplier due to its low capacity.

While Europe will in the next decade remain the main market for Russian hydrocarbons, Russia's capacity for oil shipments to Europe is rather limited. The main pipeline, Druzhba, is in need of renovation; the Baltic Pipeline System has already reached full capacity, while in the south all of Russia's oil export routes flow via Turkish straits with no viable alternatives in the foreseeable future. The throughput capacity of the Bosphorus Strait is the most vulnerable part of Russia's transport policy as Turkey is expected to continue restricting its straits to the passage of foreign oil tankers. Such a scenario will, on the one hand, reduce Russia's export capacity and, on the other, compel Moscow to use the BTC as a reserve route in the southern direction (should the Turkish straits be closed off completely).

Russia will be able to partially compensate for losses with the Burgas-Alexandropoulos oil pipeline bypassing Turkish straits. But given that the costs involved in Russian oil production and exports exceed analogous costs on the Caspian, it is quite likely that Russian oil will be partially crowded out of the European market.

The second most important market, whose influence will be growing in the period under review, is the Pacific Rim market. Meanwhile, here too Russia has only a limited capacity to ensure the declared increase in energy supply (from 3% to 30%). To meet this target, at least 60 mln metric tons of oil and 65 billion cu m of natural gas a year will have to be "re-routed" to the east. This task is technically unfeasible and financially dubious in the next 10 years.

The Russia-U.S. energy dialog is in its early stages. From every indication, the resources of the Shtokman field will be sent to

Europe, while the construction of the Northern Oil Pipeline to Murmansk will be frozen until 2015 – the deadline for putting the Eastern Pipeline into operation (Transneft will simply not have enough money to handle both projects). By 2017, the share of Russian oil and petroleum products on the U.S. market will not exceed 5%. In the most likely scenario, these restrictions will not allow Russia to emerge as a major player on the North American market in the next decade.

Russia will be confronted with growing competition on the gas markets in Europe and the Pacific Rim. European consumers are pinning hopes for energy diversification on the increasing share of North Africa (Algeria, Libya and Egypt), as well as states in the Caspian region, Central Asia and the Middle East. A number of pipeline projects, due to be completed in the next five years (the BTC, the BTE, which is to be linked with Nabucco, and others), are designed to limit Russia's influence. For its part, China will implement a number of projects, also reducing its dependence on Russian hydrocarbons – oil and gas pipelines from Kazakhstan and a gas pipeline from Turkmenistan. Furthermore, oil deliveries to China from South America and LNG from Iran will increase.

Nevertheless, in Europe, Russia will retain its status as a regional energy leader. The EU will remain the largest market for Russian energy resources in the foreseeable future. It is rather unlikely that an all-European energy market will be created any time soon that would crowd out Russia.

The major contributing factors here are:

- outstanding problems within the EU framework, and the lack of consensus on ways of ensuring energy security;
- specific projects on alternative sources of energy in Europe are implemented mainly on the national level;
- the explosive military-political situation in the Middle East (especially around Iran, which is being closely watched by virtually all Russian gas consumers in Europe and in post-Soviet states as an alternative to Russia in oil and gas supplies) creates a number of political and military risks, impeding the implementation of Western plans to build new energy corridors.

Therefore, the main task facing Russia in the next decade will be to provide conditions to minimize expected losses, first, from its declining presence on world oil and gas markets, and second, from falling world energy prices. In this context, the main priorities for Russia are:

- a greater emphasis on the domestic oil and gas production sector – both on the state level and on the part of oil and gas majors;
- incentives to stimulate investment in the reproduction of the mineral and raw materials base and the development of new deposits;
- temporary deviation from the concept of global energy expansion in favor of investment in national production projects in East Siberia and Russia's Far East, the Sakhalin, the northern shelf, etc.;
- at the same time, considering that the Middle East is going to remain the world's main energy powerhouse, Russia should concentrate on preserving and expanding the presence of Russian energy companies in Iran, Iraq, and other states of the region;
- reviewing production sharing agreements (PSA) and developing new mechanisms for participation of foreign companies in LNG projects in Russia, taking into account the interests of both sides;
- special attention needs to be given to LNG production projects as by far the most promising on the global energy market;
- enhancing technological security and effectiveness of energy transport networks;
- expanding hydrocarbon deliveries to European markets by building additional energy transport facilities (to northern and southern Europe and the Balkans) and consolidating positions on the Pacific Rim market;
- Russian oil and gas companies should take advantage of the favorable external environment to modernize their production capacities, use advanced technology, and develop their sales network, which will help them cut production costs and offer more competitive products on foreign markets.

Are the Energy Majors in Decline?

Vladimir Feygin

The title of this article may seem rather provocative and overstating the tendencies that are only emerging in the global economy. Yet these tendencies are rooted in objective processes that, should they persist, may drastically change the overall situation in the world economy.

SHTOKMAN – THE FIRST ROBIN?

Gazprom's recent refusal to set up an international consortium for developing the Shtokman offshore deposit in the Barents Sea sparked uproar around the world. This deposit, boasting the biggest reserves of hydrocarbons under the seabed – its estimated resources stand at over 3 trillion cubic meters of natural gas – is really unique. It is located about 600 kilometers away from the shore, in an area that is prone to icebergs. Thus, experts from this field realized in the early 1990s that its development would require unconventional technological solutions. However, since the discovery of this deposit in the 1980s, few practical steps have been made to prepare this deposit for commercial use.

Discussions over the Shtokman gas field have been underway since 1991 when the first consortium (then consisting entirely of foreign companies) submitted its initial feasibility study to a board of government experts. As the economic and political situation in Russia at that time was highly unstable, Western corporations – with their experience of hydrocarbon production in the North Sea –

Vladimir Feygin is Chief Director of the Energy and Finance Institute.

hoped to make the project a fully export-oriented one. The plan called for the installation of platforms in accordance with Western technologies that would deliver gas shipments via pipelines to the European continent, thereby minimizing dependence on “Russian risks.” In 1992, liability for implementation of the project was handed over to a new Russian company on the scene called Rosshelf, which brought together Gazprom and several defense producers. The latter were meant to manufacture equipment for the offshore mining of hydrocarbons in line with the then popular policy of converting defense production to civilian use.

The project, however, had a low start. In the mid-1990s, Russia had enough operational gas fields to meet a sizably diminished domestic demand, as well as in the former Soviet republics and East European countries. In the meantime, the growing demand for gas in Western Europe was supposed to be met by ramifying the pipeline infrastructure rather than launching the extremely expensive Shtokman project. But the second half of the 1990s saw a sharp decline in the price of crude oil. As a result, Gazprom’s financial situation deteriorated and, in order to remedy the falling production levels, it was forced to focus on an immediate commissioning of the Zapolyarnoye deposit in north Siberia.

The beginning of the new century witnessed a steep growth in the demand for liquefied natural gas (LNG). Today, novel technologies help to considerably reduce the cost of its production and delivery by sea, and its competitiveness with the transportation of gas via pipelines (in areas where the two methods of transportation can be used alternatively) continues to grow. Add to this the growth of gas prices on the North American gas market (where prices remained rather low after liberalization for many years). The biggest U.S. corporations that had receiving terminals, contract portfolios and a history of deepwater hydrocarbon resource development (above all, in the Gulf of Mexico), displayed great interest in organizing wide-scale supplies of LNG. It should be no surprise that they turned their eyes to the Shtokman deposit.

The Europeans also took an interest in the project, although just a few years before this market seemed to be at a standstill,

with outdated terminals in Britain mothballed and hardly any new terminals being built. Thus, the participation of European companies in the project looked not only as a way of bringing liquefied gas to the European market at an earliest possible date, but also as a counterweight to U.S. influence. Moreover, Norwegian companies, which showed the biggest interest in the Shtokman project, really had much to offer in terms of technology.

The decision to change resources to LNG has made the Shtokman project one of the biggest global enterprises in this sphere. However, the scale of this initiative does not match the gas field's potential. Initially, the international consortium was supposed to implement the entire integrated project – from developing the deposit, to building a liquefaction plant, to exporting the gas, most of it to the U.S. The shortlist of potential Gazprom partners included five foreign companies: Conoco and Chevron of the U.S., Total of France, and Statoil and Norsk Hydro of Norway. The announcement of the winning contender was put off numerous times until an unexpected notification came that Gazprom had undertaken to develop Shtokman on its own.

How can this drastic change be explained?

Gazprom's rapidly growing foreign liabilities, together with the markedly expanding capacity of the domestic market, have put full-scale development of the Shtokman deposit to the top of the agenda once again. Early tests suggest this project will have an annual output of around 90 billion cubic meters (bcm), as opposed to 22 bcm estimated for the LNG supplies. Importantly, "pipeline gas" will be channeled to the Unified System of Gas Supplies, which pools together gas supplies for foreign and domestic consumers. This project stands in dramatic contrast to what was envisioned previously: namely, it targets an altogether different market (it is no accident that a decision was made to reorient main exports to the North-European Pipeline System). Also, the new project concept makes it difficult to estimate contributions and interests of participating companies, should their number be great; at least this would require too much time.

Another important factor is the volatility of the U.S. gas market where prices are not pegged to oil. Thus, the recent start of a price slide there poses tremendous risks for the LNG project.

Arguments in favor of the recent decision to exclude foreign energy companies from the Shtokman project vary, yet all observers agree that the latest developments were very abrupt. And why were such actions taken against the largest international oil and gas corporations? It would be an oversimplification to explain the situation by Gazprom's style of conduct.

DICTATE OF THE MAJORS

The largest oil and gas projects are traditionally implemented by a limited number of the most powerful – and mostly transnational – corporations (the 'majors' as they are often collectively referred to in English), or they are carried out under their guidance. The reason for this standard practice is simple: large-scale and technologically sophisticated projects require huge investment. Their implementation demands the concerted effort of numerous contractors, together with their extensive production experience. Such projects also require a steady position on relevant markets of commodities and services.

Over the decades, only the majors have had the capabilities to meet all of these conditions. They are capable of drawing the best financial resources since they have high financial ratings, as well as good reputations. Their capitalization power puts them in the ranks of the biggest global companies. The majors clearly have the knowledge and skills required for such projects, especially since the specific skills necessary for organizing business activities are often not directly linked to oil or gas.

However, it is a big question whether the majors hold leading positions in the field of innovation. It is a popular belief nowadays that the majors should focus on their core business, i.e. their main and narrowly specialized sphere of activity. This suggests they should outsource knowledge, skills and services. Innovations are highly specific and risk-prone, so the majors often assign them to technological, servicing and engineering companies that are specialized in these

fields. As for the skill of operating on modern energy markets, the latter are becoming increasingly more open to new suppliers, due to high prices and the fear of resource shortages.

Still, the majors are able to maintain their status due to the expansiveness of their activities, of which capitalization plays an integral part. They draw their power from the amounts of resources they control. The resources are easily recalculated into capitalization and form the long-term basis for their business activities. Whereas the business of the servicing companies is contingent on the success at bidding for specific customers' orders, the majors enter these contests as certain winners by having secured huge resources.

The struggle for resources, of course, runs through the history of the global corporations. Propped up by overt support from political circles in Western countries, the majors for decades fought against the tide of nationalization and put up obstacles to the formation of OPEC as an association of countries where the production of oil and gas had been nationalized. However, in a large number of countries, they had to reconcile themselves to the roles of project operators, not owners.

THE MATURING GENERATION

A new generation of the largest oil corporations – like Statoil and Norsk Hydro in Norway, Petronas in Malaysia, CNPC and CNOOC in China – have surfaced across the world in the past few decades. This phenomenon was the result of state policies of strengthening “national champions” in the oil and gas sector; in other words, the ones that would eventually replace the “invited coaches.”

Norway offers an illustrative example. Unexpected wealth poured into this country when oil and gas deposits were discovered in the North Sea. Since the Norwegians did not have either the experience or personnel in that sphere, they pursued active cooperation with foreign companies. At the same time, they endorsed rigid tax regulations (which brought to existence the ‘future generations fund’ – experience that Russia decided to follow). Furthermore, serious efforts were made to develop national research centers and production facilities, as well as to assimilate

novel technologies. Large integrated projects embraced key areas of oil and gas technologies, such as construction of the biggest marine platforms, the extraction of deepwater resources, etc. All of the major international companies that worked on Norway's continental shelf joined in this activity (unfortunately, the realm of cooperation has not been exactly copied by Russia).

From the very start, the Norwegians realized that oil and gas wealth is finite and it must be used in a way that could ensure long-term results. Today, the output of crude on the Norwegian shelf is decreasing and the output of gas will soon reach its peak. In the meantime, Norway's largest producers, Statoil and Hydro, which are co-owned by the government, have achieved the rank of global technology leaders. Statoil built Europe's first gas liquefaction plant on the Snovit deposit, while Hydro engaged in sub-surface development of the Ormen Lange gas deposit, located in the Norwegian Sea at a depth of about 1,000 meters. In their offer to join the Shtokman project, they planned, primarily, to contribute novel technological solutions.

Other resource-rich countries have set for themselves the similar goal of turning their leading oil and gas companies that possess highly qualified technical personnel into major international players. These companies seek to export their skills and even force the traditional giants to make room not only at home, but also on the world market in general. True, an opposite trend is observable as well: oil companies in the OPEC countries, for example, also receive super-profits on crude, but lack potential in research, technologies and organization that might grant them a new stage of growth. Russian oil and gas majors should consider these examples if they seek to become powerful and independent global players in the foreseeable future.

A CHANGE OF THE GUARDS

The formation of new energy majors has received a new incentive of late after oil prices surged, which gave the oil and gas producing countries and their largest companies huge financial resources. Public companies (even those where the governments have sizable

or dominant stakes) have beefed up their capitalization. The leading ones, like Gazprom, have taken over the top positions in the rankings, pushing aside the traditional majors. Their capitalization, together with growing revenues and the attendant rise of ratings, are paving the way to greater financial might.

The newly emerging majors – or at least the most advanced of them – have good prospects for replacing the traditional majors on the global market. This may be accomplished, for example, by them becoming powerful organizers and operators of projects, first in their own countries and then globally. Their main advantage over the traditional competitors is national mineral resources, which serves as a prerequisite for gaining strength, as well as a launching pad for further expansion. Incidentally, the traditional majors developed in much the same way at the dawn of their history. They relied on their own resources (like European resources that have been exhausted or are waning now), or on the resources of the colonies.

If one views the current developments as a long-term tendency, the older-generation majors are heading for very tough competition. The governments of the resource-rich countries, and national companies enjoying governmental support, are interested in reducing the role of transnational corporations to that of ordinary contractors in developing large deposits. Naturally, the majors deem it unprofitable, since work on contracts brings virtually nothing in terms of capitalization. What is more, they will have to compete with specialized servicing companies even for these contracts.

Undoubtedly, it would be premature to write off those corporations that have dominated the energy market for over a century. Challenging projects are a tricky business. Also, it cannot be ruled out that the traditional majors will start restructurings in order to expand the scope of their core business and win back their market positions. For instance, they may focus on gaining control over crucial cutting-edge technologies. If this happens, one can expect some form of a battle between the existing resources (possessed by the new majors) and the new technologies. Whatever the case, the Shtokman project may be a forerunner of critical changes in the global energy sector.

Energy Partnership – A Dialog in Different Languages

Tatyana Romanova

Energy comprises a rather specific area of interstate cooperation, and this is especially true of relations between Russia and the European Union.

This reality is rooted, first, in the fact that stable energy supplies are vital for the development and prosperity of a state, being an essential component of energy security.

Second, energy has an immense potential for integration. In fact, it underlies the formation of the European communities because at the time of the signing of the European Coal and Steel Community Treaty in 1951, coal accounted for 80 percent of the energy balance in the European countries. Furthermore, the production and transportation of natural resources requires considerable investment and capital-intensive infrastructure, which for their part stimulate the signing of long-term contacts between consumers and producers. Finally, relations in the energy sphere can lay the groundwork for long-term contacts in other sectors of the economy, as well as in the realm of politics.

Third, there is a direct interdependence between the EU's demand for hydrocarbons and Moscow's need for revenues from the sale of energy resources (the EU buys over 50 percent of Russian oil exports and more than 60 percent of Russia's natural gas exports). This factor substantially alters the traditional lineup of forces and economic relations between the two parties. In the nor-

Tatyana Romanova, Doctor of Science (Politics), is an associate professor at the Department for European Studies of the St. Petersburg State University.

mal course of things, the EU tends to take an arrogant, condescending view of economic relations, as it attempts to impose its own rules of the game both at the bilateral and multilateral level. Although the EU has made such attempts in the energy sphere, its approach has been rather low-key, while Moscow's reaction has been fairly tough. Over the past six years, the possibility of signing a separate energy treaty has been mulled continuously.

The above factors explain the high priority that is given to Russian-EU energy relations, especially now that they have fallen on hard times.

BATTLES ON THE ENERGY FRONT

One indication of the worsening relationship between Russia and the EU in the energy sphere was the April 2006 standoff between the Russian energy giant Gazprom and the UK (EU).

In early 2006, Gazprom had stated it was interested to buy the UK gas supplier Centrica, as well as Scottish Power, an international energy company. Centrica share prices jumped, but the prospect of a Gazprom acquisition worried London. Thus, after several rounds of consultations, it was decided to adopt special legislation to prevent the acquisition of UK enterprises by the Russian company – for energy security considerations. (In 2003, a law was adopted in the UK under which the government may not block a merging of companies or their takeover on the British market for political considerations.)

The disclosure of these measures by *The Financial Times* predictably provoked a harsh reaction from Gazprom. At a meeting with the ambassadors of EU member countries in Moscow, Gazprom CEO Alexei Miller said his company did not want to face artificial obstacles on the European market that are based on considerations of political expediency. Otherwise, Miller warned, the growth of energy deliveries to Europe would decrease, with Gazprom gradually reorienting itself toward China and the U.S.

A retaliatory response was not long in coming. The European Commission stressed that the EU would not tolerate threats and expected contractual obligations to be met in full. At the same time,

it pointed out that Gazprom was free to diversify its deliveries for commercial purposes, but its behavior had once again confirmed European concerns about the stability of supplies from Russia and therefore the need to diversify channels for the delivery of natural gas, as well as natural gas suppliers. Javier Solana, EU High Representative for the common foreign and security policy, drafted a paper entitled “An External Policy To Serve Europe’s Energy Interests.” British Prime Minister Tony Blair, however, said that no one would place obstacles against the Russian company on the UK market, and the conflict was resolved.

The idea of Gazprom moving into the distribution sector arose from the liberalization of natural gas and electricity markets. One outcome of the EU energy sector reform was the abolition of the “destination clause” in Gazprom’s long-term contracts with European gas companies, i.e., the territorial proviso, which does not allow for the re-export of gas. Different gas prices for different European consumers (depending on the distance of transportation) could have led to a situation in which Gazprom products would have started competing with themselves. The only sensible solution in that situation was for the company to move into the distribution sector. It also provided access to sales – the most lucrative segment of the natural gas market. That was the compromise that Gazprom and its partners reached when the destination clause was lifted.

Gazprom’s operation in the distribution sector can also be interpreted as Russia’s departure from its traditional specialization in raw materials and a shift into the export of downstream products and associated services. But that move came up against opposition both in the UK and the EC because it was interpreted as a deviation from the fair competition principle: with no liberalization in sight on the Russian market, the Russian company was planning to take advantage of the reformed EU market. Unsurprisingly in that situation, the EC said it was going to sue Gazprom over violation of fair competition laws.

Russia’s refusal to open up its own market will be perceived by the EC as a move aimed at consolidating its position solely as the

EU's raw materials appendage. Thus, the argument goes, Russia will bar access to both the distribution segment and the market of downstream products. At the same time, it could be argued that the EC is attempting to sell access to the EU's internal market twice – first, as payment for modification of long-term contracts and, second, as an incentive for the liberalization of Russia's natural gas market.

Another indication of the Russia-EU confrontation in the energy sphere is the decision on the Shtokman gas condensate field. Discussions around this gas deposit in the Barents Sea, with probable reserves of 3.7 trillion cubic meters, have been ongoing for over 10 years now. The latest stage of the debate started in September 2005 when a short list of candidates for a consortium to develop the field was announced. It included Norwegian Statoil and Norsk Hydro, ChevronTexaco and ConocoPhillips of the U.S., and Total of France. It had been expected that Gazprom would soon announce its decision amongst the candidates.

It has long been assumed that Gazprom needs foreign partners to develop the Shtokman field. First, the field is difficult to develop and would therefore require access to advanced technology. Second, it provides for the transportation of natural gas in liquefied form, mainly to the U.S., and therefore requires LNG technology and access to the American market. Finally, it requires significant financial resources.

Nevertheless, the Russian gas monopoly dragged its feet on the makeup of the consortium. Meanwhile, competition between the potential partners, each of whom had its own perceived advantages, was fueled artificially. The Norwegians were ready to share their extensive experience in operations in the arctic seas, offering production and transportation technology, as well as asset swapping. The French offered asset swapping and LNG technology, while the Americans mainly offered access to the consumer market.

Soon, however, the lineup of forces changed drastically. At a French-German-Russian summit in Compiègne (France, late September 2006), Russian President Vladimir Putin said some of the natural gas produced at the Shtokman field could be delivered to the

European market. Observers linked this comment to Moscow's difficult negotiations with Washington over Russia's admission to the WTO. As a result, the analysts suggested that preference in the consortium would be given to European companies.

Then, in the course of his visit to Germany, the Russian president said that the North European Gas Pipeline (Nord Stream), which travels below the Baltic Sea and links Russia and Germany, would be used to carry gas not only from the Yuzhno-Russkoye field (in the Tyumen Region), but subsequently also up to one-half of gas supplies from the Shtokman field. That was taken to mean Gazprom's refusal to enter the promising LNG market. The Russian president's statement calmed the Europeans' fears that Gazprom would simply not have enough resources to fulfill its obligations to European suppliers.

Finally, on October 9, Gazprom announced that it did not need any partnership to develop the Shtokman field. Apparently the company had failed to find a partner that would offer acceptable terms – that is to say, provide Gazprom with matching assets, both in volume and quality, in exchange for a share in the deposits.

The EU interpreted the decision as yet another attempt by Russia to restrict the liberalization of its energy market. In particular, members of the Norwegian Storting expressed their regret, pointing out that cooperation would benefit all sides. U.S. politicians were more outspoken, saying that Russia's refusal was well in line with Russia's policy toward self-isolation, including the isolation of its energy sector, while the International Energy Agency described the decision as an unmistakable sign of nationalism. At an informal meeting between Putin and EU chiefs of state in October 2006, considerable time was devoted to the discussion of this issue, with the Russian side explaining its position in detail.

Finally, the third event that illustrates the state of “energy relations” between Russia and the EU were their negotiations on the Energy Charter Treaty, which Russia and a number of other states signed back in 1994 and that went into force – albeit without Russia's participation – in 1997.

The Treaty is concerned with four sets of issues.

First, trade in energy resources based on WTO principles.

Second, protection of capital investment at the post-investment stage against all sorts of non-economic risks, as well as profit repatriation guarantees.

Third, transit. Here, the Energy Charter Treaty and Protocol make provisions for free transit across the territory of all signatory states, as well as for international mediation to settle disputes on a temporary basis. Outstanding issues include auctions for available capacities, securing long-term contracts with long-term agreements on the use of capacities, and regional integration provisos. It should also be noted that Gazprom is concerned about the loss of a substantial part of its revenues and control over the Unified Gas Supply System.

Fourth, energy effectiveness.

The Energy Charter Treaty was long viewed as a dead mechanism, but in 2006 the EC and EU member states threw their support behind it. Moreover, the document's ratification by Russia has become an *idée fixe* with Brussels' bureaucracy. This turn of events was largely precipitated by the Ukrainian-Russian crisis in early 2006. In addition, ahead of the G8 summit, where Russia offered its own vision of energy security, it was suggested that the basic principles were already enshrined in the Energy Charter Treaty and that all that was left to be done was to ratify the Charter.

In a letter on behalf of the EU leadership in the run-up to the Sochi Summit in May 2006, EU Energy Commissioner Andris Piebalgs and Austrian Economy Minister Martin Bartenstein (Austria held the EU presidency in the first half of 2006) stressed that the EU was ready to preserve long-term contracts provided that Russia ratified the Energy Charter Treaty. That was yet another example of how the EU, which had already pledged to maintain long-term contracts in working out guidelines for the liberalization of the natural gas market in 1998 and 2003, as well as at a time when the contractual terms had changed, attempted to "sell" that advantageous gas delivery condition to Moscow once again.

After the May Summit, Vladimir Putin stated in no uncertain terms that Russia wanted to know exactly what it would receive in exchange for the ratification of the treaty, and what benefits it would get in addition to a possible inflow of investment. That was an obvious hint that Russian companies should be given access to the EU consumer market and that the Energy Charter Treaty provisions therefore should be reviewed.

It may be recalled that the EU partially excludes its territory from the effects of the Treaty, sticking to the regional integration clause, which gives precedence to EU internal legislation over the Energy Charter Treaty.

An informal meeting between the Russian leader and the EU heads of state in Lahti (Finland) on October 20, 2006 marked a new trend in the EU approach toward the Energy Charter Treaty. It was proposed that the relevant provisions of the Energy Charter Treaty and Protocol be incorporated into a new legal framework for their relations – i.e., the Strategic Partnership Agreement, negotiations on which are to start in 2007. In other words, the idea is to make the approval of the new legal framework for Russia-EU relations dependent on Russia's acceptance of corresponding requirements in the energy sphere. This will come into conflict with the stipulation that the Strategic Partnership Agreement proclaims only the basic principles and aims of cooperation, whereas all sector-specific accords are taken outside the framework of the Treaty. Furthermore, this will drastically change the field of negotiations.

A CONCEPTUAL DIVIDE

So what is the reason for the growing confrontation in the energy dialog between Russia and the EU? It is fueled primarily by the widening gap in the sides' conceptual approaches toward energy cooperation. Importantly, these differences have a serious impact not only within the energy sphere per se, but also on the central problem of Russia-EU relations, that is, laying the legal groundwork for cooperation between Moscow and Brussels after 2007.

The EU's approach toward energy cooperation was formulated in the early 1990s, about the time when the Energy Charter and

the related treaty were signed. At that time, energy legislation within the EU was only emerging so the Partnership and Cooperation Agreement (PCA) between Russia and the EU simply contained a reference to the Energy Charter Treaty as a basis for relations between the partners in the energy sphere. Thus, according to Article 65 (1) of the PCA, “cooperation shall take place within the principles of the market economy and the European Energy Charter, against a background of the progressive integration of the energy markets in Europe,” while Article 105 reaffirms this principle, making a reference to the Charter: “In so far as matters covered by this Agreement are covered by the Energy Charter Treaty and Protocols thereto, such Treaty and Protocols shall upon entry into force apply to such matters but only to the extent that such application is provided for therein.”

The Energy Charter and the Energy Charter Treaty were drawn up with the direct participation of the European Commission. The European community had jurisdiction on matters of trade and transit, and it was therefore essential to get the European Commission involved in the process. Furthermore, the Commission was to ensure that relations in trade, investment, and transit were not in conflict with the emerging liberalization of the energy markets of the EU member states. Finally, these documents were supposed to provide a basis for a fourth community in Europe going beyond the three communities that had been formed in the 1950s, gradually integrating Russia and other post-Soviet countries into a common European space.

Step by step, EU energy legislation began to be codified. On the one hand, it was based on general internal market principles (free movement of goods, services, capital and people, as well as the promotion of competition between all European market players). Furthermore, there were environmental protection requirements that involved substantial costs (today, they account for up to one-third of the final costs of electricity), and therefore companies violating those requirements acquired a significant competitive advantage.

On the other hand, the changes that had occurred in the natural gas and electricity sector, which were the focus of the EC’s

reform program for the EU energy system, were similar to those in any other network business sector (telecoms, transport, etc.). The plan involved large-scale liberalization – i.e., separation of producer of goods (services), carrier, and supplier of goods and services from each other.

Because the development of the EU market moved beyond the framework designated in the Energy Charter Treaty, and because Russia was in no hurry to ratify it, the EU started making new conditions for energy cooperation with Russia. The general meaning was that Moscow gradually bring its energy legislation in line with European legislation. As an additional incentive, the idea of regional integration, which exempted the EU from the effects of some of the provisions of the Transit Protocol, was brought into the negotiations on the Protocol to the Energy Charter Treaty.

So the focus in building a unified regulatory mechanism shifted into the sphere of bilateral relations. The EC's main mechanism was to encourage legislative harmonization as a basis for action by energy companies, which enabled them to operate effectively and provide the EU with the required volume of resources.

A fundamental transformation occurred within a few years: the idealistic vision of the Energy Charter Treaty gave way to the realistic perception of the Charter and the Energy Charter Treaty, as well as energy dialog as a means of ensuring energy security. At the same time, the idealistic belief that liberalization based on EU principles was good for all states, including Russia, remained.

Throughout the 1990s and at the beginning of this century, the European Commission was consistently urging the EU at all inter-governmental conferences to grant the Community the powers to formulate external energy policy, but its pleas were invariably rejected. So all it could do in that situation was to develop its energy legislation and rely on European energy companies. Meanwhile, the ban on access to the EU's lucrative internal market in the absence of liberalization was, on the one hand, an important economic regulator protecting the European producers against unfair competition and, on the other, an instrument of strengthening their positions on the global energy market.

In this light, the events around Gazprom's attempt to acquire assets in the UK, and especially the rhetoric coming from the EC, are taking on an altogether different meaning. The EC's discontent over the Shtokman decision is also understandable: it excludes those European players that are purportedly translating the EU energy security concept into reality.

It should be noted that by striving to impose its legislation, the EU does not limit itself to Russia. It is pursuing the same strategy not only with respect to EU candidate member states (which is only natural) but also in relation to potential recipients of EU energy laws.

Russia's approach toward energy cooperation evolved over a substantially longer period. Initially, a coherent long-term policy was lacking, with an aggregate of short-term, narrow interests of individual companies or sectors prevailing. Also lacking was an understanding of Russia's long-term interests in its energy dialog with the EU. That was why the European Commission succeeded in setting the agenda for negotiations by incorporating individual problems that aroused Moscow's concern.

The situation only began to turn around in the past few years, as shown by Russia's negotiations with Germany on the North-European Gas Pipeline project and the development of the related Yuzhno-Russkoye field. The focus started shifting toward the idea of asset swapping – offering a share in Russian natural gas deposits in exchange for access to distribution networks – that is to say, the most lucrative segment of the EU's natural gas market.

Moscow's views on energy cooperation were finalized during the preparations for Russia's G8 presidency (energy being one of the priority subjects there) and during the discussion of the energy security concept. It was stated in no uncertain terms that reliable security guarantees should be provided not only to consumers but also to suppliers. Supplier security guarantees mean that the natural resources that are produced will find their consumer, while investment will be recouped. In other words, this is about long-term obligations for suppliers to produce and deliver energy resources and for consumers to buy them at reasonable prices. At

the same time, obligations should not necessarily be formalized in long-term contracts.

In addition to mutual guarantees, development of relations between companies should be ongoing, with reciprocal access for producing enterprises to distribution assets and for importing countries to production assets. Such interpenetration will not only facilitate business diversification but also help involve the commercial segment (private actors) in ensuring energy security on the global level. Therefore, in working to translate their concept into reality, both Russia and the EU rely on close interaction with the energy business.

Russia's relatively new but long-term energy cooperation concept was reflected in the final energy-related document that was adopted at the G8 Summit in St. Petersburg in July 2006. Furthermore, for the past year it has been the focus of discussion at various meetings between Russian and EU officials.

Unsurprisingly, Gazprom sees the UK situation differently than the EU does. What is important here for the Russian energy company is, first, compensation for alterations in long-term contracts with access to the end-consumer market and, second, access to the distribution segment in exchange for access for foreign companies to Russia's production sector. In this context, Russia's refusal to form a consortium to develop the Shtokman field should be read as a declaration that it had not received commensurate assets, while its Western partners underestimate the capacity of its shelf deposits. At the same time, it is also a demonstration of Russia's new concept of energy cooperation on the practical level.

Finally, Moscow's position on the Energy Charter Treaty becomes as clear as can be: if it is to abandon its long-established monopoly position, Russia must know exactly what it will get in exchange for that and just how open the European market will become for Russian companies. Moscow is, in effect, saying that it will not seek unilateral action and that compromise on its part calls for reciprocal moves by the EU. This also puts into perspective the statement that the Energy Charter Treaty should first be modified and only then can its ratification be discussed.

A comparative analysis of the two concepts shows, **first**, that the EU vision is more mature and better thought through: it is better articulated and legally substantiated. But it seems that the obligations of the EU partners are given greater priority than those of the EU itself. Furthermore, the EC is evidently determined to extend the effects of EU legislation to Russia and strengthen its regulatory impact on Russian companies.

By contrast, the Russian approach is largely based on political declarations. It is noteworthy that this is probably the first time that Brussels is coming up against difficulties in setting an agenda.

Second, the EU calls for instituting a common legal environment that will give companies greater freedom of action. At the same time, Russia believes in concluding concrete agreements between concrete companies on concrete, clearly specified assets. This approach was realized on the one hand in Gazprom's negotiations with Germany's E.ON Ruhrgas and BASF on the North European Gas Pipeline Project and the Yuzhno-Russkoye gas field, and, on the other hand, in the debate around the Shtokman project. It is a political principle that should be used as a basis for specific projects. A considerable amount of dirigisme is inevitable here.

Third, Russia has raised the issue of compensation for the loss of its exclusive right to control its unique system of natural gas pipelines, as well as its deposits. Meanwhile, the EU keeps talking about the benefits of market relations in general and about the advantages of building a pan-European market. At the same time, Brussels is not ready yet to address the issue of compensation.

Finally, the situation is complicated by the fact that Russia appears to be a rather "consolidated" actor: its policy course is enunciated by the head of state and relevant government ministers, while companies actively implement it. By contrast, the EU is relatively heterogeneous. The aforementioned concept is pursued by the EC but is not always endorsed by EU member states.

Indicative in this respect is Germany's policy, as well as statements by French President Jacques Chirac at the informal EU meeting in Lahti, to the effect that EU values should not serve as the sole foundation for formulating EU energy policy toward

Russia. Such disagreements not so much facilitate the advancement of the Russian position as irritate EU member countries and representatives of EU institutions.

BEYOND ENERGY COOPERATION

Clearly, because of the different views on energy cooperation, Russia and the EU are doomed to the ongoing confrontation in this realm until both sides reach a compromise.

Negotiations on a new agreement will be extremely difficult, and the following factors need to be taken into account:

- Unlike the early 1990s, Russia today is not only opposed to a simple copying of EU laws (as provided for, e.g., in Article 55 of the PCA) but has also put forward an alternative concept. But the European Commission is not ready to abandon its traditional orientation toward the “unilateral transfer” of its legislation. Furthermore, should norms different from those accepted in the EU be codified, the European Court may refuse to approve the treaty. Otherwise, painstaking, prolonged, and capital-intensive efforts will be required to alter certain provisions of European legislation.

- Moscow is not translating its political vision into concrete legal norms. Rather, it is putting forward political projects without fleshing out their technical details. So it is not always clear to technocratic Brussels what it should do with them. A recent EC paper on external energy policy, prepared at the informal meeting in Lahti, on the one hand, acknowledges the differences in approaches between Russia and the EU. On the other hand, it only proposes practical measures that conform to the EU vision of energy dialog. Therefore, Russia and the EU are speaking in different languages not only conceptually but also technically.

- The views of individual EU member countries and institutions seriously differ from each other. This can complicate both the advancement of Russia’s “divide and rule” policy and the negotiating process. A special committee, comprised of national representatives, will watch every step the EC takes, preventing any deviation from a consensus.

Finally, the difference in approaches and the need to search for a compromise between diametric views de facto predetermines the structure of any future agreement. It should not be a big, comprehensive document, encompassing all sectors. This can only be a general agreement (strategic partnership agreement) and a number of sector-specific agreements, which will be used as a platform for a complex compromise between the Russian and the EU vision. In the interest of preserving the balance of forces, different sector-specific agreements can be consolidated into blocks, as is the case with agreements between Switzerland and the EU. In other words, several such agreements can constitute one group conditional on the “guillotine principle.” Under this principle, the tearing up of one agreement will mean the termination of all other agreements in this group. This will provide an additional guarantee that both Moscow and Brussels will fulfill their obligations.

FOREIGN AFFAIRS



Before it becomes policy, it's in *FOREIGN AFFAIRS*

When you want to be the first to know what the experts in foreign policy and economics have to say about world events—turn to *FOREIGN AFFAIRS*. With contributions from distinguished authorities like Condoleezza Rice, Richard Holbrooke, Fouad Ajami, Donald Rumsfeld, Kenneth Pollack, and Samuel Huntington—this is the forum for leaders who shape the world.

SUBSCRIBE TODAY TO
**FOREIGN
AFFAIRS**

“The most influential periodical in print.” —*TIME*

“*FOREIGN AFFAIRS* is essential reading.” —*FORTUNE*

“*FOREIGN AFFAIRS* [is] the most prestigious of America's many foreign policy journals.” —*FINANCIAL TIMES*

**SPECIAL OFFER for readers of *Russia in Global Affairs*:
One year only US\$57.00!**

You will receive 6 bimonthly issues delivered via air mail. Your satisfaction is guaranteed or you will receive a FULL REFUND on all unmailed issues.

To order, send payment to: FOREIGN AFFAIRS SUBSCRIPTION SERVICES,
P.O. Box 420190, Palm Coast, FL 32142-9970 U.S.A.
TEL: (386)445-4662 FAX: (368)446-5005 or EMAIL: ForAff@palmcoastd.com

All international orders must be prepaid, therefore, please make checks or international money orders payable to Foreign Affairs in US\$ only. We also accept MasterCard, Visa, and American Express as payment. Please allow 6–8 weeks for the delivery of your first issue.

www.foreignaffairs.org/ordernow

Global Agenda



Ossetian girls in national dresses.
Photographer D.A. Nikitin. 1881

“ The international community cannot ignore cases when, due to different interethnic problems – historical, psychological, or economic in nature – secession by an ethnic minority is more in harmony with historical reality than is the preservation of its uncertain status as an unrecognized state. The ethnic-territorial conflicts in Kosovo, Abkhazia and South Ossetia all fall into this category. ”

Security Services, Police, and Human Rights *Valery Zorkin*

48

Self-Determination: Between Law and Politics

Alexander Aksenyonok

55

East Asia and Russia's Development Strategy

70

The 21st Century Mafia: Made in China *Vladimir Ovchinsky*

84

Security Services, Police, and Human Rights

Valery Zorkin

The international community has been increasingly active in discussing principles and methods for establishing democratic control over national security services, and the European Committee on Crime Problems has conducted a special study on this issue. The Geneva Center for the Democratic Control of Armed Forces and the Norwegian Parliamentary Intelligence Oversight Committee have released a guide entitled, *Handbook on Making Intelligence Accountable: Legal Standards and Best Practice for Oversight of Intelligence Agencies*. On June 23, 2005, the Parliamentary Assembly of the Council of Europe issued Recommendation 1713 entitled, *Democratic Oversight of the Security Sector in Member States*. At the 969th meeting of the Ministers' Deputies on June 21, 2006, the Council of Europe's Committee of Ministers adopted a response to this recommendation.

It would seem that these documents set out in detail the required approaches to the problem of democratic oversight of the security sphere. Yet this issue still has many aspects that require in-depth analysis together with the development of corresponding recommendations.

One is to ensure the protection of human rights and basic freedoms while security services and police fulfill their functions in countering new challenges and threats.

Valery Zorkin is Chairman of the Constitutional Court of the Russian Federation.

Why should this problem be formulated in such a way?

First, the need to increase the protection of human rights and basic freedoms amidst the struggle against terrorism has been repeatedly raised in conceptual documents of the United Nations. It was formulated in a particularly acute and comprehensive way in the Global Counterterrorism Strategy, adopted by the UN General Assembly in September 2006, as well as in documents of the July 2006 G8 summit in St. Petersburg.

Second, the international community should not confine itself to counterterrorism measures alone. Terrorism is closely intertwined with organized crime, corruption, drug and human trafficking, illegal migration, and the illegal arms trade. Every operation conducted by security services and police is usually of a comprehensive nature, but occasionally it is difficult to draw a clear line between different kinds of criminal activity, as well as between cause and consequence. This is particularly evident in Afghanistan today where drug trafficking feeds terrorism, while drug trafficking itself cannot exist without all other forms of crime.

Third, security services must everywhere be ranked on the same level as the police. The legislation of some countries, including Russia, does not even include the notion of “security service.” Meanwhile, police quite often fulfill the duties of a security service. As a rule, especially during counterterrorist operations, police and security services operate as a single unit and, naturally, bear joint responsibility for violations of human rights and democratic freedoms.

Particular problems that demand a solution are:

1. *Observance of the sovereignty of nation-states.* World leaders repeatedly declare their intention to support those efforts that ensure sovereign equality for all states, as well as respect for their territorial integrity and political independence. Appeals are often made to nations to abstain from using force or the threat of force, which would not correspond to the objectives and principles of the United Nations. In keeping with the principles of justice and the right to self-determination of peoples that still remain under colonial rule or foreign occupation, it is always emphasized to seek the peaceful set-

tlement of disputes. Global leaders proclaim the principles of non-interference in the internal affairs of states; respect for human rights and basic freedoms; equality for all without distinction as to race, sex, language or religion; and international cooperation in addressing economic, social, cultural or humanitarian problems.

These issues are directly linked with ensuring human rights in the course of operations conducted by security services, police and armed forces.

Inflexible and stringent actions that undermine state sovereignty (such as those taken by the armed forces and security services of the United States and some European countries in Iraq) provoke fierce resistance from citizens of the victim countries, and myriad destructive elements take advantage of such developments. As a result, the level of violence in these countries surpasses all acceptable limits and introduces new waves of terrorism.

Not a single decision involving military intervention is made without the knowledge of security services and their concrete assistance. Accordingly, special national forms of control over intelligence agencies are necessary. At the same time, international legal restrictions on the influence of these bodies are also crucial.

National sovereignty is often violated when security services of one country perform a mission on the territory of another country. There are also disturbing cases when a security service of one country violates the human rights of a citizen of another country, while using the territory and special institutions of a third country for protection. I refer here to the scandal over the existence of CIA secret prisons in some European states. Such a practice cannot be recognized as acceptable under any circumstances.

2. Torture. Despite international legal bans, this medieval practice continues today. European organizations often accuse Russia of practicing torture in the course of its counterterrorism operation in the Chechen Republic. Unfortunately, this criticism is sometimes well grounded, and Russia's prosecutor's offices are presently investigating several criminal cases involving torture there.

However, Russia is not the only country notorious for torture. Suffice it to recall the unsavory actions by troops and security ser-

vice officers of the U.S. and some European countries in the course of the counterterrorism operations in Iraq and Afghanistan.

In November 2006, a huge scandal erupted in Great Britain after an investigation revealed that 164 officers had for 10 years practiced refined tortures in British prisons.

Amidst the general practice of tortures, which is kept under a shroud of secrecy, then UN Secretary General Kofi Annan pointed to an even more alarming tendency: some countries, pleading national security considerations, have proposed lifting bans in their national legislations over the use of torture. Annan rightfully argued that fear of terrorists cannot justify the use of their own methods.

The former UN chief reminded that an absolute ban on the use of torture is fixed in international law and is obligatory for all states on all territories under their jurisdiction or control. Those who sanction and employ torture must not remain unpunished. No state should close its eyes to torture being practiced on the territory of a third party. Finally, no person should ever be extradited to a state where there is a threat of torture.

3. Human rights and the employment of weapons and special methods in anti-terrorism and anti-crime operations. Serious concern must be given to the employment of weapons against suspected terrorists, as such operations result in numerous casualties.

Everyone remembers the tragic hostage seizure at a Moscow theater in October 2002, when more than 100 people died as a result of a gas used by security forces to subdue the hostage-takers. Or one can mention the security operation to free children taken hostage at a school in Russia's Beslan. On each of these tragic occasions, there arise questions over the adequacy of the methods of the security services and police to free hostages or seize terrorists.

Another issue involves the physical liquidation of terrorists, and on this point there arises a paradoxical situation: all European countries have abolished the death penalty, while Russia has introduced a moratorium on it. In other words, a terrorist cannot be executed on the basis of a court sentence. On the other hand, any

terrorist or suspect can be easily shot dead during a counterterrorism operation, even if he shows no resistance and simply tries to run away, as happened last year in London. [On July 22, 2005, Brazilian national Jean Charles Menezes was chased onto the London subway by plainclothes British police officers and shot dead at point blank range – Ed.] Such situations are rather common in everyday police practices, as well.

4. *Human rights and the employment of biometric and visual means of control by security services and police.* Any person wishing to rent a car at London's Stansted airport must have his or her fingerprints scanned. For now, this is only an experiment that is being conducted by the police in the county of Essex, where the airport is located, together with rental firms. Yet this experiment is obligatory for all. The fingerprints of clients are duly passed on to the police if a rented car is stolen or involved in some other crime.

In 2006, Britain introduced biometric passports for its citizens, in which information about the passport holder is stored on a tiny computer chip. More than a million British citizens have already voluntarily acquired such documents.

However, the use of biometrics in official documents raises many questions: Where and how will the information on passport holders be stored? Who will have access to this information? Should any centralized body be established for overseeing this new program? And why should information on innocent people be collected at all?

There were no public discussions prior to the introduction of biometric passports, and now there are more questions than answers in this sphere. Technologies are developing at a rapid rate, but is anybody interested in hearing the public's opinion on the matter?

It would be expedient if the police and security services have precise instructions concerning reasonable limits and reasons before their entire populations are subjected to biometric technologies.

5. *Expansion of control over citizens by security services and police, and limitation of human rights.* Following the tragic events of September 11, 2001, some European countries have broadened

the practice of placing their citizens under the control of security services and police. Oftentimes this practice entails limiting individual rights as citizens can be checked and searched without any grounds, and information about them can be transferred to state bodies and law-enforcement organizations of other countries (for example, via Interpol and Europol). This practice can have grievous consequences for citizens of such countries: they can be denied employment or extradited from the country without citing any reasons. It must not be permitted that operational information, which once served as grounds for placing a person on record, should later ruin this person's life.

This kind of work with the population must be streamlined, and criteria for placing citizens on record with security services and police must be made legal and transparent. Also, rigid external control must be established over such procedures.

6. *The most acute aspect of control over the operation of security services and police is the protection of human rights in the course of operational work, especially in what regards intelligence.* There are numerous human rights violations in this field, particularly when citizens are provoked to commit crimes. Unfortunately, this is often done not to disclose a grave crime or neutralize terrorists, but simply to improve the crime detection figures of security services and police.

Therefore, the European countries should introduce strict limitations on such actions in their legislations.

7. *Freedom from discrimination and operation of security services (police).* Measures to combat terrorism must not be at variance with the ban on racial, ethnic, gender, religious or political discrimination.

While taking measures against members of specific terrorist and criminal groups, security services and police must see to it that these measures are not discriminatory and that they do not result in racial, tribal or ethnic persecutions.

Concern must be given over widespread cases of oppression and racial discrimination against people of certain ethnic origin. Such things happen both in Russia and other European countries.

States must guarantee the full exercise of their citizens' religious and cultural rights, as well as the protection of the right of detained persons not to be subject to arbitrary and continuous detention, as well as such basic freedoms as equality before the law, inviolability of the individual, and the right to a fair trial.

8. Operation of security services and police in a state of emergency and in other legal regimes limiting human rights. According to Clause 1 of Article 4 of the International Covenant on Civil and Political Rights, "In time of public emergency which threatens the life of the nation and the existence of which is officially proclaimed, the States Parties to the present Covenant may take measures derogating from their obligations under the present Covenant to the extent strictly required by the exigencies of the situation, provided that such measures are not inconsistent with their other obligations under international law and do not involve discrimination solely on the ground of race, color, sex, language, religion or social origin." Clause 2 of the same article specifies fundamental rights, without exception, even if there is a state of emergency in a given state.

Unfortunately, security services and police violate human rights en masse even in the legal regimes of counterterrorism operations.

States should take inventory of the laws that regulate the limitations on human rights in the course of implementation of security measures. Most importantly, they should ensure various controls over security services and police by parliamentary and governmental bodies.

Permitting any compromise on the observance of human rights by security services and police amidst new challenges and threats, we thus give criminals and terrorists a chance to achieve a moral and ideological victory that they themselves are unable to implement without our assistance.

Self-Determination: Between Law and Politics

Alexander Aksenyonok

The fallout from the geopolitical upheavals that shook the world at the end of the past century has yet to be fully appreciated, but their impact on world politics is becoming increasingly pronounced. Today, there is a growing gap between the generally recognized rules of international law and the new realities. The erosion of hitherto inviolable principles compels a review of the balance that has evolved between two tenets of international law – territorial integrity and the right to national self-determination – that are often in conflict with each other. How do these concepts apply in practice? What are the historical precedents? And finally, what are the objective standards of judgment needed for applying them?

Dramatic events, such as the chaotic disintegration of the Soviet Union, the civilized “divorce” between the Czechs and Slovaks, and the bloody breakup of Yugoslavia, amongst others, effectively repudiated the inviolability of postwar borders in Europe, which in 1975 was solemnly proclaimed in Helsinki. Furthermore, international recognition of the newly formed states legitimized the changes, regardless of whether they had occurred peacefully or through the use of force.

The violation of territorial integrity in Europe – regardless of the causes of the breakups – gave ethnic minorities within multi-

Alexander Aksenyonok, Doctor of Science (Law), Ambassador Extraordinary and Plenipotentiary of the Russian Federation (ret.), between 1995-1998 was a special envoy of the Russian Foreign Ministry for Bosnia and Eastern Slavonia. He is an Arabist and for many years worked in the Middle East.

ethnic states a powerful incentive for asserting their independence (including extreme forms of ethnic separatism). Interethnic tension can also be viewed as a byproduct of democratic transformations, for example, the decentralization of state governance, especially in Russia and East European countries.

To date, the strongest incentive for reviewing the concepts of “territorial integrity” and “national self-determination” are the dramatic turn of events that occurred in Kosovo in the late 1990s – and most importantly, NATO’s one-sided reaction to the situation. There is little doubt that this province of Serbia, with a predominantly Albanian population, is close to acquiring independence from the hands of the international community.

The primary question now is: Can Kosovo’s imminent independence be seen as a precedent in resolving other internal state conflicts, including in the former Soviet republics, or was it some sort of an exception in international practice?

The West replies categorically that it cannot be viewed as a new precedent, while Russia believes it can. Meanwhile, this problem has gone from being a subject of academic dispute to an explosive element of realpolitik. This applies above all to the ongoing conflicts over the so-called unrecognized states in the post-Soviet space – Transdnestr, Nagorno-Karabakh, Abkhazia, and South Ossetia.

The search for universal approaches to resolving complicated interethnic problems could be facilitated by a comparative analysis of Kosovo in the former Yugoslavia with Abkhazia and South Ossetia in the post-Soviet area. In undertaking this analysis, the author has advisedly put aside the historical aspects of these issues, since each nation and each ethnic group has its own “truth,” and it is all but impossible to resolve such conflicts by invoking the past.

KOSOVO’S PATH TO INDEPENDENCE

As a part of the former Socialist Federal Republic of Yugoslavia, Kosovo had the status of an autonomous region; later it was recognized as an autonomous province. Under the 1974 Constitution, Kosovo was empowered to elect its own parliament, form its own government and Constitutional Court, and it also acquired full

cultural and even economic autonomy. In other words, already in the 1970s-1980s, the scope of the province's regional authority was approaching the criteria that were later enshrined in the Council of Europe's Framework Convention for the Protection of National Minorities.

Kosovo did not become a hotbed of interethnic and interfaith tension until the late 1980s, when, on the initiative of the country's president, Slobodan Milosevic, the central government in Belgrade started "rectifying the mistakes" of decentralization. The resistance of the Albanian majority was originally of a political and civil nature, but gradually it transformed into an armed struggle.

Following the abolition of the province's extended autonomy, power was turned over to regional bosses appointed by Belgrade who relied on ethnic Serbian law enforcement and security structures. The Albanian population boycotted the new governing authorities, creating their own parallel administrative, educational, health, and social security agencies. In July 1990, a constituent assembly of the self-proclaimed parliament in Pristina adopted a declaration of independence and then the Constitution of the Republic of Kosovo. Alongside the consolidation of the political structures of the unrecognized state, the military organization of Albanian militants, known as the Kosovo Liberation Army (KLA), began to gather strength.

The next stage in the evolution of the Kosovo situation can be described as an unstable balance in the armed confrontation that by now had already begun. In response to mounting terrorist attacks against official structures, as well as the Serbian minority population in Kosovo, Belgrade began to build up its police presence there. When it became obvious that police forces were ineffective for dealing with the situation, army units were brought into Kosovo.

The international community became directly involved in the resolution of this internal Yugoslav problem following major clashes between regular troops and KLA militants in February 1998 in the Drenica area, which inflicted a heavy death toll, including among civilians. Large-scale military actions continued

for several months, placing the province on the verge of a humanitarian catastrophe. Responsibility for the crisis was laid exclusively at Belgrade's door, although in the majority of cases the Serbian side had only responded, albeit not always proportionately, to the armed provocations of the Albanian militants. Furthermore, it has never been proven that the Serbians were the ones who provoked the displacement of many refugees at that time. Subsequent conflicts involving the participation of illegal armed groups in Chechnya, for example, or more recently in Lebanon, show that terrorist organizations regularly use civilians as human shields, counting on the reaction of the international community.

Whatever the case, it is now all but senseless to apportion blame for the tragic events of 1998-99. In making a comparative analysis of the Kosovo precedent and the Georgian-Abkhazian or Georgian-Ossetian conflicts, there is another factor of greater importance: to objectively understand the nature of these conflicts and the role of extraneous factors.

The main goal of putting the Kosovo problem on the international agenda was to prevent a humanitarian catastrophe. But insofar as the West a priori placed all responsibility for the crisis on the Serbs and personally on Slobodan Milosevic, this became the keynote of all discussions at the OSCE, the Kosovo Contact Group, and the international conference in Rambouillet (France) on the political settlement in Kosovo (late 1998-early 1999). For its part, the Serbian leadership underestimated the seriousness of the situation, displaying shortsightedness during the negotiations. As a result, more subjective conditions evolved, thereby giving the North Atlantic Alliance a formal excuse for armed intervention.

Another specific feature of the Kosovo crisis is that the UN, as an instrument of political settlement, only became involved post factum. In treating the Kosovo case as "unique," Russia's Western partners at the Contact Group refer to UN Security Council Resolution 1244 and its violation by Milosevic. Such references were inappropriate at the very least. The UN resolution was adopted on June 10, 1999, that is, more than two months after Yugoslavia had begun being subjected to massive missile and air

strikes (the NATO military operation against the Federal Republic of Yugoslavia began on March 24, 1999). The main goal at that specific time was to end the air strikes that had placed one ethnic group, the Serbians, on the verge of a national catastrophe for the sake of “saving” another ethnic group, the Albanian Kosovars.

Resolution 1244 was in fact the price that had to be paid for ending the air strikes. It gave the UN and its Security Council a central role in the settlement process and sanctioned the presence of an international peacekeeping force in Kosovo (KFOR), as well as the deployment of the UN Interim Administration Mission in Kosovo (UNMIK). As a matter of fact, Belgrade was forced to cede a part of its territory and agree to foreign military presence – the NATO-led KFOR.

The UNMIK, defined under the aforementioned UN resolution as the supreme political and administrative authority in Kosovo pending the final definition of its status, has since been consistently pursuing a course toward Kosovo’s maximum isolation from Serbia and the creation of yet another independent state on the territory of the former Yugoslavia. Eduard Kukan, former foreign minister of Slovakia who in 2000-01 frequently visited Kosovo as a special envoy of the UN secretary general, described the situation as follows: “It was amusing to see former militants, who had recently changed their camouflage uniforms for civilian clothes, continue to press for full independence.”

Despite the declarations that a democratic, multiethnic society has been built in Kosovo, the situation for the Serbian minority remains critical. The exodus of non-Albanians has led to the creation of a mono-ethnic Albanian space. The outstanding problems have yet to be settled, which include the return of more than 200,000 non-Albanian refugees and temporarily displaced persons, provision of equal security and freedom of movement for ethnic minorities, and the creation of a genuinely multiethnic environment.

In pushing for independence, the Kosovo Albanians are striving to keep international interest in Kosovo alive by all means (including acts of violence against the Serbs). The aim is to demonstrate

that if the “independence scenario” does not materialize, bloody interethnic clashes, as in March 2004, will resume. In this situation, the West is seriously concerned by the unpredictability of its belligerent Albanian protégés, who are more than ready to use force – and not only against the Serbs. That would mean a total collapse of NATO’s policy in the Kosovo conflict with far reaching implications for other hotbeds of tension in the region. This explains the strong pressure that is being exerted on a weakened Serbia, which forwarded a compromise formula for the status of Kosovo: “More than autonomy, less than independence.”

Summing up this retrospective review of the Kosovo case, it is essential to note that the territory’s final status was predetermined by a combination of three internal and external factors:

- demands from the Albanian ethnic minority in Yugoslavia, accompanied by the use of violence, not to mention the use of blackmail against the international community;

- the coincidence of U.S. and EU interests, dictated by the simple considerations of political expediency, in removing Milosevic’s nationalist regime;

- the possibility, without the risk of a global confrontation, to impose that expediency scenario by military-political means amidst a new lineup of forces on the international arena.

THE CAUCASUS: SIMILARITIES, DIFFERENCES

The evolution of the Georgian-Abkhazian and Georgian-Ossetian conflicts, which have led to the formation of two so-called unrecognized states, has a number of similarities with the Kosovo case. Meanwhile, the differences between them only highlight the need for a clear-cut definition of universal principles in resolving such internal state conflicts.

In the late 1980s, unitary states were introduced by brute force in both instances. Smoldering interethnic conflicts flared up with new intensity when the central governments abolished the broad privileges that had been enjoyed by ethnic minorities both in a federal state, Yugoslavia, and in a constituent member state of the

Soviet Union, Georgia. In other words, South Ossetia and Abkhazia began to break away at a time when Georgia had not yet become an independent state. It is important to bear this in mind at a time when Georgia continues to insist on its territorial integrity.

In 1989-90, well before the breakup of the USSR, the Supreme Soviet of the Georgian Soviet Socialist Republic (SSR) passed a series of resolutions abolishing the Soviet republic's 1978 Constitution and restoring the 1918 Constitution of the Georgian Democratic Republic, which ruled out the existence of regional autonomies. In response to that move, in July 1982, Sukhumi declared the abrogation of the Constitution of the Abkhazian Autonomous Republic as part of the Georgian SSR and the restoration of the 1925 Abkhazian Constitution that proclaimed the sovereignty of Abkhazia.

The events in South Ossetia followed a similar scenario, when in late 1989 the Georgian authorities brought police forces into Tskhinvali, while in November 1990 Georgia's Supreme Soviet abolished the South Ossetian Autonomous Region, which sparked the breakout of hostilities. Against that backdrop, on January 19, 1992, a referendum was held in South Ossetia in which the majority of the population voted for independence and accession to Russia. A few months later, the Supreme Soviet of the South Ossetian Republic adopted an Act on State Sovereignty.

Just as in Kosovo, armed conflicts on the territory of the former Georgian SSR took a heavy toll in human lives and had devastating humanitarian consequences for the Georgian and Abkhazian populations. Of 550,000 citizens of pre-war Abkhazia, 7,000 were killed, with 200,000 to 250,000 fleeing the region, mostly ethnic Georgians. Another parallel with Kosovo is that both conflicts were frozen with the involvement of external forces – in the case of Kosovo, NATO member states – with Russia playing a marginal peacekeeping role; and in the Georgian-Abkhazian conflict, it is Russia that took the main initiative with the West playing a marginal role. Importantly, both sides formally agreed to political settlement mechanisms, which were laid down in an array of international documents.

Over the past seven years, Kosovo has been formally under the jurisdiction of the UN, while UN Security Council Resolution 858 (1993) also applies to the situation in Abkhazia. This resolution established the UN Observer Mission in Georgia (UNOMIG), which is still active. Furthermore, the UN is involved through the special envoy of the UN Secretary General who heads a coordinating council with the participation of the OSCE, Russia, the UK, Germany, France, and the U.S. The collective peacekeeping force (made up predominantly of Russians) deployed in the zone of the Georgian-Abkhazian conflict has a CIS as well as a UNOMIG mandate (under UN Security Council Resolution 1666, March 31, 2006).

As for South Ossetia, here too a quadripartite peace mechanism known as the Joint Peacekeeping Force and the Joint Control Commission (JCC), which was instituted with Russia's mediation in 1992, is supplemented by the efforts of international organizations. An OSCE mission has been working in Georgia and South Ossetia since December 1992, while EC representatives have been involved in JCC operations in an observer capacity since 1999.

But the main similarity between these scenarios is the political will of the mono-ethnic community (ethnic majority) in Kosovo, Abkhazia and South Ossetia. The referendums sponsored in these regions reaffirmed this will, and far more convincingly than the EU sponsored plebiscite on Montenegro, for example, which the international community recognized.

Statehood on these territories evolved in the same way and within the same timeframe as in all post-Soviet republics. Geopolitically, Abkhazia, for more than 10 years now, has been a de-facto independent state with all the trappings of a state that conforms to democratic standards. It even has its own army and law-enforcement structures. Its economy is self-sufficient and not dependent on Georgia. The people of Abkhazia see themselves as citizens of an independent state, and make their future economic prosperity contingent on the republic's integration into Russia. At the present stage, recognition of Abkhazia's independent status is of paramount importance.

The majority of Abkhazians perceive any denial of their right to independence as the “enslavement” of an entire nation “within Stalin-era boundaries.” In a conversation with Thomas de Waal, a Caucasus expert and project coordinator for the Institute of War and Peace Reporting (IWPR) in London, Sergei Bagapsh, the president of the unrecognized Republic of Abkhazia, stressed that Abkhazia has more grounds for acquiring the status of an independent state than Kosovo does because the former was forcibly incorporated into Soviet Georgia. While acknowledging that this argument was not incontestable, de Waal, writing in *The Financial Times*, admits that he has not met a single person in Abkhazia who envisioned it as ever becoming a part of Georgia.

The strive toward reunification with Russia is especially strong in South Ossetia, which is rather weak economically and populated by people who have relatives in North Ossetia [which is part of Russia – Ed.]. The South Ossetians see themselves as being forcibly separated from their “blood brothers” due to unfair subjective and objective historical events.

THE POSITION OF “MOTHER COUNTRIES”

For all the similarities between the situations in Kosovo, Abkhazia and South Ossetia as de-facto independent states (UN jurisdiction over Kosovo only formally conceals this status), there remains one rather substantial difference – specifically, the difference between the positions of Serbia and Georgia, i.e., the ‘native people,’ or so-called ‘titular nations.’

The final decision over the status of Kosovo is a serious test for the democratic forces of Serbia that replaced the authoritarian regime of Slobodan Milosevic. The new governing authorities are between a rock and a hard place: to agree to the separation of the historical cradle of Serbian culture and Orthodoxy means courting the danger of being overthrown by a wave of Great Serbian nationalism. On the other hand, to resist outside pressure in granting independence to Kosovo means losing the chance to open negotiations on EU membership – the direction that all other Balkan countries, including former Yugoslav republics, are now

moving. Thus, just as in the case of Montenegro's separation from Serbia, admission to the EU is a good incentive for completing the 'Balkanization' process.

Yet, for all the complexity of the situation, the Serbian leadership pursues a fairly sensible, well-balanced line, taking into account the hard legacy of the Milosevic era, as well as the current situation in and around Kosovo. In searching for a compromise solution, it prioritizes high democratic standards in guaranteeing the legitimate rights of Kosovo's Serbs, protection of Orthodox sacred places, and decentralization of power. These problems have not been resolved, despite the numerous declarations and promises by UN administrators and KFOR command. These issues are now at the top of the agenda amidst ongoing negotiations between the Serbian and Albanian sides with the mediation of a special representative of the UN Secretary General in Vienna.

The negotiating process on Abkhazia and South Ossetia, however, is shaping up quite differently. Tbilisi is standing firm on Georgia's "territorial integrity," but within the old Soviet borders, offering the Abkhazians and Ossetians "broad autonomy." Sukhumi and Tskhinvali have made any political settlement conditional on the international legitimization of their de-facto independence as the logical conclusion of the breakup of the Soviet Union with full guarantees for the rights of ethnic Georgians.

All indications suggest that the chances for arriving at a solution that is acceptable to both sides are remote, while the overall situation continues to worsen. Tbilisi's line of conduct, always unpredictable and meandering, is becoming utterly destructive under the leadership of Mikhail Saakashvili. There are increasing violations of current agreements and the security regime in the conflict zone; offensive weapons are being constantly built up; peacekeepers are becoming a target of provocation while unjustified demands are being set on them. Finally, bellicose rhetoric is beginning to grow louder. All of this gives the Abkhazians and Ossetians reason to believe that the Georgian leadership has decided on the use of force; to this end it is necessary, above all,

to eliminate the existing settlement mechanisms and compromise the Russian peacekeeping mission. The Georgian parliament's resolution, *On Peacekeeping Forces in Conflict Zones*, makes it incumbent on the government to implement measures to ensure the earliest possible withdrawal of Russian peacekeepers from Abkhazia and South Ossetia, abrogate the relevant international treaties and structures with their subsequent replacement by a new format, including the deployment of an "international police force." Meanwhile, the ongoing rapprochement between Georgia and NATO further encourages radical elements within the country's leadership.

The experience in peacekeeping operations in other parts of the world shows that their successful completion is impossible without each party to the conflict maintaining an atmosphere of trust and refraining from steps that could be misinterpreted. That was the atmosphere in which Eastern Slavonia was reintegrated into Croatia under the auspices of the UN Interim Administration and with the close involvement of Russia, which had taken part in both the military and civilian components of the operation.

Another condition for a successful peacekeeping operation is the voluntary acceptance of an imposed settlement by all parties involved. These operations are known as 'peace enforcement' and, as a general rule, involve 'nation building.' A case in point is the Dayton Peace Agreements on Bosnia and Herzegovina that brought about the end of the civil war in the former Yugoslavia (1992-1995). The NATO-led multinational force that was deployed there in 1996 had a tough mandate, which included the use of force, and guaranteed the implementation of these agreements. That mandate provided additional leverage to the chief administrator who had been entrusted by the international community with special functions, similar to those of a governor general.

Peacekeeping operations in Abkhazia and South Ossetia are based on a narrower mandate and an international mechanism that does not provide for the imposition or enforcement of specific solutions on any of the parties involved. In both cases, Russia acts only as a facilitator in settling conflicts. The peacekeepers'

mandate is reduced to preventing engagement of forces and maintaining the security regime.

Considering the differences in the scope of mandates and settlement mechanisms, the attacks by the Georgian leadership against Russia, including accusations of obstructing the peace process, point to a pronounced attempt to impose at any price a different format providing for enforcement functions with respect to the “separatists.” At the same time, it is well known that the mandate cannot be changed without the consent of both sides. But neither Abkhazia nor South Ossetia will give such consent, fearing, and not without reason, that the withdrawal of Russian peacekeepers could have disastrous consequences for the civilian population, causing widespread destabilization. The unrecognized republics see the Georgian parliament’s resolution as Tbilisi’s intention to resolve the problem by force.

The current ethnic-territorial conflicts in the South Caucasus are dangerous insofar as they can grow into a permanent hotbed of tension. Georgia, in its striving to have its way no matter what, is presumably acting on the assumption that if the restoration of its territorial integrity is delayed for another few years, this could perpetuate the status quo, which would be subsequently recognized by the international community. There are also internal political considerations involved: it is necessary to bolster the ruling regime, which is going through serious difficulties, with time-tested nationalist arguments. But just as in the Kosovo scenario, external factors play a crucial role in the South Caucasus as well.

The evolution of the situation around the unrecognized states of Abkhazia and South Ossetia reflects the logic of the old “zero sum game,” but in new, non-confrontational conditions. Tbilisi’s defiant, provocative actions with respect to Russian representatives would hardly have been possible without open support or connivance on the part of the United States. If Washington’s policy is really aimed, in defiance of Russia, to steer Georgia toward full NATO membership, even as it turns a blind eye to its failure to meet the established standards and criteria, Tbilisi cannot fail to construe this as *carte blanche* abilities for a one-sided resolution

of the problem of Abkhazia and South Ossetia. This incorrect interpretation of the nature of international support will continue to encourage the Georgian leadership to take ill-considered actions, which is fraught with escalating tensions throughout the region.

As the conflict worsens and the sides toughen their negotiating positions, the Russian Federation as a neighboring state that is deeply involved in the peace process could end up in a rather delicate situation. Because of Russia's geographic position, the outcome of the conflict in the South Caucasus is probably more critical for it than the outcome of the Kosovo problem is for Europe.

Today, Russia's political position is based on the recognition of two principles – territorial integrity, with the proviso that in the case of Georgia it is just a “possibility,” not a “politico-legal reality,” and the right to self-determination. The international community fully endorses the last principle. In this way, Moscow indicates that the principle of territorial integrity is not absolute and may not be applied automatically.

This two-pronged position leaves some room to maneuver. But the field is narrowing more and more, and there is an increasing danger of Russia being held responsible by both sides – Abkhazia and Ossetia on one hand, and Georgia on the other – for freezing the conflict.

The delicacy of the situation is that either outcome – in favor of territorial integrity or in favor of secession – involves both advantages and disadvantages for Moscow. But in neither case are there any absolute advantages.

In the boiling ethnic cauldron in the Caucasus, where everything is closely interconnected and interwoven, the use of force to coerce Abkhazia and South Ossetia to return to Georgia's fold will imminently create new hotbeds of tension in southern Russia – in North Ossetia, Adygeya, Chechnya, Karachayevo-Cherkessia, and possibly beyond. In such a situation, there is no way Russia can count on Tbilisi's loyalty. At the same time, responsibility for the fate of ethnic minorities also has a moral dimension for Russia. The Russian state, just like any other state, is obligated to defend

the interests of its citizens. Moreover, as is already known, a substantial part of Abkhazia's and South Ossetia's population (who were denied the right to a free and democratic expression of their will either in the Soviet Union or later in independent Georgia) are in fact Russian citizens.

To date, nobody has successfully explained to the Abkhazians and Ossetians why the Kosovars and Montenegrins have a right to secede but they do not. All references to the "uniqueness" of the Kosovo case are unconvincing. Furthermore, if Kosovo's independence is to be formalized *de jure*, the paradoxes of *realpolitik* on the ethnic-territorial issue will be too obvious even to non-professional politicians. On the one hand, the United States and Europe, as punishment for Serbia's uncooperative and "despotic" regime, encouraged separation on its territory, but on the other, the same group of influential states continues to deprive other peoples of the right to secession by supporting the "democratic" Georgian regime, which is amenable to them.

Whatever the case, in the context of post-confrontational politics, the following question on the international agenda is becoming increasingly important: Are there any objective criteria for striking the right balance between the principles of territorial integrity and national self-determination?

Needless to say, the idea of secession for secession's sake is flawed, and will ultimately lead the world to chaos. However, there are other forms of self-determination, such as, for example, cultural autonomy, federative and confederative designations, ethnic-territorial formations with different degrees of economic independence, and finally, interstate integration with voluntary delegation of part of national sovereignty to the center. But in all of these cases, the crucial conditions are the high degree of trust between a state-forming nation and an ethnic minority, common sense displayed by the central governing authorities, and their ability for guaranteeing a worthy life to their citizens.

Canada and Spain may serve as models for the civilized resolution of ethnic problems. The results of a recent referendum in Quebec, for example, showed that the French-speaking popula-

tion trusts the historical state in which it lives. In Spain, greater autonomy was handed to Catalonia, which acquired the status of a separate ethnic entity within the country. This shows that self-determination does not necessarily mean the acquisition of state independence.

At the same time, the international community cannot ignore cases when, due to different interethnic problems – historical, psychological, or economic in nature – secession by an ethnic minority is more in harmony with historical reality than is the preservation of its uncertain status as an unrecognized state. The ethnic-territorial conflicts in Kosovo, Abkhazia and South Ossetia all fall into this category. Responsibility for the situation that has evolved is ultimately borne by the central governments that alienated their citizens with their arrogant chauvinistic policies. The main criterion here should be an international consensus on the legitimacy of the secession of ethnic minorities, based on generally recognized democratic and humanitarian standards.

East Asia and Russia's Development Strategy

East Asia positions itself as a region that is rapidly developing economically and non-uniform politically. Despite the rapid economic growth of the East Asian countries, together with their increased role in global politics, Russia has not yet provided convincing proof of its ability to use its geographical position in the region for its national development. Moscow often disregards geopolitical changes occurring in that part of the world and perceives the dynamics of the situation in East Asia only through the prism of its rivalry with the U.S. Also, Russia's economic strategy fails to take into account the great economic progress in the region.

Irrespective of Moscow's reaction, East Asia's dynamic and intricate development will objectively have an increasing influence on the development of Russia. This will affect, first of all, its East Siberian and Far Eastern regions, causing us not only to adapt to challenges and opportunities coming from East Asia, but also to look for mechanisms to influence the region in a way

This material was prepared as part of the project *The World Around Russia: 2017*. The project is being implemented by a group of experts, headed by Sergei Karaganov, from the Council on Foreign and Defense Policy, the Department of International Economics and International Politics of the Higher School of Economics, the Institute of Strategic Studies and Analysis (ISSA), the Institute of Europe and other organizations, with the support of Rio-Center. The main author of this material is **Vassily Mikheyev**, Corresponding Member of the Russian Academy of Sciences.

advantageous to Russia. The most important task in this context is working out a Big Asian Strategy that would link internal objectives and development mechanisms with the East Asian factor.

The main factor of political and economic change in the region is China. The growth of China's economic might and, therefore, political influence causes leaders to change their traditional view of "the Chinese factor" and adapt to its new global and regional positioning. China's integration into East Asian political and economic processes, as well as the way it is perceived by regional actors, has not been smooth. This reflects the difficult and contradictory nature of the deep transformations taking place in East Asia, where the rivalry for national leadership and competitive advantages is intertwined with ideology and the practice of multilateral cooperation.

It was the dynamism of the Chinese economy and policy that was responsible for increasing Russia's interest in East Asia, as well as changing the structure of its ties with the region. Over the last decade, China has become Russia's main trading partner in the region, leaving behind Japan and South Korea. In the next five years, China stands a good chance to become also the largest investor in the Russian economy.

EAST ASIA: STATE, TENDENCIES AND PROBLEMS

In 2001-2006, average annual GDP growth rates in individual countries differed essentially: from 1.5-2.0 percent in Japan to 9.5-10 percent in China. China also featured the highest growth rates in foreign trade — about 30 percent a year. The aggregate East Asian GDP stands at 75-80 percent of the GDP of the United States and the European Union. Three countries of Northeast Asia — Japan, China and South Korea — account for more than 90 percent of the regional economy. Japan, which has been developing slower economically than China, still remains the regional leader in absolute economic terms and through its influence on the global economy. Japan's GDP

(about 5 trillion dollars), which is approximately 45 percent of the U.S. GDP, is more than double that of China. Yet China is ahead of Japan in the volume of foreign trade (1.6 trillion dollars in 2006).

From a military and political standpoint, East Asia is divided into different unions. The U.S. maintains special relations with Japan and South Korea; ASEAN is another political and economic structure; other countries also play unique roles in the region: China, for example, is a member of the Shanghai Cooperation Organization (SCO) beyond the geopolitical borders of East Asia; North Korea (formally a member of a military-political union with China); and Mongolia, which is an observer at the SCO. The 2000s have seen growth in defense spending in East Asia to 1 percent of the GDP in Japan and 2.5 percent in China. The North Korean economy is 70 to 80 percent oriented to meet its defense needs. Japan leads the region in absolute volumes of defense spending, which is now 10 to 15 percent ahead of China.

Stability tendencies will prevail over destabilization tendencies in the political situation in East Asia. Due to specific interests of interaction in the economy, the energy sector, and in efforts to counter terrorism and atypical threats (natural cataclysms, bird flu, etc.), old rivalries between the main actors in the region will not develop into direct military-political conflicts. The main factor holding back a possible deterioration of political relations between China and the U.S., and China and Japan will be greater economic interdependence between these counterparts – under any scenario of the aggravation of the situation.

East Asia is developing an increasing need to pool together the economic resources of Japan, China, South Korea and the ASEAN countries. For the first time in history the liberalization and marketization of the Chinese economy may create prerequisites for ***regional integrative co-development***. However, some things stand in the way of the parties' rapprochement, including the persisting imbalance between military-political forces, the perception of China by the U.S. and Japan as a politically "alien" actor,

although they still view it as an economically “friendly” market “partner-rival,” and last but not least, the preservation by the Chinese Communist Party of its monopoly on power.

The main ***threats and challenges to security*** in East Asia are:

- the North Korean nuclear problem;
- territorial disputes involving Japan, Russia, South Korea, China, and several ASEAN countries in the South China Sea;
- Chinese-Japanese and Korean-Japanese disagreements over matters of history, including visits by Japanese leaders to the Yasukuni Shinto Shrine;
- the Taiwan question;
- energy security of Northeast Asia;
- new and non-conventional threats, including terrorism, piracy, ecological and natural disasters, epidemics, etc.

Along with destabilization factors, there are the following ***factors of stabilization*** of the political situation in East Asia:

- the six-partite talks concerning North Korea in Beijing;
- the search for ways for multilateral regional mutual support in energy matters;
- cooperation in combating new and atypical threats;
- multilateral economic formats now emerging in East Asia: the Asia-Pacific Economic Cooperation, “ASEAN Economic Community,” “ASEAN Plus Three (Japan, China and South Korea),” “ASEAN Plus China,” “ASEAN Plus Japan,” “ASEAN Plus South Korea,” the ASEAN Regional Forum (ARF), and the East Asian Community (EAC) set up in late 2005, which includes the members of “ASEAN Plus Three,” Australia, New Zealand, India, and Russia as an observer.

China plays the role of a regional “disturber of the peace” as it seeks to strengthen its political influence on the basis of its growing economic might, its important and sometimes even leading role on world markets, and the active expansion of its capital abroad, which began in the mid-2000s.

India, entering the geo-economic and geopolitical space of East Asia, is becoming a new factor in the changing situation in the region. India seeks to expand the horizons of its domination

in the Indian Ocean by joining the processes underway in Southeast Asia and, later, in the whole of East Asia. To date, the influence of the Indian factor has not been great. India seeks to consolidate its regional positions by normalizing relations with potential opponents, namely Pakistan and China, and establishing a new relationship with the U.S.

EVOLUTION OF THE REGION BY 2017

In the next 10 years, East Asia will continue to build a new integration model that is different from that in the EU. The East Asian model focuses not so much on the reduction of customs duties and the creation of a free trade zone (although the region will continue its efforts toward stage-by-stage tariff liberalization within the frameworks of the APEC, ASEAN and ASEAN Plus Three by 2010-2020), as on integration in more open sectors of the knowledge economy, compared with the traditional economy, and on financial interaction in order to prevent a recurrence of the Asian financial crisis of 1997-1998. In 2017, East Asia will still be no closer to the creation of a common currency despite the increased discussions on this issue. However, it will increase interaction between national central banks within the framework of swap agreements in case of a currency and financial crisis and will broaden the sphere of application of the Asian Currency Unit (ACU) – a currency basket, i.e., a weighted index of East Asian currencies – within the framework of the Asian Development Bank.

In the security field, emphasis will be made not on the dismantling of the present military-political structure in East Asia, based on the American-Japanese and American-South Korean military-political unions. Nor will the emphasis be on the creation of any “counterbalances” involving China. Rather, emphasis will be placed, first, on the formation of new multi-lateral regional security structures, which could stem from the six-partite talks on the North Korean nuclear problem. Secondly, it will be based on interaction in combating new and atypical security threats.

Unresolved territorial problems and historical issues will have less influence on relations between East Asian neighbors than they do today. In a more distant future, they will be resolved in a “natural” way through the joint development of disputed territories and regional integration.

The increased role of new and atypical security threats in national strategies will gradually modify the United States' military unions with Japan and South Korea, making them more open to cooperation with other countries in the region, including China and Russia.

Chinese-U.S. relations will be characterized, on the one hand, by greater economic interdependence of American and Chinese capital, and on the other hand, by increased mutual concern: Washington is concerned by the non-transparent growth of China's military might, while Beijing is concerned over the proliferation of the “Chinese threat” theories. In both China and the U.S. there will be competing voices over these issues: some will strive to intensify mutual suspiciousness, while others will seek to ease them, each according to their own corporate interests. However, the role that economics, new threats, poverty, natural disasters, etc. play will have a positive influence on Chinese-U.S. relations. By 2017, these relations will most likely be characterized by a higher degree of interaction and lesser hostility than today.

Chinese-Japanese relations will develop according to a similar scenario, but with some peculiarities. China and Japan will not fully change their negative perception of each other due to their different interpretations of history. Nevertheless, the coming to power in 2012 of the “fifth generation of Chinese leaders,” many of whom have received their educations in the West, and the rejuvenation of Japan's political elite thanks in large part to politicians of the postwar generation, can greatly reduce the atmosphere of historical hostility by the beginning of the 2020s in favor of interaction in implementing mutual interests. In the interest of cooperation there will evolve the creation of a tripartite U.S.-Japan-China format to discuss matters of regional security and development.

If no progress is made at the negotiations on the global liberalization of trade, this factor will stimulate economic regionalism, including in the ASEAN and ASEAN Plus Three formats.

China will become increasingly closer to the West as it deepens its market reforms and integrates into the global economic, informational and political space. The following factors will promote these changes:

- growth of interdependence of Chinese and international business interests;
- changes in the composition of China's political elite, due in large part to politicians who have received their education in the West, rather than in the former Soviet Union (the Jiang Zeming generation) or in China (the Hu Jintao generation);
- democratization of Chinese society on the basis of a broader rule of law and a socio-economic "strategy of non-destabilizing inequality" ("harmonic society");
- cooperation with the international community in combating terrorism, WMD proliferation, and new and non-traditional threats.

China will retain high economic growth rates at 9-9.5 percent, making the East Asian region the fastest developing in the world. By 2017, China's GDP will reach the present GDP level of Japan. This forecast is based on the growth of domestic demand, which started around 2005 due to the urbanization of more than 700 million Chinese peasants and a rapid growth of the middle class. This tendency has revoked the description of China as a "world factory," which was correct in previous years when the Chinese economy was developing largely on the basis of export-oriented production. Now China can rather be described as something like a "vortex of consistent demand."

At the same time, China will face threats and risks that, under certain conditions, may bring about a deep crisis and a total downward revision of the forecasts. Domestic and external economic factors are more likely to provoke a deep crisis than external political factors. In the short term, the social, financial and energy sectors are the most vulnerable spheres. Other vul-

nerable areas include the Taiwan question (in the medium term) and ecological concerns (in the long term).

In the next decade, the Chinese Communist Party will preserve its monopoly on power. However, external and internal factors will force the CCP to conduct a political reform in the country. In particular, the West – in its competitive struggle against China on the global markets – will exploit the fact that the CCP enjoys a political monopoly. The internal factors include: the already mentioned growth of the middle class, as well as a class of Chinese bourgeoisie, which want their political interests to be taken into account as well; the decline of the CCP's authority among young people; the merger of the partocracy and the oligarchy, which requires a broader structure than the CCP for harmonizing political and economic interests between different groups; and the deepening of social stratification.

Relations between Beijing and Taipei will preserve a status quo, although occasionally their relations will be marked by political disturbances, together with intensified efforts on Beijing's part to integrate Taiwan into the rapidly growing Chinese economy.

Simultaneously, several factors will serve to increase international tensions. The growth of defense spending by China – with a view to acquiring the status of a global superpower – will provoke countermeasures by Japan and the Japanese-U.S. military union. Other countries in East Asia will increase their defense spending as well. Although the “status” nature of the new stage in the arms race will not lead directly to military conflicts, it will increase rivalries and threaten cooperation in international relations in East Asia.

The Korean problem will remain unresolved, continuing to be a slow-developing conflict with occasional disturbances caused by North Korea's provocations by means of missile tests, flare-ups in the Demilitarized Zone, rumors about nuclear test preparations, etc. However, the possibility of a war on the Korean Peninsula is unlikely. Technologically, North Korea will not be able to develop nuclear weapons and long-range missiles

of its own, and will continue resorting to tactics of nuclear bluff and blackmail to ensure the survival of the present political regime. The demise of North Korean leader Kim Jong Il may entail radical changes in the country, although not necessarily.

The India factor will have a gradually increasing effect on East Asia; however, by 2017, India, even having consolidated its positions in South Asia, will nevertheless be unable to compete with traditional leaders either in Southeast or Central Asia. Therefore, it will not be able to play the role of a counterweight to Chinese and Japanese influence in the East Asian economic and political space.

India, relying on its growing influence in South Asia, will try to use the EAC mechanisms to gain access to East Asia. These efforts will run up against stiff opposition from China, which will be one of the reasons why the EAC will remain a rather amorphous political organization.

India's attempts to consolidate its positions in East Asia will complicate the configuration of its relations of cooperation and competition with China. At the same time, India and China will seek to avoid military clashes over unresolved territorial and political problems (Pakistan, Kashmir, Tibet). The two countries will develop mutual trade, cross-border cooperation and interaction in the energy sphere. At the same time, competition and opposition between them will increase as well.

The main spheres of Indian-Chinese rivalry will be:

- relations with the United States. India will seek closer relations with the U.S., compared with China, playing on two factors: "Indian democracy" as a counterweight to "Chinese socialism," and the help that India can give to the U.S. in "restraining" China;
- global sources of financing the economy. India will try to attract financial flows now going to China from the world financial centers (including from Japan);
- influence on neighbors. India will retain its monopoly on the control of the situation in the Indian Ocean, while simultaneously attempting to enter the zone of Chinese influence in Southeast Asia;

- energy and the “new economy.” India will seek to oust China from international energy and high-tech markets where it is more advantageous to India than interaction with China;

- military cooperation with Russia. For India it is important to become a preferential partner of Russia in the military-technological field. At the same time, India will use to its advantage Russian-American and Russian-European competition on the South Asian arms market.

In the tripartite Russia-India-China format, India will make emphasis on the development of bilateral ties. India can use both bilateral and multilateral relations in the “triangle” for applying political pressure on the U.S. in the case of disturbances in Indian-U.S. relations.

India will emphasize bilateral relations also in its policy toward the SCO, seeking to gain competitive advantages on the Central Asian hydrocarbon market. India does not view China and the Central Asian member countries of the SCO as “truly democratic” and will preserve its status of observer in the organization to monitor the level of energy cooperation in Central Asia, as well as China’s behavior.

China’s rapid economic growth, its transformation into a regional leader in East Asia, and the possibility of a Chinese-American rapprochement will increase the “competitive spirit” and “motivation for rivalry” in India’s policy, bringing about fluctuating changes in India’s behavior.

The future prospects of the *Shanghai Cooperation Organization* depend on the organization’s readiness to adjust its development strategy. It remains an open question whether the SCO can shift the emphasis in its efforts on ensuring social and political stability in Central Asia on the basis of economic growth and the development of democratic institutions and civil society, despite the importance of the struggle against terrorism and other new threats and despite the usefulness of military cooperation. If it fails to do so, by 2017 its activity may grow increasingly vague and uncertain, which will weaken its regional political potential and will cause Russia and China to implement their interests in

Central Asia outside the SCO frameworks: Russia will seek to strengthen the Collective Security Treaty Organization and the Eurasian Economic Community (EurAsEC), while China will seek dialog with NATO. This, in turn, will increase the military-political imbalance in Central Asia, caused by the absence of a clear-cut division of labor between the SCO, including China, and the CSTO Plus EurAsEC, which actually comprises all the SCO member countries, except for China. A persisting imbalance in Central Asia, where the U.S., Japan and India have displayed their interest in establishing their own dialogs with countries in the region without the participation of Russia and China, may turn Central Asia into a zone of rivalry – as opposed to interaction – between the large countries. Such developments will not meet the interests of ensuring Central Asian security through mechanisms of cooperation and co-development.

THE RUSSIA FACTOR: RISKS AND OPPORTUNITIES

Despite Russia's geo-economic position as a bridge between the European and East Asian integration zones, this afctor does not play a decisive role in setting its national development priorities. Its economic strategy lacks "spatial economic thinking" that would enable it to see the problems of the depressive regions in Eastern Siberia and the Russian Far East in a supra-national, geo-economic context, rather than within the narrow framework of state borders. Also lacking is a "two-vector" development model that would allow for the orientation of the Russian economy, extended in space, toward parallel integrative interaction with the European Union and East Asia.

By 2017, these shortcomings in Russia's vision of its place in the East Asian region may result in missed economic gains, not to mention political troubles. As China consolidates its economic and political positions in the region, East Asia's political and economic interest in Russia will tend to decline.

On the other hand, as Russia becomes a major actor in global energy supplies, China, Japan, India and South Korea will

display a growing interest in energy resources, energy assets and energy cooperation with Russia. The ASEAN countries will seek to use Russia's energy and, consequently, political influence as a counterweight to the influence of the U.S., China and Japan in Southeast Asia.

The interest in Russia as a transport space between Europe and East Asia will depend on Russia's policy in developing its transport infrastructure, above all in Eastern Siberia and the Russian Far East.

The interest in Russia as a partner in the knowledge economy will continue to be selective and will depend on Russia's policy in the realms of research and technology. It also depends on its ability to revive Russian science, which from about 1990 until the turn of the century was severely hit by a "brain drain" and conceptual losses.

The interest in Russia as a possible recreational zone for East Asia's growing and increasingly rich population remains hypothetical and will depend on Russia's actions and on whether it is ready to view itself as a global recreational area.

The main *risks for Russia in East Asia* in the next decade will be as follows:

- as China integrates into the global and regional economy, ***Russia may find itself farther from the West – most importantly, the U.S. and Japan – than China.*** This factor will reduce Russia's competitive advantages and weaken its political positions;
- Russia may end up outside the integration processes in East Asia, involving Japan, China and South Korea;
- Russia may yield to the political temptation to play on Chinese-U.S. and Chinese-Japanese differences, seeking tactical gains but overlooking strategic prospects;
- Russia still runs the risk of missing the opportunity to use the six-partite talks on the North Korean nuclear problem for joining multilateral mechanisms of security and cooperation in Southeast Asia, which are emerging on the basis of these discussions;
- Russia may continue misinterpreting the main threats from East Asia as concerns the prospects of a demographic or eco-

nomic “invasion” of its East Siberian and Far Eastern regions. At the same time, it fails to notice that the main tendencies in East Asia’s development sharply minimize such threats, putting into the foreground the threat of missed benefits because of Russia’s nonparticipation in regional integration processes.

The main *opportunities for Russia in East Asia* include:

- it is important for Russia to use the long-term interest displayed by other countries in its energy sector to create an East Asian hydrocarbon market on the basis of Russian energy resources;

- it is vital for Russia to develop a new integration model for its parallel co-development with the European Union, the U.S. and Northeast Asia as a locomotive for the entire East Asian economy;

- it is important for Russia to continue participating and increasing its activity and initiative in economic and political formats in East Asia;

- Russia must continue deepening national market-oriented and democratic transformations and large-scale cooperation in East Asia with the U.S., Japan and China, while taking the initiative to find and use areas where the interests of all these nations coincide in order not to fall behind China in terms of relations with the U.S. and Japan. In this context, it is important for Russia to build permanent strategic dialogs with the U.S., Japan and China on East Asian issues and thus to prevent the formation of a tripartite American-Japanese-Chinese regional partnership without Russia.

ESSENTIAL RUSSIAN RESOURCES

**Four critical English-language journals
from Russia which no library can afford
to overlook!**

International Affairs

The voice of Russia's Foreign Ministry. Offers unique, first-hand analysis of major foreign policy issues facing Russia and NIS. Available in print, microform and online. ISSN 0130-9641. 6/yr. Subscription: Individuals \$59; Institutions \$419.

Military Thought

Leading theoretical journal of Russia's Ministry of Defense. Provides critical insight into current trends in Russian military doctrine and planning. Available in print, microform and online. ISSN 0869-5636. 6/yr. Subscription: Individuals \$106; Institutions \$523.

Social Sciences

Indispensable overview of contemporary Russian scholarship in the social sciences. Selected works from over 25 Russian-language journals of Russian Academy of Sciences. Available in print and online. ISSN 0134-5486. 4/yr. Subscription: Individuals \$80; Institutions \$332.

Far Eastern Affairs

The journal of the Institute of the Far East, a renowned Moscow think-tank researching developments in China, Japan, and the Asia-Pacific region. Available in print and online. ISSN 0206-149X. 4/yr. Subscription: Individuals \$79; Institutions \$259.



3020 Harbor Lane North
Minneapolis, MN 55447 USA

tel: + 1(763) 550-0961

fax: + 1(763) 559-2931

e-mail: eastview@eastview.com

The 21st Century Mafia: Made in China

Vladimir Ovchinsky

China, which is rapidly becoming a leader in global development, is now the talk of the world. However, the positive manifestations of this diverse phenomenon are closely linked with negative ones. For example, as China continues to consolidate its leading positions in the global economy, Chinese organized crime is expected to broaden its presence in global criminal links. This is of tremendous concern for Russia and the world.

THE “TRIADS” AND REFORMS

Many observers believe that information concerning the negative processes in contemporary China is classified, but this view is largely exaggerated. Chinese criminologists (including Liao Ping, He Bisong, Xin Yan, and others) have conducted in-depth studies into organized crime in their country, and the results of these studies have been translated into other languages, including Russian. Furthermore, Chinese officials from the Communist Party and law-enforcement bodies eagerly share their information about the criminal situation.

Analysis of these studies suggests that any shift from a command economy to a market economy brings about, as a negative side effect, an upsurge (or rather an outburst) of organized crime and corruption. China launched market reforms earlier than the Soviet

Vladimir Ovchinsky, Doctor of Science (Law), Major-General of the Police (Ret), is an advisor to the Chairman of Russia’s Constitutional Court, and a member of the Editorial Board of *Russia in Global Affairs*.

Union, followed by Russia, and therefore was in the position to recognize the problem at an earlier time. While the Soviet Union first confronted the problem of organized crime and corruption in the mid-1980s, beginning with the famous “Uzbek affair,” China already experienced this phenomenon in the late 1970s, with the revival of the notorious “triads” (which, incidentally, played a significant role in the Celestial Empire back in the 17th century).

The study of contemporary organized crime in China, carried out by Chinese scholar Xin Yan, shows that mafia-type organizations seriously destabilize public order. Their leaders actively infiltrate economic structures as corruption ties grow stronger and economic crimes become more refined. Meanwhile, low-level government bodies (in villages and small towns) and law-enforcement agencies become increasingly infiltrated by criminal elements.

Eventually, the leaders of criminal organizations succeed in rising to high positions in the social hierarchy. For example, they become deputies of the National People’s Congress or members of political consultative councils in the provinces. Criminal organizations are more frequently interfering with the reshuffling of high-ranking officials. Moreover, there were even cases when the authorities of some Chinese regions asked the mafia to take over low-level administrative power (for example, in villages), while many local administrators asked the mafia for financial aid. Thus, criminal organizations in those regions evolved from a “criminal force” into a “criminal power.”

Xin Yan has studied many criminal cases and concluded that organized crime groups are often organized and run by former party and administrative functionaries and high-ranking officials of prosecutor’s offices. There were even reports alleging that these criminal leaders were active deputies of the National People’s Congress, secretaries of Communist Party cells, and chief executives of local Public Security Bureaus.

An increasing number of triad societies now operate under the umbrella of legitimate companies and enterprises and infiltrate governmental economic entities. Triads, which generate massive profits, have built a system for laundering illegal revenues.

According to Chinese experts, about 200 billion yuans (U.S. \$24.7 billion) is laundered in China each year; huge sums of money circulate through illegal money-changing shops.

Triads are more active in the coastal provinces, especially in Hong Kong. They control heroin and opium supplies, the hard currency black market, and the trafficking of Russian and Ukrainian prostitutes for brothels in Hong Kong and Macao. Finally, they control arms trafficking and provide “protection” for local businessmen. In Hong Kong, for example, there are 15 to 20 triad groups that actively engage in criminal activities, each having at least 30,000 members.

The official *China News Weekly Review* published an article in 2005, revealing that, apart from Hong Kong and Macao, the Chinese mafia has spread its operations to large industrial centers in mainland China, such as Guangzhou, Tianjin and Shanghai.

Mafia organizations are taking advantage of both the negative and positive aspects of China’s economic reforms. Of course, they could not ignore the country’s fast-developing Internet market (as of early 2006, China placed second in the world with over 110 million users, behind only the U.S.) and organized on-line sales of pirated audio and video materials. Now, items offered for sale by triads also include drugs, prostitutes, stolen cars, weapons, false documents, and even human organs for transplantation.

The Beijing authorities work hard to control the Net by means of over 30,000 Internet police officers. Since the beginning of the 21st century, more than 2,000 web sites have been closed down for offering sexual services and gambling entertainment. Yet every day new sites appear that replace the closed web sites.

The rapid growth in fuel prices tempted the mafia to steal crude oil from pipelines, many of which were seriously damaged. The police estimated the amount of oil stolen in 2005 at over U.S. \$120 million.

CHOPPING OFF THE DRAGON HEADS

The architect of the Chinese reforms, Deng Xiaoping, laid the ideological and organizational basis for the struggle against mafia

structures and corruption in the People's Republic of China. In the early 1980s, he pointed to a steadily worsening criminogenic situation in the country and emphasized the need for a long-term struggle against this social evil. In particular, he ordered full-scale operations against organized crime.

Deng also initiated the establishment of powerful analytical subdivisions within the Ministry of State Security and the Ministry of Public Security. These subdivisions prepare long-term forecasts for the development of the geostrategic and regional criminogenic situation and devise plans for full-scale operations. There are also several central analytical organizations (for example, the Research Office under the State Council).

From 1983 to 2005, at least ten full-scale operations of this kind were carried out, in which more than one million criminal groups were liquidated. Many of their leaders, together with the most odious members, were executed.

Importantly, these types of operations against organized crime, together with the ongoing struggle against the mafia and corruption, are conducted in China in strict compliance with the law. China's criminal law, together with those laws that pertain to criminal procedure, is constantly modified to respond to changes in the situation. Chinese laws, unlike Russia's, contain clear definitions of mafia organizations, while the Supreme People's Court regularly gives detailed explanations of judicial practices pertaining to cases on organized crime and corruption.

To counter the increased scope of money laundering by the mafia, the Chinese government in 2004 set up the Anti-Money Laundering Monitoring and Analysis Center. Additionally, the Ministry of Public Security has an anti-money laundering department, which develops specific measures, interacts with foreign counterparts, and coordinates the activities of the ministry's local divisions. There is even a special computer network that controls money flows 24 hours a day.

All these organizations participate in the full-scale operations, after which criminal activities subside for some time. Yet, after a while, criminal groups become active again, because these opera-

tions fail to eliminate the main reasons for crime. Thus, in place of the chopped off head of the dragon, many more deadlier heads grow in its place.

Unless unemployment, China's main social problem, is solved, the self-reproduction of liquidated criminal organizations will continue. The number of the unemployed in the country is estimated at 182 million to 199 million, or 26 to 28 percent of the number of the employed. This figure equals 10 Chinese armies, and the mafia uses a large part of these redundant people.

A source of special concern is that the army of the unemployed is largely recruited from young people below the age of 35. According to a study conducted by China's Ministry of Labor and Social Security, the unemployment rate among young people in 62 cities across China has exceeded 60 percent. Even graduates from institutions of higher learning have difficulties finding a job.

The "going outward" and "welcome to come" strategies, conducted by China in the last few years, are intended to increase the country's foreign trade and foreign direct investment and, simultaneously, to solve the unemployment problem through intensive labor migration to other countries.

THE EXPANSION PROJECT GAINING STRENGTH

The above strategies helped China to increase its foreign trade almost threefold between 2001 and 2005. According to expert estimates, by 2020-2030, China will pass the United States in terms of GDP, thus becoming the world's economic leader. The same conclusion is drawn by the well-known 2020 Project [Mapping the Global Future, prepared by the National Intelligence Council, a CIA advisory group, and issued on January 15, 2006 – Ed.].

As regards the "welcome to come" strategy, according to some Western analytical centers cited by Maxim Chereda, the leaders of the largest and most influential triads established contacts with representatives of the Chinese leadership at all levels, which ensured the safe infiltration of their cash into Mainland China, mainly in its southern provinces. The triads' money was used for

establishing profitable joint ventures, such as nightclubs and casinos. The co-founders of these ventures included regional representatives of China's security organizations, in particular the Ministry of Public Security and the People's Liberation Army.

However, any sort of "peaceful coexistence" between the Chinese mafia and the country's leadership could not last for long. "Triads were alright for Beijing for as long as their capital was needed for economic reforms in the country," Chereda wrote. "Now the reform process no longer needs support from 'not quite legitimate organizations,' to put it mildly." As a result, the Chinese leadership has launched an offensive against triads.

At the same time, as prominent sinologist Vilya Gelbras writes, China has attracted U.S. \$600 billion in foreign direct investment in the course of its "going outward" policy. According to some estimates, China has invested U.S. \$700 billion in American securities, thus protecting the dollar and securing its presence on the U.S. market. From 2002 to 2005, foreign direct investment by Chinese enterprises alone (without taking into account financial organizations) amounted to \$17.9 billion (with an average increase of 36 percent a year!), while more than 10,000 various enterprises have been set up outside the country. Considering the toughening of the government's anti-mafia and anti-corruption policies inside the country, and the continuing "going outward" strategy, triad leaders objectively benefit more from directing their expansion out of the country.

This global criminal project is already being implemented – and very effectively. Chinese mafia organizations have established control over migration processes and have taken leading positions in organizing human trafficking and illegal migration. As follows from the U.S. Department of State's report of 2005, China now ranks amongst the countries that require special attention due to the vast number of people who are made victims of human trafficking. A June 2006 report by Europol described Chinese mafia groups as leaders in human trafficking throughout the European Union.

Chinese triads have even made Japan's mafia, yakuza, make room in its own country: the Chinese account for about half of all

crimes committed by foreigners in Japan (double the figure from a decade ago), while their mafia organizations control two-thirds of heroin trade in that country. According to U.S. expert estimates, these organizations have also infiltrated the U.S. legal and black-market economies, surpassing even the Colombian cartels. In Italy, in early 2006, law enforcement bodies launched a major investigation into links between Chinese gangsters and the Italian mafia. An investigation is being held in Milan's Chinatown with regard to suspicious investments in real estate and trade. In Rome, investigators have revealed dummy firms and banks engaged in money laundering. The first large-scale investigation concerning the financial resources of the Chinese mafia in Italy involved 22,000 Chinese. In total, the Italian police have launched 250 criminal cases against the leaders of Chinese mafia organizations and their assistants.

A 2005 report by Italy's chief prosecutor said that the local Chinese triad was becoming more and more aggressive and united. The last few years have seen a rise in illegal activity, such as robberies and acts of extortion with regard to Italian citizens, and the emergence of mixed Chinese-Italian criminal groups.

Chinese organized crime can provoke global economic crises and influence market prices. In particular, in 2005 the world copper market was on the brink of collapse after a disastrous gamble on the London Metal Exchange. Chinese copper trader Liu Qibing, well known among business circles, sold 200,000 tons of copper on the exchange on behalf of the Chinese State Reserve Bureau, after which he disappeared, while world copper prices reached a record high.

Given the vast expansion of Chinese organized crime, it was impossible that the phenomenon would bypass Russia, but the intensity and forms of this expansion differ in many respects from the situation in other countries. There are objective reasons for this.

INFILTRATION OF RUSSIA

Sociological studies conducted by Russian scholars on Chinese communities in Moscow, Irkutsk, Khabarovsk and Vladivostok, in addition to the results of polls taken in Blagoveshchensk, Nizhny

Novgorod, Rostov-on-Don, Barnaul and Belokurikha (the Altai Region), have shown that Russia, like the rest of the world, is experiencing a decisive moment: the development of new conditions for the global expansion of Chinese migration, and the rise of Chinese communities in foreign countries. This largely spontaneous growth has given way to the organized expansion of Chinese immigrants abroad and the broadening of their business activities.

The estimated number of Chinese migrants in Russia varies from 400,000 to 3 million. The main problem posed by this relatively new phenomenon is the damage these groups inflict on the Russian economy: the Chinese communities, according to police information, are covertly controlled by Chinese mafia organizations. Meanwhile, relations within these communities are patterned after those in the triads (strict obedience to the leaders, a vow of silence, severe punishment of recalcitrant members, etc.).

The majority of Chinese migrants, organized by mafia, go to Russia's Far East. There are objective historical, demographic and, particularly, economic reasons for this choice. Sinologist Andrei Ostrovsky writes that Russia's market reforms, marked by the loss of state regulation in the economy, have not made the region attractive to investors. Actually, in the competition for attracting capital to the Far East, Russia lost out to China.

The governor of the Khabarovsk Territory in the Russian Far East, Victor Ishayev, told the *Izvestia* newspaper in April 2006: "The Far East has been isolated from the Russian economy. In the Soviet times, 75 percent of all our products were supplied to Russia's domestic market, whereas today we supply only 4 percent. Full-scale ties with the rest of Russia are impossible due to unequal conditions, in particular high tariffs on heat energy, electricity and transport, and the absence of industrial restructuring... Today we are legislatively determined to be a raw-material appendage of the advanced, fast-developing countries (Japan, China, Korea)."

Chinese mafia organizations exploit Russia's Far East and Siberia precisely as a raw-material appendage. Yuri Yegorov and Alexander Samsonov, who studied organized crime in Russia's

East Siberia and Far East on the basis of police information available for the period 1999-2003, cite the following figures.

Table 1. Ethnic Organized Crime Groups

Nationality	Percentage of all ethnic groups	
	East Siberia	Far East
Chinese	34.3	32.2
Vietnamese	12.1	13.1
Koreans	5.3	5.8
Mongols	3.0	–
Other nationalities	45.3	38.0

Of all criminal cases launched by the Russian police against ethnic organized crime groups in 2002, Chinese criminal groups accounted for 38 percent of the criminal cases in East Siberia, and for 40.9 percent of all cases in the Far East.

Poaching and smuggling of the forests and seas in the Russian Far East is also carried out on an organized basis. Hundreds of Chinese citizens are repeatedly detained in the Ussuri taiga with ginseng roots and other plants included in the Red Book of Russia. During the season for pine nut picking, Russian police recovered many tons of pine nuts from Chinese illegals. In China, pine nuts are processed for oil, which is later used as a component in pharmaceuticals and perfumes. Products that are valuable on the Chinese market, including trepang, ginseng, tiger skins and even bear bile, are smuggled out of the Maritime Territory. There is also an underground market for various kinds of frogs and turtle. In 2003, Chinese citizens began to actively smuggle various species of sturgeons into China from Russia.

Chinese poachers have destroyed the commercial stock of autumn salmon in the Ussuri River and have taken almost complete control over the migration routes of valuable fish species, including Siberian salmon and Siberian sturgeon, as well as popular sturgeon spawning areas.

Initially, the Chinese caught the fish themselves; now they actually hire the local Russian population for this task. The

Chinese organized crime groups also hire Russians for cultivating plots of land leased by these groups. In other words, instead of serving as additional manpower resources, these Chinese “migrants” mercilessly exploit the Russian population: the mafia never becomes a manpower resource!

Professor Vitaly Nomokonov of the Far Eastern State University warns that Chinese mafia organizations in the Far East are intensively integrating with the Russian mafia. In Ussuriisk, for example, triads have established business relations with local criminal leaders: Russian organized crime groups help triads to buy metals in the region and to ship them abroad. Also, Russians set up passenger transportation firms, which are used by the Chinese, and provide warehouses for storing goods, including contraband. The last few years have seen the rise of yet another phenomenon: more and more Chinese are joining Russian organized crime groups, tipping them off about the movements of Chinese traders. At least one Chinese trader is robbed every month.

Professor Valery Sobolnikov of the Siberian Academy of Civil Service points out that in 2002-2005 Chinese organized crime groups registered businesses with dummy Russian owners, which allowed the actual heads of these firms or commercial structures to evade taxes. In many cases, the Chinese mafia establishes firms for single transactions. In the Chita Region, for example, about a thousand such “companies” have been revealed. In the Novosibirsk Region, numerous facts have been disclosed about foreign-trade operations carried out by front businesses. Incidentally, a majority of such commercial structures export strategic raw materials out of Russia.

Professor Anna Repetskaya of the Baikal State University of Economics and Law points to a similar tendency in the Irkutsk Region. She cites reports collected by the local bodies of the Federal Security Service (FSB), which thwarted the thefts of strategic raw and radioactive materials that were intended for export to China. Many Russian and Chinese organized crime groups divided functions: Russians stole the products from local enterprises, while the Chinese smuggled them to China.

FOREST MANDARINS

Researchers are warning that the greatest threat to Russia's national security (especially in the economic realm) comes from criminal operations in the timber sector. Anatoly Lebedev of the Bureau of Regional Public Companies in Vladivostok has analyzed this problem in detail in the course of a journalistic investigation. Below are its main findings.

The lack of funding of the State Timber Service and Inspectorate in past years, compounded by official permission to seize confiscated illegal timber, resulted in unprecedented rates of corruption in the timber sector. Later, in 2002, a new government decree outlawed the practice by foresters and law enforcement bodies to profit by means of confiscated timber. Since then, all confiscated timber must be sold in favor of the Ministry of Property, while the foresters no longer receive a cent from these revenues.

Yet the corruption continues. The system of illegal logging and timber resales has become too widespread and involves too many local high-ranking officials to be easily liquidated. Chinese businessmen play a major role in this system. This is why attempts to adopt a new Forest Code that provides for the abolition of forestry enterprises, together with the delegation of their functions to leaseholders, have caused a panic in the region. For the Far East, this would mean that the vast forests could simply fall under the direct control of Chinese businesses.

Many retired Chinese generals and agents of special services actively participate in legal and illegal commercial operations in the Far East, buying property, hiring workers and controlling the most profitable kinds of businesses. The Chinese have quickly learned to copy Russian methods of evading taxes, with a slight difference: they are more effective at it. Thus, the large-scale smuggling of timber continues to the mutual delight of Russian and Chinese businessmen – and to the detriment of the Ussuri taiga.

Many Chinese, who operate under alias Russian names, control areas for wholesale timber sales in several cities of the Maritime Territory – Luchegorsk, Dalnerechensk, Lesozavodsk,

Ussuriisk, Nakhodka and Dalnegorsk, in the Khabarovsk Territory, the Jewish Autonomous Region, and in the Amur and Chita Regions. According to the Anti-Organized Crime Department of the Maritime Interior Affairs Agency, there is enough proof that Chinese timber businesses in the Maritime Territory are under the strict control of triads.

DARING THE DRAGON

Why is it important to focus attention on these natural and raw-material resources? The matter is that over the years of reforms the Russian and foreign (including Chinese) mafias have got possession of what must never fall into their hands: Russia's natural wealth, raw-material resources, metals (including rare-earth varieties and gold), timber and coal.

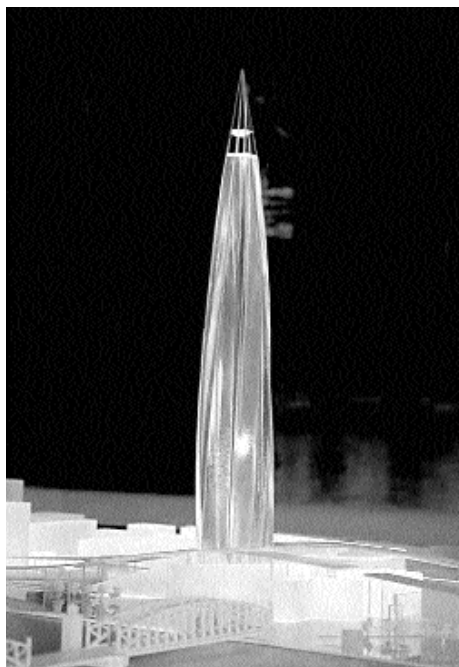
This situation is tantamount to a loss by the state of the levers of governance in the law enforcement sphere. If the government does not realize where it must focus its efforts, the law enforcement resource will continue to be dissipated without yielding the required results. Since it is impossible to address all the problems at once, the government must first set national priorities. Then it will be clear what methods will be the most effective against the Chinese mafia: cleaning up Chinese markets, dislodging triads from the taiga and timber-felling sites or launching military operations against those who destroy Russian bio-resources and ship trainloads of nonferrous metals and timber to China. On this last option, it would be extremely useful for Russia to borrow from China's experience in conducting full-scale operations against the mafia. Certainly, the success of any law-enforcement operation depends on whether the government makes a turn for the better in its social and economic policy in the Far East and East Siberia, which, in turn, depends on its policy nationwide. Why not follow the example of the Chinese leadership, which has admitted making serious mistakes pertaining to the "going outward" and "welcome to come" strategies?

The 5th Plenum of the Chinese Communist Party Central Committee of the 16th convocation (held in October 2005) dis-

cussed the five-year plan for 2006-2010 and set the task of “revising the view on the development” and “creating a new development model.” In its desire to “reform the reforms,” the Chinese authorities are focusing their ideological efforts on two major areas — propaganda of a new economic policy, with an emphasis on social justice and maximum expansion of the domestic market, together with a struggle against the liberal ideology, viewed as a challenge to China’s political stability. At the same time, the authorities have shifted the focus of the polemic away from Chinese problems to Latin America, Russia and other states of the Commonwealth of Independent States, asserting that those regions have turned into disaster areas due to America’s policy of imposing its liberal model on them.

Beijing has already announced that the economic model that has been used to rapidly enrich the most active part of Chinese society has exhausted itself. Now, the time has come to pay attention to the quality of growth, smooth over social conflicts, remove inequality, and provide equal opportunities for hundreds of millions of Chinese.

Russia on the Rise



The controversial project
of Gazprom's headquarters in St. Petersburg

“ Cities are acquiring new identities. They resemble one another less and less and each is seeking its own way to modernization and a unique place in the country and the world at large. But a closer examination of their strategies reveals a number of common approaches that turns their strategies – different in form and analytical content – into conceptual twins. ”

Strengths and Weaknesses of the Russian Economy

Vladimir Mau

98

Russia Against the Background of Major Economies

Valentin Kudrov

117

A Development Strategy for Russia's Largest Cities

Olga Vendina

129

Strengths and Weaknesses of the Russian Economy

Vladimir Mau

The essence of Russia's ongoing social and economic transformation is to be found in the modernization of the Russian economy and its changeover from an industrial system to the postindustrial model. This presents a well-known economic problem that Western countries resolved in the 1970s and 1980s. And like the West did previously, we are solving this task through a transformation crisis.

The problem is that Russia entered its postindustrial transformation much later than the West. Thus, we must ensure an accelerated level of modernization in order to reduce the gap between the levels of development in Russia and the world's most technologically advanced countries. In fact, we must choose an effective model of a postindustrial market and produce a set of state policy instruments that will ensure its proper functioning.

Economic theory offers some well-known recipes for accelerated modernization. Back in the middle of the 19th century, John Stuart Mill spelt out the key principles of resolving the tasks of modernization. With reference to Russia, these principles involve promoting the protection of ownership (against governmental arbitrariness, in part), human development and borrowing of foreign finance.

Vladimir Mau, Doctor of Economics, is Director of the National Economy Academy under the Russian Government; a member of the Editorial Board of *Russia in Global Affairs*. The author offers acknowledgments to Vladimir Novikov and Oleg Lugovoi for assistance in preparation of this article. The article was originally published in Russian in *Economicheskaya Politika*.

Russian Finance Minister Sergei Witte, who developed these ideas at the dawn of the 20th century, focused intensively on stimulating the transformation of financial savings into investment. To this end, he proposed to “lubricate” business activity among the general population and to bring in foreign investment. He insisted on lifting a prohibition for establishing joint-stock companies with foreign stakes, as well as on allowing foreigners to own land in Russia. Also, Witte urged the regional and local authorities to stop putting up obstacles to business operations.

It might seem that we can draw on our own experience of modernization – which witnessed the most rapid industrialization in the first half of the 20th century – while we develop a market strategy; our politicians (especially from the left) and even some economists who advocate the mobilization economic model often support such a stance.

And yet the content analysis of postindustrial economy makes one skeptical of ideas that originated in the traditions of an agrarian-industrial society. Postindustrial society witnesses the rapidly growing technologies and, consequently, growing consumer demand and increasing opportunities to meet it. This predetermines much uncertainty around the tendencies of, and prospects for economic and technological development, not to mention vague economic forecasts for the future. Hence, it is impossible to stipulate clear priorities for each industry. Moreover, any industrial branch or economic sector may become priority in certain situations. In contrast to the era of industrialization, concentrated financial resources may fail to deliver the desired effect. That is why *a policy of stimulating adaptive opportunities of economic agents* and their ability to grasp rapidly changing demand, as well as the ability to react promptly to those changes, falls into the limelight as opposed to resource concentration. As a result, priority is shifting to the sectors related to human development. It is the achievements in human development that create the necessary conditions for the postindustrial market.

Discussions of a model for such a transformation began at the 9th Economic Forum in St. Petersburg in June 2005, where an

approach based on the methodological principles of historicism was recommended. It specified an attitude of dirigisme and liberalism from the perspective of special features or stage of development of the labor forces. However, this type of formulating is too abstract and generalized. What is really needed is a detailed set of principles and actions that will enable the country to resolve the tasks it now faces.

STRATEGY AND RISKS OF POSTINDUSTRIAL DEVELOPMENT

Elaborating a strategy for Russia's postindustrial market involves a clear identification of the strengths and weaknesses of today's economic and political processes in the nation, together with an analysis of all internal and external factors that determine this country's development.

1. *Political and macroeconomic stability* has become a major prerequisite for the rejuvenation of economic growth and plays a decisive role for continued rapid growth. It is foolish to believe that stability once acquired in the past will continue long into the future. Russia's economic situation remains rather vulnerable to shocks and the authorities must continually work to ensure that the situation does not get out of hand.

The runaway prices of crude oil do not guarantee macroeconomic stability. On the one hand, the possibility of a drop in oil prices and the resultant destabilization of the budget, not to mention the entire economy, is always a threat. The longer oil prices remain high, the more painful a later adaptation to change will be. On the other hand, a favorable market situation may lead to destabilization if it lasts too long because it may provoke populist decisions that will trigger budgetary spending beyond the accumulation of revenues. In other cases, destabilization may arise from a debt crisis on foreign commercial liabilities, a crisis on the market of consumer loans, or instability in ownership relations.

A toughening of the government's administrative levers expands the opportunities for stimulating investment activity, but

it is important to ensure that newly created institutions do not exceed the government's administrative resources.

To prevent a crisis, Russia needs conservative budget policies that depend only on resources earned through an increase of labor productivity, a policy of low and flat taxes, and careful monetary policies that curb the increase of the ruble's exchange rate.

2. **Human capital.** The postindustrial era places emphasis on the development of man and his creative capabilities as a crucial factor in rapid social and economic growth. This includes, most importantly, the provision of respectable healthcare and education, together with the reform of the national pension system, science and other social spheres. Human capital can play a role similar to that of the railroads during industrialization, that is, it will serve as an engine that powers demand for the development of other industries. Russia has an inherent advantage in this sphere – its human capital is much more advanced than in other countries that have a similar level of GDP per capita. However, the situation remains highly unstable.

The widespread conviction that Russia enjoys a sizable edge over other countries in terms of human resources is only partly true (as shown in Table 1, which reflects Russia's rankings along separate indexes of economic and social progress). The situation still looks quite acceptable in the field of education, but the status of our healthcare is disastrous. In the meantime, the human potential index is strongly intertwined with per capita GDP. This means that Russia's edge is not particularly impressive and may decrease significantly unless dramatic measures are urgently taken.

This brings up two possible versions of Russia's future development:

- the economy will be upgraded to match the level of human potential, i.e. the human potential will be used to speed up a structural and economic transformation;
- Russia's human resources will degrade to a level witnessed in medium-developed countries.

Table 1. Russia's Rating in Social and Economic Development

Ratings and indices	Russia's place in ratings (2000-2005)
Index of competitiveness:	
<i>World Economic Forum</i>	64
<i>Doing Business</i>	79
GDP per capita (PPP-based)	55–60
Human development index (UNDP)	60–62
Including:	
Life expectancy	115
Education	30

It would be a mistake to claim that the current crisis in the social sphere was borne out of the crisis of the Soviet system. This is only partially true, since today's developments reflect a crisis of the industrial system as a whole. The current model of a social state – i.e., a state that spends significant resources on the well-being and development of its human potential – no longer works. This model emerged in a radically different demographic and social situation marked by a growing population that was predominantly rural and without a system of social security. All the available models of the social state took root in the industrial past, at the end of the 19th century. The demographic scenario was also dramatically different, as there were more young people than elderly, thus healthcare and other public services were financed by way of deductions from the former's earnings. But today, as the demand for retirement benefits for a rapidly aging population increases incessantly, a new and vastly different model of the social state should be devised.

A search for the best possible model of human capital development can be based on existing experience to only a small degree since the models that match today's challenges simply do not exist. The country that proves able to build such a modern and efficacious system will receive huge advantages in the postindustrial world.

It is also important to understand that the modernization of institutions (rules of the game) has a much greater role than their

mere financing. Pouring more money into the social sectors in the absence of their comprehensive institutional reforms does not produce lasting value. On the contrary, it can facilitate the conservation of outdated methods that have more than once shown their inefficiency.

It is important to concentrate our intellectual and political efforts on precisely these issues and to make this vector of development an unconditional priority for the government, both from the point of view of political attention, as well as through the concentration of budgetary resources. Such a crucial step forward can be found in the national projects formulated by President Vladimir Putin's administration.

3. **Taxation policy.** Over the past few years, Russia has made decisive steps to organize its tax system. Taxes were reduced considerably and their collection improved markedly as a result. Actually, the rate of non-payment of taxes fell practically to zero. Introduction of flat taxes (primarily the income tax) signaled an important step toward forming a modern tax system.

Three fundamentally important facts should be taken into account before further developments are made in this sector.

First, Russia's taxation traditions reveal big differences from the European tradition. In the West, a tax is something that people are ready (or are expected) to pay to the state for the services it provides to society. Correspondingly, this duty may increase or decrease depending on what volume of services the citizens expect from their government, as well as the quality of the services provided.

Russia has a totally different tradition in the field of taxes, which dates back to some degree to the times of Tatar-Mongol rule. Russians interpret taxes as a fee to the "Tatar khan" (or government) for his abstaining from intrusions into people's business during the year. Any talk of services is irrelevant in this case. People want only one service from the government, and this is to leave them alone; they can only bargain about the price of abstaining. That is why debates on the size of taxes make little sense. Naturally, the smaller the tax the better, since only one service is

at stake and it does not depend on the price. In other words, a tax increase cannot be the subject of a social contract.

Second, reducing taxes makes very little sense now, as most of the problems pertain to the quality of tax administration. If the tax agencies can simply re-compute taxes from several previous years, and produce amounts that exceed a company's revenue, then any discussion about tax rates loses its sense.

Third, the aforementioned problem demonstrates the significance of a correlation between the tax system and the government's ability to make proper use of it. For instance, the introduction of a flat tax scale derived more from the Russian authorities' inability to collect taxes along the progressive scale rather than from liberal ideological aspirations.

4. *High economic growth rates* play an important role in reducing the gap that now separates Russia from the most developed countries. The Russian economy is still registering high, although somewhat slowing, rates. This slowdown is natural for a transition from recuperative growth to investment growth. However, arguments to the effect that economic growth is the most decisive indicator of the effectiveness of the government's actions contain inherent risks. In the first place, they pertain to purely quantitative parameters and extol growth to the detriment of quality and other structural shifts.

The dangers that come with an obsession with growth rates are as follows. First, it tends to neglect the quality of growth and structural shifts. The package of scenarios for Russia's social and economic development that came under discussion over the past twelve months contains a proposal for doubling GDP through a steep increase of mineral resource output, partly with the aid of government investment. This scheme looks dangerous. Along with solving the political task, it increases the country's dependence — economically and politically — on international market fluctuations and thus prompts Russia to practically replicate the experience of the Soviet Union.

Second, there is a danger of political falsification. As soon as quantitative parameters are thrust into the foreground, the entire

state administration begins a rush for “fulfilling and over-fulfilling the objectives.” This is a well-known phenomenon in China, where the aggregate GDP of the provinces exceeds the data of national statistics by a factor of 1.5.

Recently, special techniques for stimulating economic growth have appeared in Russia’s economic policy – something that has not been seen in the fifteen years following the collapse of Communism. These new instruments provide the government with an opportunity for greater engagement in economic projects, such as work in special economic zones, investment funds, and concessions. Yet these “strong medicines” may turn out to be risky. Although they may become an important factor for speeding up social and economic growth, if handled carelessly they may fuel a degradation of the political and legal environment of economic activity.

5. *Judiciary, law-enforcement and administrative institutions.* Political institutions play a key role in ensuring steady social and economic development. It is even possible to speak about the declining productivity of economic legislation when its enforcement is inefficient. In other words, we have run out of resources for raising economic efficiency and consolidating economic growth solely within the format of the economic system and economic legislation proper. As a result, Russia has approached the phase where political institutions will predetermine further economic development to a large degree.

In order to stimulate an economic breakthrough, we must get quality labor and land legislation, laws on banks and bankruptcies, as well as tax and budget laws. All these norms and rules must receive implementation. But this requires efficient governmental machinery, fair judiciary, and a decent law enforcement system – in a word, the basic institutions of state power. Not a single law will produce the desired effects if the state fails to assure its enforcement, or if the courts fail to defend a citizen whose rights have been trampled on.

There can be no standard solutions in this sphere. The only conclusion is that the development of an adequate institutional environment (i.e. a system of incentives and sanctions) is of greater impor-

tance than increased financing of relevant sectors. The methods of stimulating economic activity include easing of administrative procedures and improvements in the conditions for business operations. Russia made a few steps forward in this area in the beginning of this decade but eventually the trend came to a halt. And if we take a look at the World Bank's research, we will see that *Russia has favorable conditions for opening a business. However, in the terms of contract implementation it is very vulnerable* (See Table 2).

Table 2. Selected Parameters of the Administrative Environment for Business

Country	Ownership registration		Contract execution	
	Period (days)	Costs (% of property value)	Period (days)	Costs (% of property value)
Russia	37	0.8	330	20.3
China	32	3.1	241	25.5
India	67	13.9	425	43.1
Brazil	42	2.0	566	16.5
Portugal	83	7.3	320	17.5
Poland	204	1.6	1,000	8.7
Hungary	79	6.8	365	8.1
Kazakhstan	52	1.8	400	8.5
Azerbaijan	61	0.5	267	19.8
Armenia	18	0.9	195	17.8
Belarus	221	0.2	250	20.77
UK	21	4.1	288	15.7
Germany	41	4.2	184	10.5
Italy	27	1.3	1,390	17.8
Australia	7	4.3	157	14.4
U.S.	12	0.5	250	7.5
DR Congo	106	10.1	909	256.8

Source: Business in 2005: Elimination of Obstacles to Development. Moscow, 2005

6. Affluence of oil & gas resources and its impact on the economy. Today, it is frequently heard that Russia's abounding natural

resources constitute one of its basic advantages and the only problem is we cannot learn how to use them properly. In the meantime, the natural rent is plagued with grave risks that can be described in the following ways:

- ‘Dutch disease,’ a growth of the ruble’s exchange rate and declining competitiveness of national manufacturers, in which import substitution becomes practically impossible and a country becomes dependent on the fluctuation of prices for its export items;

- imports of commodities prove to be more lucrative than imports of capital (technologies), while a strengthening ruble demands an ever greater inflow of foreign currency for solving investment tasks;

- structural shifts tend to be destimulated, i.e. the economic structure begins to degrade, risking to follow the plight that befell the Soviet Union, in which the economic system, based on high oil prices, collapsed after the oil market’s downturn;

- the inflow of finance generated by natural resources has a negative impact on the country’s political system, as the government is subjected to temptations of populism. It may allow itself to stage experiments with economic policy and to take unusual and irresponsible decisions that are compensated for with profuse infusions of money. The risk of corruption, which becomes practically inescapable when the government engages in the handout of the natural rent, becomes more pronounced as well;

- the demand for quality education drops, as the mineral resource sectors typically set forth lower qualification requirements for the workforce. Their domination in the economy cuts down the demand for education services, and this may produce a dangerous and enduring consequence.

History offers extensive evidence of the latter thesis, beginning with 16th-century Spain. Not a single country (with the exception of a few absolute monarchies) has been able to make breakthroughs solely by exploiting oil, gas or precious metals. However, a few recommendations are called for to confront those risks and neutralize the vulnerability of energy resource prices:

– *The Stabilization Fund* must be kept intact and not squandered for populist projects. In theory, this fund may have four functions: it can be used as a fund for future generations; as budget security in case of unfavorable market situations; as a tool for controlling the money supply; and for preventing the economy's adjustment to high crude prices (to prevent a repetition of the Soviet Union's fate). The latter two functions are especially topical for today's Russia.

– *A strategic plan of action in case oil prices collapse.* This document is yet to be drafted, but it need not be made public. The strategic plan should contain a set of coordinated measures in the field of monetary, budgetary, customs, liabilities, and structural policy, and also specify many other issues pertaining to development of the national economy and its separate sectors should a long-term decline of oil prices begin.

SCENARIOS FOR LONG-TERM DEVELOPMENT

Given the current condition of state institutions, in addition to the controversial social, economic and political tendencies witnessed in Russian society, there are three qualitative models for the nation's development:

– the Australian model: presupposes the diversification of an economy that is initially hinged on the production of raw materials and a simultaneous maintenance of political institutions of Western society;

– the Mexican model: the oil industry dominates the economy, although the latter is diversified by and large;

– the Nigerian/Venezuelan model: wherein the economy is pegged to oil, diversification is insignificant, and political institutions are feeble.

The labeling of economic models is rather conventional and there is no doubt Russia will have its own original model someday, regardless of whether the model is successful or not. Russia will not turn into Australia, or even Mexico or Nigeria for that matter, yet the unique experiences of those nations enable us to

single out some circumstances of development and the consequences that should be reckoned with in the process of elaborating economic policy.

1. ***The Australian model.*** The experience gained by Australia, a country rich in natural resources, which was forced to cope with economic restructuring and the adaptation to large inflows of migrants, can be very useful for Russia. The export of raw materials to Japan and Southeast Asian countries provided the Australians with substantial resources, which they used to diversify the domestic manufacturing sector and build a modern postindustrial economy.

If applied to Russia's long-term prospects, this pattern of development implies moves in the following directions:

- attainment of high or medium growth rates (the GDP and, especially, the GDP per capita) that would make it possible to push development up to the level of the most advanced countries;
- an increase of foreign investment that is diversified for various branches of the industry. The bulk of this investment is no longer concentrated in the fuel and energy sector. The latter retains a big share in exports, but its share in domestic production is gradually decreasing. This is how the model of industrial diversification through revenues gained from resource exports is translated into practice.

Depending on market prices for energy resources, the balance of payments on current operations is either close to zero or moves into the red due to the intense activity of foreign investors. The ruble continues to strengthen, which is made up for by growing labor productivity thanks to foreign and internal investors. The government abides by a conservative investment policy, which includes restrictions on overburdening the budget. The share of the budget in the GDP remains at a much lower level than in most developed countries and inflation does not exceed 3 percent annually.

Reform focuses extensively on political institutions and on upgrading the efficiency of the social sphere (in education and public health), as these very sectors offer answers for progressing

along the road to development. The development of political and social institutions is oriented at the standards of modern democracy, and conditions for business resemble those of developed countries, and occasionally are even more lucrative in some areas (for instance, in terms of its less stringent labor laws). The judiciary system is free of political pressure and the authorities energetically fight corruption. This pattern of development lays the groundwork for gradually creating a common economic space between Russia and the EU, lifting tariff and non-tariff trade barriers and creating a common market.

This is the most dynamic model, and to make it feasible the government needs to conduct an active policy in building state institutions, restructuring the entire subsidized sector of the economy and raising the efficiency of budgetary spending.

2. *The Mexican model* presupposes high growth rates due to the development of the fuel and energy sector and related industries. If the price of crude remains at a consistently high level, growth rates and investment activity may be substantially higher than under the Australian model. The inflow of foreign direct investment is also high, but these funds largely become concentrated in the fuel and energy sector, and a handful of other sectors.

This model envisions a moderate diversification of the economy since the investors pay major attention to energy resource production. Hydrocarbons dominate in the structure of exports and account for a big percentage of the GDP. Diversification, although positive, is rather slow due to the threat of Dutch disease. Raw materials make up the bulk of exports, but the share of other industries – metallurgy, chemistry, and other ecologically unsafe branches, as well as agriculture – may see growth.

Trade balance shows a steady surplus, and the situation is the same with the balance of payments, although its surplus decreases continuously. This does not pose serious problems, however, unless the energy sector's role experiences a dramatic tailspin in the global economy.

There is a high probability of an increase of the government's role in the economy, primarily in two directions. First, the state

may build up investment activity by investing in general-purpose infrastructure, as well as in the transportation of energy resources. Also, it may invest directly in those branches of the economy that private businesses find unattractive. In this case, the mechanism of private-state partnership takes on a key role as a mechanism of combining investment activity on both sides. Second, the government may work to protect domestic producers from foreign competitors. Reducing competitiveness for some domestic producers serves to enhance the positions of proponents of protectionism, and the government will have to resort to it sooner or later. Some sectors of the national economy (most importantly, agriculture and foodstuff producers, as well as some types of machine-building sectors) will be closed off from foreign competitors and this will produce a further reduction in their competitiveness.

In this model, the economic activity of the state collides with objective political and administrative barriers, as the country's ability or inability to considerably improve the quality of state institutions, including the administrative and judiciary agencies, will become a key problem of increasing economic efficiency.

As for the political regime, it will most likely develop in the "one-and-a-half party" format in this situation, meaning that democracy as such will remain, but one of the political groups (or parties) will considerably increase its influence and constantly win elections. As it is clearly seen from the experience of Mexico, as well as Italy and Japan after World War II, such models can ensure rather successful economic development even in spite of some side effects (like high corruption levels). On the other hand, the energy resource sector's domination will have an adverse effect on the stability of the "one-and-a-half party" system, bolstering the illusion of reliability and steadiness and thus undermining the responsibility for and quality of decisions taken.

The absence of significant social reforms constitutes a typical feature of this model; the availability of finance perpetuates the status quo in these sectors and does not give rise to loud social protests. Various segments of society will remain in a neo-Soviet condition and will not support the emergence of a social/economic market.

To sum up the characteristics of the Mexican model, let us underline two possibilities for Russia's development. First, the model is vulnerable to internal and external shocks. It can function smoothly if the situation on the global markets is favorable for Russia, but a long, drawn-out fall in oil prices may trigger a heavy or even systemic crisis. Its severity will depend chiefly on the price of products within the energy resource industry. The longer the oil boom continues, the greater the structural dependence of the economy (internal production, first and foremost) on infusions of "easy money" and, consequently, on the supply of cheap imports. The risk of replicating the plight of the Soviet Union becomes a real threat at this point. Secondly, the implementation of this model will block any opportunity to make a breakthrough into the postindustrial system and to catch up with the most advanced countries in terms of development. This is the side effect of dropping a resolute modernization in the social sphere.

Events can take yet another turn. If oil prices remain high for a long period of time, the very economic process will impel a strengthening of political institutions, an ongoing democratization, and the bridling of corruption.

In summarizing the Mexican model, it guarantees a relatively stable economic development at moderate or high rates without structural changes in the economical, political or social spheres, thus setting up conditions for immediate economic and political stability, given the absence of external shocks. But the vulnerability to shocks and the barriers it contains for a postindustrial breakthrough remain very serious problems for this model of development.

3. *The Nigerian model* identifies the development of a country that has abounding natural resources and uses them amid advantageous foreign trade. It implies conservation in the economic and social sphere against the background of dominating patterns of lackluster development. Growth rates under this model depend fully on what is happening on the international market of energy resources, which are the only tools of making hard currency revenues necessary for the solution of all other economic, social and political tasks.

Thus, growth rates will decrease over the medium term even though the prices of exported commodities may stay at high levels. This is due to the quality of economic policies and, correspondingly, the overall level of economic efficiency, which will worsen as long as the economy – pegged to oil resources – gains strength while crude oil brings in ever-larger hard currency revenues.

This scenario raises the probability of two tendencies in policy-making in general, and in economic policies in particular. In the first place, it signifies the strengthening of authoritarian trends. Large fuel and energy resources easily lend themselves to concentration in a trust, thus laying the groundwork for an authoritarian regime. The availability of vast financial reserves unrelated to a growth of labor productivity opens up the way to a system of government that does not bother to learn about the opinions of the taxpayers. The second tendency is related to the growth of populism in economic policies. Inexpensive financial resources are instrumental in buying political support through budget infusions and staging newfangled experiments in the economy.

Conditions of this kind make government investment a crucial factor for supporting high or medium rates of economic growth. Foreign investors treat such countries rather skeptically and invest money almost exclusively in the fuel and energy sector or in related industries. This produces an unenviable situation that includes a sharply deteriorating balance of payments on current operations, a gradual ebbing of fiscal and monetary policies, and a transition to a policy of budget deficits. As a source of government investment, the budget deficit acquires the role of an accelerator for economic growth, but this only worsens the economic situation in the country.

The result is classical forms of macroeconomic populism, evidenced perfectly well in Latin American countries; economic policies showed ominous signs even at the industrial stage of development of the labor forces. Virtually all the countries that acted on such prescriptions failed to bridge the gap that separated them from the highly advanced states, while others (like Argentina) widened the gap sharply. In those cases, a brief period of eco-

nomic growth gave way to dire economic and political crises. Any withdrawal from such a populist model has always proven to be painful and has typically involved some sort of a military coup.

This means that the Nigerian scenario presumes a steady reproduction of political instability. Development along this path naturally leads to a deepening of the crisis of political and legal institutions with attendant high corruption levels and degradation of the social sphere. The latter gets the leftovers of government finance, while any allocations it may receive have a strong populist taint.

LIMITS TO GROWTH

Let us stress once again that whatever model of social, economic or political development is chosen for Russia will depend on its ability to build up-to-date social, economic, and political institutions. However, the progress of these sectors is heavily dependent on the rates of economic growth over the medium term (about two decades). Recall that the level of a country's economic development (measured in GDP per capita) correlates with the status of society's social, political and economic institutions.

Projections have been made for Russia's development on the basis of three types of averaged annual growth rates:

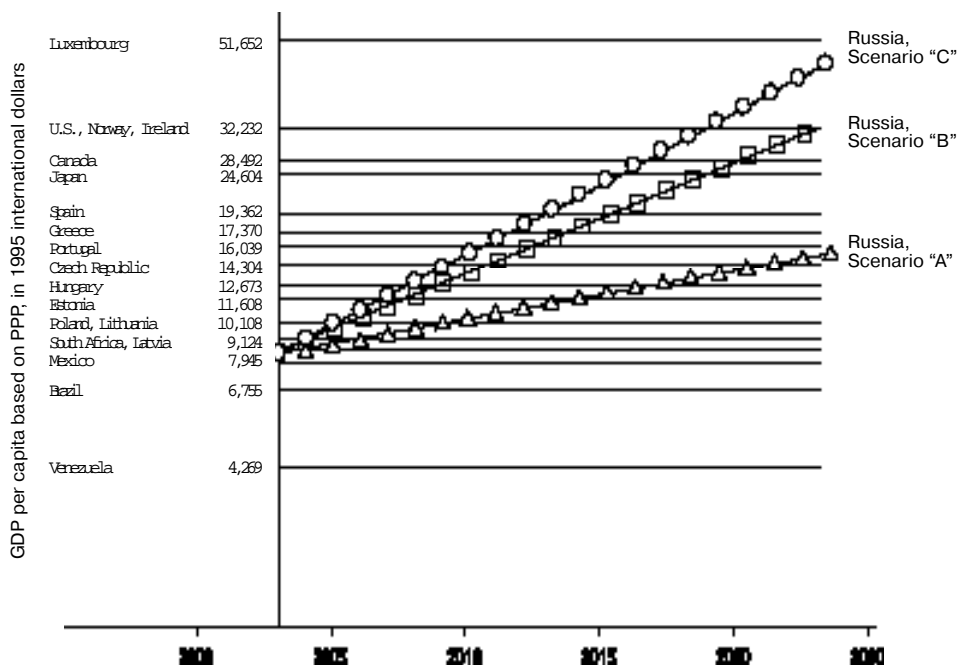
Option A: Annual growth rates at 3-percent minimum rate, which generally corresponds to the average global rate;

Option B: Annual growth rates at 5-percent growth, which fails to solve the task of doubling the GDP but exceeds the averaged growth rate of the most developed countries and hence helps to balance economic development (the task of catch-up development). This growth rate seems to be the most suitable from the perspective of in-depth structural reforms in the economy and the social sphere;

Option C: Annual growth rates of 9 percent at the maximum, which is somewhat more than what is required for doubling the GDP over a decade.

Calculating the different models is based on an assumption that countries having similar levels of economic development (estimat-

Graph 1. GDP Dynamics Under Various Development Scenarios



ed against the GDP per capita) also require comparison in other realms of activity, including economic, social and political life. More importantly, the most economically developed countries have the most developed systems of political institutions. In other words, this projection is based on a theory that the achievement of certain levels of economic development will keep pace with changes in other parameters of economic, political and social life.

Whatever model is used as the basis for calculations operates the rate of growth of the GDP in both the absolute and per capita expression. To make international comparisons simpler, the GDP at purchasing power parity was selected as the main parameter. This method enables a researcher to analyze the target conditions and disregards fluctuations within a specific period of time. One important feature are the instruments that take account of general global trends that are linked to global economic growth regardless of the situation in each particular country. In other words, the attainment of a certain level of GDP per capita does not require a

straightforward use of current data on a similar country but envisions corrections reflecting the shifts that result from global economic development. Chart 1 shows the dynamics of development over 20 years under each scenario. Also, it relies on a supposition that growth rates, compared to the level of development of certain countries and falling into a specified range in 2003, were steady.

The results of this calculation point to three conclusions that are important for understanding the tendencies of and prospects for Russia's development.

First, even a 9-percent growth rate over a period of twenty years will not allow Russia to exceed the level of economic development that any of the advanced countries in the world had in 2003.

Second, the Nigerian model is not anywhere in sight even considering the prospect for very low GDP rates. To slide into a degradation of that scale, a country must struggle through chaos and this is scarcely possible for a country at Russia's level of social and economic development.

Third, even low growth rates shown in Option A will eventually place Russia at the level of EU member-states, albeit the ones at the bottom of the EU list. Under Option B, the country will achieve the levels of Norway and Ireland, the two countries having the biggest GDP per capita in today's Europe.

A more scrupulous quantitative analysis of long-term economic growth factors produces a result unexpected at first glance. It shows that the quality of institutions does not improve automatically over time. This is to say, there is no statistically meaningful correlation between the quality of institutions and the time factor. But steady economic growth always improves the quality of institutions (like the institution of ownership). Global tendencies show that revenues do not grow anywhere without improving the institutional environment. Expansion of modern democratic institutions always correlates with growing revenues, which proves once again the thesis running through this article. It stipulates that improvement of the institutional environment is a fundamental prerequisite for resolving the tasks of accelerated modernization Russia is faced with today.

Russia Against the Background of Major Economies

Valentin Kudrov

There has been much talk lately in Russia about its future global leadership. How realistic are these popular projections? An answer to the question can be found in an unbiased in-depth analysis of quantitative and qualitative characteristics of Russia's economic development against major countries. Such an analysis is also essential for formulating the main strategies required to attain leading world positions.

COMPARATIVE ANALYSIS

What is the global ranking of Russia's total production volume? In most cases, this index is underrated since analysts estimate Russia's Gross Domestic Product (GDP) in U.S. dollars at the official exchange rate. However, this is wrong because estimates must be based on the purchasing power parity (PPP) of the ruble and the dollar, as is done by professionals, above all in international economic organizations. Russia's GDP in 2006, if based on PPP, would be not U.S. \$600-800 billion (if it is estimated on the basis of the official exchange rate) but U.S. \$1.5 trillion.

Since 1968, the United Nations has been implementing the International Comparison Project (ICP), which is designed to compare the purchasing power of national currencies, as well as the GDP per capita across countries. The Soviet Union for years declined to take part in this program, not recognizing "bourgeois

Valentin Kudrov, Doctor of Science (Economics), is professor at the Higher School of Economics; head of the Center of International Social and Economic Comparisons of the Institute of Europe, Russian Academy of Sciences.

parameters” of the GDP and the GNP. Thus, it conducted its own overestimated international estimations of its national income and other indices in U.S. dollars. It was only in 1990 that the Soviet Union took part in the ICP, just one year before the breakup of the U.S.S.R.

The Russian Federation was admitted into the ICP in 1993, and subsequently became a permanent participant in the program, providing all the necessary basic data. In particular, for calculating PPP for 1999 within the framework of the Eurostat-OECD program, Russia provided data on prices for almost 3,000 goods and services, thus forming a “basket” for comparing, in dollars, its GDP with that in other countries. Similar calculations were made for 1996, 1999 and 2002, involving an increasing volume of data on prices for comparable goods and services included in the GDP.

Table 1 below cites the results of international comparisons of the GDP of Russia and major countries for 2003.

Table 1. GDP of Russia and Other Major Countries for 2003

Country	GDP, bln, USD	% of U.S. figure	GDP per capita, USD	% of U.S. figure
Russia	1,318.8	12.1	9,195	24.6
United States	10,870.0	100.0	37,348	100.0
China	6,635.4	61.0	5,150	13.8
Japan	3,582.5	33.0	28,162	75.4
India	3,096.2	28.5	2,909	7.8
Germany	2,279.1	21.0	27,609	73.9
France	1,632.1	15.0	27,327	73.2
UK	1,606.9	14.8	27,106	72.6
Italy	1,559.3	14.3	27,050	72.4
Brazil	1,371.7	12.6	7,498	20.1
Mexico	934.6	8.6	7,767	20.8
Canada	963.6	8.9	30,463	81.6
Western Europe	10,550.0	97.1	26,838	71.9

Source: World Economy and International Relations, 7/2005, pp. 85-89 – Russ. Ed.

These calculations show that Russia's GDP in 2003 exceeded \$1.3 billion and that it ranked 10th in the world, lagging behind the U.S. and Western Europe by about 8 times, China by 5 times, Japan by almost 3 times, India by 2.3 times, France, Great Britain and Italy by 1.2 times, and Brazil by 4 percent.

In the same year, *in terms of GDP per capita*, Russia lagged behind the U.S. by 4 times, Western Europe by 3 times, Japan and Canada by 3.1 to 3.3 times, Germany by 3 times, and Great Britain, France and Italy by less than 3 times. At the same time, Russia was ahead of Mexico by 18 percent, Brazil by 22 percent, China by 1.8 times, and India by 3.2 times.

In terms of GDP, Russia is closely behind Brazil, and in the next few years Russia may overtake Brazil in this category. More importantly, Russia's GDP has approached that of France, Britain and Italy, lagging just 20 percent behind. In the meantime, Russia's Asian neighbor, China, enjoys much stronger positions in the world. China's GDP is already more than 60 percent of the U.S. GDP, while Japan's GDP is only about 50 percent of China's.

Table 2. Industrial Production in Russia and Other Major Countries for 2000

Country	Bln dollars	% of U.S. figure	% of global figure
Russia	450	20.1	4.4
United States	2,235	100.0	21.9
China	1,130	50.6	11.1
Japan	790	35.3	7.8
India	240	10.7	2.4
Germany	675	30.2	6.6
France	365	16.3	3.6
UK	335	15.0	3.3
Italy	335	15.0	3.3
Brazil	212	9.5	2.1
Mexico	170	7.6	1.7
Canada	230	10.3	2.3
Western Europe	2,400	107.4	23.6

Source: World Economy: Global Tendencies For a Hundred Years. *Moscow, 2003, pp. 545, 546, 549, 550. – Russ. Ed.*

Now let's analyze data on industrial production. As Russia's State Statistics Committee (Goskomstat) does not make public international comparisons on industrial production in dollars, the figures given in Table 2 are cited from PPP surveys carried out by B.M. Bolotin of the IMEMO on the basis of international statistics and international economic literature.

These figures show that Russia's place in the world in terms of *industrial production volume* is much higher than in terms of its GDP. In industrial production, Russia ranks 6th in the world with slightly over 20 percent of the U.S. figure, whereas in Europe Russia is 2nd after Germany and ahead of France, Britain and Italy. This is due to Russia's mighty extraction industry and military-industrial complex. Russia's industrial production is almost twice as large as that of Canada.

The next table gives figures on international comparisons of labor productivity and Russia's place in the world economy in this aspect. The figures were provided by the IMEMO.

Table 3. Labor Productivity in Russia and Other Major Countries for 2000

Country	GDP per employed person (\$)	% of U.S. figure
Russia	15,400	21.1
United States	73,100	100.0
China	7,000	9.6
Japan	54,900	75.1
India	5,900	8.1
Germany	56,200	76.9
France	54,500	74.1
UK	55,800	76.3
Italy	58,800	80.4
Brazil	17,900	24.5
Mexico	24,300	33.2
Canada	62,100	85.0
Western Europe	53,900	73.7

Source: World Economy: Global Tendencies For a Hundred Years. *Moscow, 2003, pp. 539, 540. – Russ. Ed.*

Table 3 shows that Russia lags behind the U.S. in labor productivity by almost 5 times, Canada by 4 times, Japan by 3.7 times, and Western Europe by 3.5 times, while it is 100 percent ahead of China, and almost 3 times ahead of India. At the same time, Russia is 36 percent behind Mexico and 14 percent behind Brazil.

Russia's per capita income in 2003 stood at 4,690 dollars, that is, 95 percent of the world's average; 17.9 percent of per capita income in the U.S.; 28.8 percent of per capita income in Germany; 29.7 percent of the figure in Japan; and 211.7 percent of per capita income in China.

This was a statistical, purely quantitative characteristic of Russia's place in the global economy in the late 20th-early 21st centuries, which does not include analysis of qualitative aspects of the Russian economy and society.

A COUNTRY OF UNFINISHED REFORMS

Shortly after the financial default of August 1998 and a sharp devaluation of the ruble, Russia saw growth in production. Undoubtedly, production growth is important, but exactly what products have begun to be produced in larger quantities? Are these modern and competitive products, meeting stringent requirements of the global market?

Unfortunately, Russia's economic growth is purely quantitative and is due to the output of traditional, noncompetitive products. Russia manufactures few modern high-quality, civilian (that is, non-military) goods that are competitive. Moreover, unlike the new industrial countries and large developing countries, such as Brazil, India and particularly China, Russia has not yet grabbed reliable niches on the world market of finished industrial and agricultural products.

Unfortunately, Russia also remains a country of unfinished reforms. Most of Russia's setbacks in economic reforms stem from weak governance institutions and a lack of political will for forming a truly effective market economy and democracy. An inefficient level of professionalism and decision-making, together with an atmosphere of indolence, are commonplace factors in the pre-

sent governance system. Oftentimes these factors are aggravated by the outright sabotage of the fulfillment of decisions at various levels of state power, and the merger of the latter with the financial and private business circles. These factors have a very negative impact on the development of the Russian economy.

Mention should also be made of the vague public mindset in Russia, which is often described in the West as “Russian mental disability.” The latter stems from the incomplete departure of Russian society from the Soviet form of ideologized thinking, which prevented the Russian people from drawing a line under the Communist past by means of a public opinion tribunal over Bolsheviks’ crimes, or repentance for the lawlessness and violence committed throughout the Soviet period of Russian history.

Russia, which has not yet resolutely embarked on the path of market reforms and stable democratization, is already apprehensive about “orange” and other revolutions, not to mention the “pernicious” influence of the West, and often takes the path of isolationism while rejecting globalization and Europeanization. The outstanding German politician Otto Lambsdorff gave a characteristic assessment of Russia in this respect: “I was under the impression that contemporary Russia remains undecided about its goals. I think Russian society itself has not yet decided what it wants and which path it must follow. Thus, coexisting in Russia today are the most progressive, as well as the most reactionary tendencies, comprised of a market economy and a state economy, freedom and authoritarianism, progress and reaction. Using outdated terms, I could say that a ‘unity of opposites’ now reigns in Russia. There is nothing surprising about this. Russia has witnessed not only 70 years of Communist dictatorship, but also 700 years of authoritarian rule. Naturally, society is unable to exit this phase of protracted infancy overnight and become a democratic civil society. Germans know this very well. We had to learn democracy in the course of a long, painful and horrible process.” This is quite an explicit characteristic of Russia.

The above reasons suggest that Russia and its economy still have many difficulties in store for them, especially those that may

be caused by an aggravation of social discontent and territorial problems. Yet Russia has everything it needs not only for economic growth but also for economic and social prosperity. This includes, above all, huge manpower pools; technological, production and natural resources; enterprising and educated people of the new generation; and a large research and technical potential, which comprises scientists, numerous research institutes and design bureaus, the huge military-industrial complex, etc. One can add to this list financial resources and the political will for Russia's revival, which has emerged in the country under President Putin.

But today, in order to avoid a historical impasse and secure a worthy place in the world, Russia must create conditions for consolidating the market economy, while securing legal and social support by the federal bodies, which are in the process of being renovated and strengthened. Russia must work out a long-term strategy for the development of its social and economic realms, while consolidating its internal unity in every way possible in order to prevent any element of separatism and disintegration. Furthermore, it must work to develop the economy of Siberia and the Russian Far East.

The most important thing is to start establishing a new updated model of economic reforms. The main elements of this model are: all possible encouragement of investment; modernization of production; consolidation of market institutions; a large-scale innovation policy; social orientation of production; the strengthening of the country's territorial integrity and interregional economic ties; the final overcoming of residual, decaying Bolshevism and nationalism; and further integration of the Russian economy into globalization processes, with an emphasis made on high-tech products.

The state must promote in every way the systemic transformation of its economic system. This should be done through the government's direct investment in research and development, together with various economic regulatory measures, including tax breaks, subsidies, and depreciation and industrial policies.

Building such an economy requires the extensive use of modern economic knowledge, together with the serious development of economic science in the country.

CATCH UP OR OVERTAKE?

In the period until 2015 Russia can improve its GDP and industrial production both quantitatively and qualitatively. The average annual growth rate of the GDP during this period can reach 5 percent, while industrial production will increase at a rate of 4 percent. A slower growth of industrial production is characteristic of countries that are at the postindustrial stage of their development, and there are grounds to believe that the Russian economy has already begun moving toward the postindustrial stage.

Apart from growth in capital investment, which now is faster than growth in the GDP, other factors must start working in the future, such as the acceleration of technological progress, large-scale business initiative, and accelerated export of finished goods, primarily machine-building products. The Russian government, in its economic development program for the period until 2008, has set a target of achieving an almost 6-percent average annual growth rate of the GDP.

Naturally, my forecast, which is based on a high growth rate of Russia's GDP, proceeds from the assumption that in the period until 2015 Russia will avoid economic disasters, like the August 1998 financial default, and will continue market economic reforms and the modernization of its economy and production. Otherwise, economic growth rates will inevitably decrease, and any discussion about Russia's place in the global economy will acquire an entirely different meaning.

The economy develops according to its own laws, and political games or opposition cannot abolish them. At the same time, the state can speed up or slow down economic growth or production decline.

There are two possible variants of a federal economic policy for the period until 2015: (a) partial return to authoritative methods of direct state influence on economic development through market mechanisms, economic levers and incentives on the basis of the already created elements of the market infrastructure; and (b) a more resolute and authoritative continuation of the already begun market reforms (while recognizing and correcting mistakes

made), adjusting market policy, and developing further the cooperation with advanced Western countries, making the emphasis on values of a rule-by-law state and civil society.

In my opinion, the second variant is more preferable. However, it requires introducing a modern legislative basis and fitting economic growth into the framework of a rule-of-law state and civil society. It is important to clip wings of those bureaucrats that interfere in the natural process of competitive economic activity from purely selfish motives, and to carry out a long-awaited administrative reform with a view to making the whole of society healthier. Equally important is to remain within the framework of democracy and normal interaction between market and democratic institutions, and to base the country's economic development on competitiveness and the large-scale introduction of innovations.

To prognosticate economic growth rates in countries and regions of the West in order to determine Russia's place in the future global economy, one should analyze their growth rates for long periods of time in the past and during the 1990s.

In the United States, long-term or "historical" average annual growth rates of the GDP stand at about 2.7 percent. However, in the second half of the 1990s, the U.S. economy showed a higher growth rate – about 4 percent a year on average, although the period between 2001 and 2003 saw a marked decline in the rate. One may assume that in the period until 2015 the average annual growth rate of the U.S. GDP will be not less than 2.8 percent. Since the growth rate of American industry usually accounts for slightly more than 70 percent of the GDP growth rate, it is realistic to estimate the average annual growth rate for U.S. industry at 2 percent.

In Germany, former long-term average annual growth rates of the GDP were traditionally higher than in the U.S. However, in the 1970s, Germany began to lag behind the U.S. in economic growth rates. The lag increased most notably in the 1990s, as the German economy, hit by various internal factors, had become one of the most ailing economies among the EU member countries. In the period until 2015, the average annual growth rate of the

German GDP is estimated to be 2.6 percent, while industrial production is put at 1.8 percent.

In France, the long-term (“historical”) growth rate of the GDP was lower than in Germany and the U.S. In the last few years, however, France has made some gains on the U.S. At the same time, in the period until 2015, the average growth rates of the French GDP and industry will hardly exceed 2.5 and 1.2 percent, respectively.

Very unusual and interesting things have been happening to the economic growth rate in Britain. For decades, the British economy developed much slower than other major capitalist economies. Europe even coined the term ‘English disease.’ However, the liberal reforms launched by Margaret Thatcher boosted the country’s economic growth, and in the 1980s the average annual growth rate of the British GDP (2.7 percent) was higher than in the U.S., Germany and France. In the last few years, the economic growth rate in the UK has slowed down and remains lower than in the U.S. Yet it has been higher than in Germany, France, Italy and Japan. The Western press has even begun to seriously discuss the possibility of Britain overtaking France in GDP volume in the foreseeable future. However, in the period until 2015, the average annual growth rate of Britain’s GDP is estimated at only 2.4 percent, and that of industrial production at 1.1 percent, that is, not higher than in France.

Forecasts for major West European countries make it possible to give approximate estimates of possible growth rates for the GDP and industrial production in the whole of Western Europe. The average annual growth rate of the West European GDP in the period until 2015 may be about 2.5 percent, and that of industrial production, 1.7 percent.

The West European economy in the period until 2015 may grow somewhat slower than the American economy. The economic positions of Western Europe, after their relative consolidation in the last two to three decades, have begun to weaken as compared with U.S. positions. Today, there are no grounds to think that this tendency will change by 2015. The U.S. has

lower taxes, savings and unemployment rates than in Western Europe, as well as a higher competitive potential. The U.S. has stronger positions in high-tech production, innovation and in the overall infrastructure of technological progress, which will largely determine the economic growth and economic face of every developed country in the beginning of the 21st century. Traditionally, the U.S. has superiority over Western Europe in terms of the scope and risk-taking behavior in the realm of business activity.

The above data make it possible to estimate approximate ratios of growth in GDP and industrial production for 2015 (Table 4).

Table 4. GDP and Industrial Production in Russia and Major Western Countries for 2015 (%)

Ratio	GDP		Industrial production	
	2003	2015	2000	2015
Russia vs. U.S.	12.1	15.6	20.1	25.4
Russia vs. Germany	57.9	76.5	66.7	86.2
Russia vs. France	80.8	108.0	123.3	171.0
Russia vs. UK	82.1	111.0	134.3	188.6
Russia vs. Western Europe	12.5	16.7	18.8	24.6

These estimates show that by the year 2015 Russia will not have achieved its own GDP ratio against the U.S. (which it had in 1913); yet it will approach closely Germany and overtake France and Britain. Russia's lag behind the U.S. continues to be significant and will remain so for a long time. As regards industrial production ratios between Russia and major countries of the West in 2015, they will be better for Russia than in 1913.

Russia's share in the world's GDP in 2000 was only 2.1 percent (compared to 6.2 percent in 1913 in Russia's contemporary borders). The ratio between the GDP of Russia and the whole of Western Europe in 2003 stood at 12.5 percent (in 1913, the figure stood at 18 percent). In 2015, Russia's share in the world's GDP will be about 3 percent, while the ratio between the GDP of

Russia and Western Europe will be about 17 percent. Russia's share in the world's GDP in 2015 will be at least half of the figure registered in 1913. Russia's contribution to global industrial production will be less, too. According to IMEMO estimates, Russia's share in global industrial production in 1913, in its contemporary borders, stood at 8.9 percent; in 2000 it was 4.4 percent. In 2015, this figure will hardly exceed 5 percent, which is much less than in 1913. Over the last few centuries, Russia has never had such a low ratio between its GDP and the GDP of major European countries, not to mention in comparison with global GDP.

So, by the year 2015, Russia's share in the global economy will not be higher than it was more than 100 years ago; nor will its major macroeconomic indices improve in comparison with the U.S. This will be the price for 100 years of disturbances, revolutions and utopian illusions about building a "paradise" first in one country, then in a bloc of countries, and finally in the whole world. This led Russia down a path that diverted from democracy, the market economy, and a global civilization.

Nevertheless, in the long term, Russia will inevitably be a strong state economically and will rank first in Europe and 5th or 6th in the world in terms of GDP. But the situation is different from the political, social or civilizational points of view: unless Russia has an intelligible and specific strategy for its development, unless it makes a final choice in favor of globalization and Europeanization, and unless it adopts a guiding national idea for itself within the frameworks of modern civilizational norms and priorities, anything can happen to this country.

A Development Strategy for Russia's Largest Cities

Olga Vendina

By virtue of their size, large cities act as centers that service the needs of adjacent territories and, at the same time, as junctions of diverse networks, or hubs. This significance extends far beyond the limits of their territories. While the former function deals with the local characteristics of urban centers, the latter has a bearing on their external properties, including involvement in globalization processes. The duality of these cities' nature provides them with the necessary stability and adaptability. The local element plays the role of a stabilizer of development, while the global element stimulates it.

Proponents of globalization believe that Russia's largest cities must follow in the footsteps of the 'global cities' and compete for command positions in the global economy, using the geopolitical and geo-economic advantages of their Eurasian location and Soviet-era heritage.

As good as all of this might sound, it does not seem very realistic, and the crux of the matter is bigger than just Russia's backwardness or the lack of readiness of its major cities to take on commanding functions on a planetary scale. In the Western countries, truly 'global cities' are few in number, too, and they have somewhat specific functions. Anthony Giddens (2000) says they help form the institutional structure of the global economy and global society instead of merely redistributing the spheres of economic influence.

Olga Vendina, Doctor of Science (Geography), is a leading researcher at the Center for Geopolitical Studies of the Russian Geography Institute.

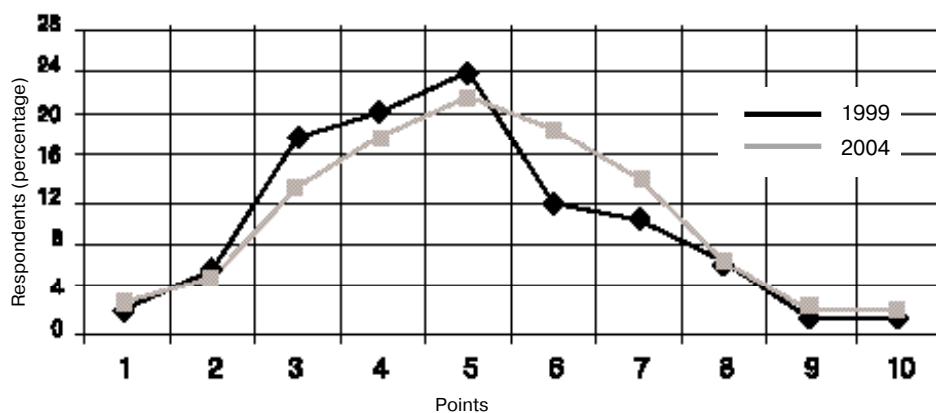
The last ten years have shown that the conscientious separation of local and hub functions, which could possibly set the whole mechanism of economic growth into motion by the push of just one button, does not produce the desired effect. In spite of the belief that development requires firm reliance on one's own strength, only a fraction of the cities with a population between 300,000 to 500,000 people, and located near export-oriented manufacturing giants, have been able to improve their position thanks to support in the form of local resources. These are the centers of resource production and/or primary processing, like Surgut in West Siberia, Cherepovets in the upper reaches of the Volga, Magnitogorsk in the Urals, Lipetsk in the south of western Russia, and some others. A slightly bigger group of large cities have managed to use their location at the crossroads of financial, commodity and human resource flows as a lever for radical economic transformation. This group embraces the capitals of Russia's constituent national republics, the central cities of seven federal districts that service the state governance system, the few resort places, some seaports, and towns located along the state border, since they act as gates to the outside world. The fact that some large cities, including historical inter-regional centers with a population of over a million people, have fallen off of this list testifies to the importance of searching for a new paradigm of development.

THE CRISIS OF THE LOCAL:
OLD SOLUTIONS TO NEW CHALLENGES

The winds of change have introduced the opportunity of independent action to the governmental authorities of all levels, and simultaneously vested in them responsibility for the decisions they make. However, neither government agencies nor the people proved capable of making such decisions in a situation where open markets and dependence on global processes poured down like rain out of a clear blue sky. Only the city of Moscow, which concentrated its financial and human resources, succeeded in efficiently exploiting its status as a national capital. It successfully

transformed its monopoly over command and administrative functions into big economic advantages. All of the other large cities needed almost a decade to adapt to the changes. A clear trend toward economic growth with attendant improvements in incomes, as well as quality and standards of living, came to replace the steady degradation of the urban environment and economic decline only in 2001-2002. Evidence of this change was found in many polls, which exposed the growth of Russia's urban middle class (see Graph 1).

Graph 1. Changes in Social and Economic Climate in Yekaterinburg



Source: Sotsium Foundation, Yekaterinburg, 2004

Almost all regional capitals and largest cities have drafted their own strategic development plans. By 2005, six out of Russia's eleven cities where the population exceeds a million people had designed and endorsed those strategy documents. They are St. Petersburg (1997), Novosibirsk (2002), Yekaterinburg (2003), Omsk (2002), Rostov-on-Don (2004), and Kazan (2003). Other major cities incorporated the key concepts of the strategic development in program documents, setting out the social and economic guidelines for the coming years. Most typically, such documents resemble a declaration of intentions – they mention objectives without specifying the techniques for achieving them.

They combine far-fetched prospects with very detailed programs, but provide little cohesion between them.

The basic reason why those strategic plans are largely declarative is due to the difficulty of identifying a city's place in the system of political, social and economic relationships. Their authors proceed from the assumption that the municipal administration of those urban areas enjoys considerable freedom in choosing the strategies of development, together with the methods of attaining the chosen strategic objectives. Yet the real situation shows that a huge number of external and internal factors influencing a city's development are beyond the control of the local authorities.

The list of factors that interfere with the social and economic decision-making process includes political problems, covert conflicts between mayors of regional capitals and governors of those same regions, and competition between geographically divergent centers of administration and centers of economic growth. An administrative center is rarely the center of economic growth in, or a financial donor for, a particular region. Not infrequently, it deprives the revenues earned by the region's second or third largest cities. The examples of such couples or triads of cities are many: Chelyabinsk and Magnitogorsk, Yekaterinburg and Nizhny Tagil, Samara and Togliatti, Khanty-Mansiisk and Surgut/Nizhnevartovsk, Krasnodar and Novorossiisk/Sochi, to name just a few. And yet, even if one ignores the list of above factors, the cities will still have to overcome managerial obstacles and revise the guidelines for social and economic growth.

Postindustrial economies show in bold relief that *the places where money is consumed have greater chances for advancement than the places of production*. This means that the sector of material production has reached a certain level of efficiency and scale, beyond which a quantitative buildup of output no longer brings the desired results. Apart from trading in energy resources, the tertiary sector of the economy – most importantly, the information industry, as it offers better wages and

consumes increasingly more labor resources — becomes the main tool for generating super-profits.

In the meantime, a strategy of development requiring a redistribution of resources in favor of the innovative and tertiary sectors of the economy does not fit the logic of routine decision-making at local administrations. No one can resist the temptation to spend the money coming today, even though this may have negative consequences for the future. St. Petersburg offered a good illustration when it struggled to win a Toyota factory on its territory against the city of Perm. St. Petersburg's authorities are touting their city as a Russian Detroit, as they attempt to arrange the placement of Renault and Nissan factories there as well. But the sizable investment of \$770 million to \$950 million, which may breathe some oxygen into the city's construction industry and provide an impetus to the economy through the creation of new jobs, will bring more problems tomorrow since the factories will need a large workforce, and the workers will need housing and social services. Also, different business sectors will begin to compete for placing their own facilities in one of the country's crucial postindustrial centers. Yet the experience of the biggest European cities — which eventually had to relocate automobile factories from their territories — proves that the abovementioned problems are unavoidable. Moscow is now following in Europe's footsteps and has announced plans to move AZLK, the manufacturer of small cars, from overly expensive city property.

Postindustrial trends in the economy have predetermined *shifts in the nature of interconnection between population settlement and location of most efficient economic activities*. It is not the population that moves to newly developed zones where relocated industrial facilities will be situated; rather, the new branches of the economy emerge in the places where the population possesses the appropriate qualities.

Society's moral guidelines and values have changed, too. While industrial society struggled to rid itself of poverty and 'spongers' (recall the campaigns on 'parasites' in the former Soviet Union), the postindustrial society looks at these things differently. It does

not generate money with sweat running down the spine anymore, as the amount of consumption becomes excessive in many ways. This society, the backbone of which consists of the middle class, does not struggle with economic misfortunes – it simply fences itself off from poverty. High-standard comforts, exclusivity and quality of life replace the ownership of an apartment, an automobile or a country house as the main criteria of success and prosperity. Spare time also becomes a crucial value.

A changing configuration of the relationship between the center and provinces is the third hallmark of postindustrial society. These relations become more complex and do not boil down to a simple formula under which the capital exists as a pump for sucking the provinces dry. Instead, the system of territorial governance receives an overhaul. An open economy that has little restraint on communications and transcends administrative borders demands that equal importance be given to vertical and horizontal relations. It also demands that the coordination of interests replace subordination. The coordination of plans increases, pushing competition aside, and is substituted by external investment and external demand, on the one hand, and the redistribution of roles and exchange of services, on the other.

THE CITY'S HUB FUNCTIONS AND SOCIAL STABILITY

Anyone who defines the strategy of a city's development as a 'network junction' has to admit that the city is embedded in several dimensional systems at any given time. Therefore, the goals of strategic development differ in each case, requiring a diversity of political instruments and concrete steps. The process of globalization has vastly expanded the dimensional relationships and opportunities of the urban areas, and increased the variety of options for development that provide for variable degrees of participation in global and local processes. An intertwining of these two concepts means that the old forms of governmental mobilization based on the *monopoly-concentration-competition triad*, which used to secure economic growth, have

become far less efficient in terms of practicality, although they have not lost their significance altogether.

In light of the dominant role that the junction functions of large cities play (with economic concentration and competition as guidelines), all the flows are drawn into the most powerful focal points of the economic space. The policy of territorial administration based on these principles resembles a casting to a club of select personalities, and the local elites are fighting with all their might to gain membership. Yet the artificial selection of “the most powerful” centers slashes the number of centers that are capable of structuring a space around themselves and ensuring regional integration. Thus, wealthy centers emerge – “dissociated islands... surrounded by impoverished lumpenplanet” (Riccardo Petrella, 1995). This policy has a side effect in the form of a gradual decay of the once united space of the country, and signs of this process are visible already now.

In the meantime, the abovementioned process is not inevitable and it can be channeled to a different direction by leveling off disparities between territories. This will be possible if city development strategies revolve around a different triad, namely, ***mobility-coordination-specialization***.

Mobility implies that interdependence becomes prevalent over geographic proximity and administrative subordination, and accessibility turns into a key parameter for development. These factors reduce the levels of centralization in a natural way and help make the population's living standards more equal across the board. ***Coordination*** is impossible without an openness of information and a search for a balance of interests. Competition and competitive advantages must not hamper a neighbor in this case but, rather, bring benefits to society. Finally, ***specialization*** means not so much a buildup of competitive advantages but rather a complementary relationship amidst high levels of development of a particular branch of the economy in each city, given its importance for society as a whole. Apart from a growing autonomy in the decision-making process of each urban area, the tapping of a city's identity implies the importance of coordinated actions, the redistribu-

tion of functions. Furthermore, it implies the responsibility among the centers of various levels, together with an intensified exchange of services.

In other words, the currently predominant logic of ‘power and money concentration’ runs into a systemic contradiction with the logic of ‘concerted effort,’ which emphasizes the relations of partnership, as opposed to the command-and-administrative methods.

Illustrative in this context are classic examples of the global cities concept as regards the driving forces of development. Although many Russian cities can scarcely hope to achieve such a status, many of the approaches to the global cities concept have relevance for us, too. Peter Taylor, for example, believes that the transformation of cities into hubs of the global economy arises from multinational companies, which demand financial services, high-speed transportation, marketing, consumer options, etc. Hierarchic relations emerging in networks of cities and, consequently, the central roles they play are derivatives of the companies’ business strategies. The presence – or absence – of a major corporate headquarters, the proliferation of globally acclaimed brands, and a high rate of international flights are all indicators that a particular city falls into the category of ‘global.’ Add to this the institutional element of globalization and the role in the global political processes that cities have inherited.

Manuel Castells offers a somewhat different approach when he suggests that the role of manufacturing is subjugated to that of information and knowledge in today’s world. *The cities engaged in the exchange of information, capitals and state power grow into “relatively freestanding ‘nodal points’ of global flows” and augment their centralizing functions* regardless of their size and geographic position. All other cities are heading for diminished status and will be eventually pushed to the periphery of major processes.

Olaf Hunners, the author of a third approach, addresses the human as opposed to the economic dimension of the city, since global cities, above all, are centers of human flows, and only then are they flows of state power, finance, and information. Hunners’

concept appeals to the city's focusing role in the global cultural process. He asks why it happens that only a handful of cities become the centers of production of a new culture and draw in huge numbers of people from around the world — and not just from nearby regions. Hunners shows that cultural productivity is transitory and that the creativity of cities dies out and re-emerges again. He perceives the cultural process in a broad format and views the city as the marketplace of culture, claiming that four very different categories of people — business executives (and especially expatriates), tourists, migrants and artistic professionals, including actors, artists and designers — give shape to that market today. All of these contemporary nomads are united by the brevity of their sojourns in a city, where they actualize their careers and creative ambitions, while maintaining close ties with their past or future residence.

It follows from all three approaches that a global city is a center generating and accepting human flows, and its internal life depends solely on its ability to adjust to the preferences of the nomads of globalization. ***Sustainable development of a global city demands its unending variability and its status as transit point is the most productive form of its existence***, determining to a great degree its image, ability for innovations, centralizing role and its engagement in global processes. It is not accidental that the 'global city' concept is developing in step with the concept of a 'dual city' which is a city of double standards or, to use the French interpretation, a city with differing rates of progress.

If one takes a look at Russian cities through the prism of Western theory, the overlapping of many tendencies and risks becomes so apparent that it will not require any special evidence. Quite obviously, Russia's largest regional centers have a very tentative access to the redistribution of global wealth and get dividends from mediating in the export of natural resources. This does not mean, however, that they do not witness the problems typical of global cities. The domestic Russian market is big enough, to say nothing of the country's size, and that is why it is the internal and not external impulses that play a key

role in the ongoing processes. As the largest cities stay inside a general flow of economic, social and cultural change, they gradually begin to act as partners, not subordinates, of the national capital, taking part to one degree or another in the economic, information and cultural exchanges. They are drawn into inter-regional and international relationships and eventually get independence on the global markets.

The basic transforming role in the largest cities in Russia, as in all industrialized countries, is taken by the **banking sector**, big corporations and main distributing networks that locate their headquarters and/or offices there.

The second crucial player that stimulates urban transits is **government** that invests certain cities with power-wielding functions. Russia has a well-tested and original technique of raising a city's status and wellbeing, and this is to enlarge an administrative and territorial entity where it is located or to create a new territorial entity and give it additional administrating powers. Take the city of Tyumen, for example, which has gained much from a partial reinstatement of its former administrative duties, which gave it the functions of a capital of three territorial units at a time – the Tyumen Region proper, the oil-rich Khanty-Mansi Autonomous Area and the natural gas-rich Yamal-Nenets Autonomous Area. The city – that once received a meager three-percent regional investment – has regained the role as distributor of tax money raised in the country's most affluent territories. One reaction to Tyumen's growing administrative importance was population growth that began in 2001, together with increasing costs of living. Tyumen's prices for housing are 15 percent higher than in Yekaterinburg, 25 percent higher than in Novosibirsk, and 30 percent higher than in Omsk. This is happening at a time when wages in Tyumen are 60 percent less than in the neighboring oil-and-gas producing areas, and only 1,500 rubles to 2,000 rubles higher than in nearby regional centers of the Urals and West Siberia. Nonetheless, the expanding financial opportunities and the imported demand for housing gave an impetus to the city's development.

Yekaterinburg, the biggest city in the Urals, is implementing a similar but somewhat different scenario. The city is the administrative center of a federal district that does not enjoy the status of a constituent territory of the Russian Federation and, consequently, does not have the necessary taxation base. Yet the authorities position Yekaterinburg as the capital of the Greater Urals and Russia's "capital number three," uniting around itself the regional and industrial centers like Tyumen, Ufa, Izhevsk, Salekhard, Orenburg, Magnitogorsk, Surgut, Khanty-Mansiisk, Chelyabinsk, Sterlitamak, Kurgan, Neftekamsk, Nefteyugansk, Nizhny Tagil, and – with some reservations – Perm. The provisory boundaries of the Greater Urals encompass a territory much broader than the geographical Ural Mountains area and even broader than the Urals Federal District. Thus, Yekaterinburg, enjoying its new status and traditional closeness to the regions of West Siberia and the Southern Urals, has not only maintained its leading position but has also expanded its influence.

The story of Rostov-on-Don, the "capital of Russia's South," looks less successful by comparison and transformation processes there are developing along a different scenario. The provisory Greater South is more multifaceted than the Greater Urals, given the presence of the North Caucasus and regions in the lower reaches of the Volga. The ethnic and cultural divergence there is so great and the transport infrastructure is so insufficient that people living in Volgograd or Astrakhan do not view Rostov as a mini-capital of some kind. This means that "South Russia" is reduced to the North Caucasus and that Rostov's zone of influence is much smaller than the territory of the Southern Federal District.

The third important factor for cities as transit points is *migrants and ramified channels of communication* (traditional transportation, as well as mobile, satellite and Internet communications) together with the uninterrupted flow of human relations and contacts. An acquaintance in Chelyabinsk I spoke to commented with sadness: "German businessmen and their investments settle in the cities Lufthansa flies to and that's why we lose to Yekaterinburg a priori."

Russia's migrant milieu is heterogeneous, as the new arrivals have diverse social and proprietary status. These people include top managers, actors and guest workers, for example, who travel to Russia for very different purposes – business, search for subsistence, tourism or performing. But they all exert strong influence on the life of each city and bring in new standards, opportunities, fashions, assessments, demands for services and lifestyles.

Take dilapidated St. Petersburg, whose feeble beauty and inherent air of decadence is now considered in vogue among Moscow's artistic glitterati, who travel and live there; they enjoy the juxtaposition of the cultural intensity of 'Northern Palmira' to the businesslike bustle of overcrowded Moscow. Now, business people have started making treks to St. Petersburg in the footsteps of the arts professionals. This has pushed housing prices there sky-high and kicked off the mushrooming of elitist apartment blocks, especially on the city's famous Vassilyevsky Island. The factor of cultural reproduction plays an important role in the image of Kazan, the capital of the constituent Republic of Tatarstan, now going through a period of ethnic and cultural revival; it is found in Yekaterinburg, which has evolved into a capital of non-conformist arts and rock culture; and in Perm, which was named the cultural capital of the Volga area in 2006.

Yet a much greater share of influence on city life belongs to the migrating business class, whose representatives fill airliners and high-speed trains. Local sociological services in Yekaterinburg, Chelyabinsk, Rostov and Krasnoyarsk say businessmen make up about 80 percent of all inter-city and international passengers.

The growing transportation flows and booming housing markets are not the only indicators of intensifying activity and mobility of qualified personnel. The rate of use of the Internet is illustrative, too. A comparison of regular opinion polls, taken by the Public Opinion Fund, and Internet indices drawn up monthly by the Yandex search engine for Russia's 50 leading cities, reveals a curious disparity between the levels of Internet accessibility and its real use (See Table 1).

Table 1. Population's Access to Internet and Web User Activity

City Name	Internet proliferation (%)		Yandex Internet index, 02.2006	City name	Internet proliferation (%)		Yandex Internet index, 02.2006
	2001	2005			2001	2005	
Moscow	29.8	35.2	-	Izhensk	-	5.9	138 (31)
St. Petersburg	13.0	20.0	-	Perm	4.56	9.0	279 (9)
Yaroslavl	-	8.9	214 (16)	Ufa	2.81	6.9	240 (13)
Ryazan	-	5.3	118 (40)	Orenburg	1.2	6.0	122 (38)
Voronezh	-	10.3	231 (14)	Yekaterinburg	7.5	12.0	494 (1)
Lipetsk				Chelyabinsk	4.29	-	287 (7)
Rostov-on-Don	4.84	15.0	178 (22)	Tyumen	-	10.0	212 (17)
Krasnodar	12.2	16.0	328 (5)	Omsk	2.0	5.6	166 (26)
Nizhni Novgorod	2.73	-	271 (10)	Novosibirsk	6.33	12.0	464 (2)
Penza	-	-	-	Baraul	1.96	6.2	140 (30)
Vologda	0.92	12.0	209 (18)	Kemerovo	2.17	-	116 (41)
Ashkani	-	-	89 (45)	Krasnoyarsk	-	7.8	271 (11)
Saratov	-	5.8	202 (19)	Irkutsk	6.71	9.0	281 (8)
Ulyanovsk	1.06	5.6	102 (43)	Khabarovsk	-	5.8	134 (34)
Kazan	3.09	13.0	267 (12)	Vladivostok	8.16	12.0	308 (6)
Samara	5.36	8.5	376 (3)	Tomsk	-	-	169 (24)

Source: Data cited from a review of Yandex's Internet index of cities (http://goroda.yandex.ru/ii_total.xml) for February 2006, and the Public Opinion Fund's research Internet In Russia/Russia In Internet, vol. 13, autumn 2005 (<http://bd.fom.ru/report/map/d051060>).

The 'dual city' phenomenon, which underscores differences between the inhabitants of cities, highlights this disparity too. It implies that a person's living standards are dependent on his or her ability to keep pace with ongoing changes. A large segment of urban dwellers live in a local world that moves slowly and has little opportunities. Then there is that part of the population that services the cities' nodal functions and exists amid the powerful current of life. These are in essence two parallel worlds coexisting in a common geographic space but confined to different social spaces at the same time. They learn about each other's problems mostly from TV.

This disunity has existed in all times, but it has become especially apparent today due to the intensifying rates of change, increasing social polarization, the transitory nature of the economy, increased significance of ties with the outside world, and differences in lifestyles.

There are few things that link together the local and global worlds today, but contact points still do exist. First, it is apparent in the 'black labor' market, the tentacles of which touch every section of society. Next come civil institutions, public associations and organizations, whose activities work for the benefit of local communities and are based on networking principles. Quite often these organizations are financed from the outside. Third, there is the Internet – not in the physical sense of infrastructure availability, but in the organizational and institutional sense.

In the past three years, regional markets of Internet services have matured into entities autonomous from the all-Russia web market. In an analogy with Ru-net (the national section of the Internet), some regional sections of the web have begun using self-names, like Novonet in Novosibirsk, Tonet in Tomsk, Irnet in Irkutsk, or Krasnet in Krasnoyarsk, etc. Almost every regional section of the Russian Internet has its own organizational structure, regional portals and news agencies. The Internet in this country is de facto made up of regional blocks that not only carry information or reflect globalization processes, but also serve as instruments for building numerous ties at the local level. They work toward strengthening the cities' identities and making them more recognizable in other parts of the country.

It appears that the key strategic objective in the development of large urban centers is melting the advantages of the cities' nodal location and networking activity into benefits for the majority of the population.

DO CITIES NEED UNIFIED DEVELOPMENT STRATEGIES?

The nodal and centralizing functions of cities have changed places today. The center city begins to play a service role for the hub city,

thus ensuring jobs where human labor can be applied, comfortable and attractive living conditions, as well as entertainment for new generations of urban nomads. Both functions are growing in equal importance and, more importantly, each dimension of city life loses its sense in the absence of the other. This situation never existed before.

Cities are acquiring new identities. They resemble one another less and less and each is seeking its own way to modernization and a unique place in the country and the world at large. But a closer examination of their strategies reveals a number of common approaches that turns their strategies – different in form and analytical content – into conceptual twins.

In the first place, those strategies idealize the future, in which everything must transform and acquire a new humanistic meaning. The program part of their strategies outline the methods of curing ailments of the past and overcoming the impact of economic decline, things which the authorities and the population are all too familiar with. These involve housing problems, the dismal quality of medical services, insignificant wages and pensions, covert and overt unemployment, the crisis-stricken education system, and the polluted and littered environment of some urban areas.

Second, the analysts drawn into strategy development mostly rely on statistics that by virtue of their origin can only reflect inertial trends without pointing to any incipient processes. The space factor of ongoing processes, the interlinks among neighboring regions evidencing a growth or decline of their population, the economic rise or decline, the proximity of urban centers that are included in or excluded from the globalization processes – all these things are more likely to determine the future of the cities than the unified statistic data.

Third, development strategies are presented as forecast documents drafting a desirable future for the urban areas. They begin with defining the mission of a particular city and its major development objectives. These strategies are of very generalized character and repeat the priorities of social policies mapped out in the Russian president's state-of-the-nation addresses. Local specifics

glimmer through the polished verbal exterior of those documents. Following these preludes are the assessments of the city's competitive advantages and the opportunities for using them. The descriptions of development resources (interpreted as the city's wealth that is capable of generating dividends on condition that current problems – typically financial ones – are solved) occupy center stage. At the top of the strategies are specific measures – or programs – designed for reaching the targets.

For all their logic, these strategy declarations resemble bombastic reports to the top hierarchy, not programs of action, since they aim to mate local ambitions with available resources.

Documents of that kind usually fail to define the principles that a city would never surrender even if it got alluring offers. These principles should reaffirm *the maintenance of identity and status of a center of decision-making with a sizable share of autonomy*. Today, as the urban centers continue to retain slivers of independence and defend their place in the ongoing social and political processes, these principles are being attacked by the government. The future of some regional capitals is at stake now: the government's idea of enlarging the regions (for example, the project of merging the Yaroslavl and Kostroma regions) puts them at risk of turning into towns of local-county, while the proposal to eliminate mayoral elections denies the people the opportunity to actively influence the life in their city. One more principle presumes transparency of decisions. Although all documents state the importance of dialog amongst the authorities, businesses and society, and ascertain civic partnership as the foundation on which to build and implement strategies, they do not mention anywhere how a greater openness in relations can be attained given the current levels of corruption.

A strategy must also provide for a *realistic assessment of the city's position with respect to its neighbors, partners and competitors*. These assessments can never be univocal and are liable to brisk changes of vectors from positive to negative depending on the situation. St. Petersburg offers a bright instance of this. It claimed at the end of the 1990s that it was the main contact center in connections between the Baltic Sea littoral countries and northwest

Russia. Today, however, it is trying to position itself from a totally different angle — as a reliable partner for Moscow that is capable of taking over from the capital some extra governmental functions. An urban metamorphosis is also evident in Nizhni Novgorod, which lost its former status as the country's main site for economic and political experiments, and is now doing its best to break out of Moscow's shadow.

The problem has another facet, however. A city's advantageous position in the system of economic and political connections is a more valuable asset for new ideologies of development than the potential accumulated over years. Proof of this is found in the success of agrarian centers, such as Belgorod and Krasnodar. The two cities have never set the tune to the style of urban development in the past, but they have managed to transform the advantages of their nodal political position into economic growth. Their future is contingent not so much on the initial rate of development or underdevelopment as on a matching of local policy with federal or international interests, as well as on contacts with major corporations and federal authorities, in which regional and city administrations act as mediators.

Last but not least, a city's development strategy must determine the degree of *maneuverability of governance*, that is, the observance of the balance between stability and liability to change, together with the necessary reforms and compensatory steps to cushion against their painful effects. In the meantime, no city strategy provides for protection against external reforming influences that might upset the balance of local forces and interests. Nor do they envision the establishment of a reform-friendly environment. For instance, no city is strategically ready to reform the public utilities sector, for example, or to enforce a law concerning the replacement of tax benefits with cash compensations. All decisions and steps in that sphere have been rather improvised.

City missions deserve a separate mentioning. Cities copy their strategies from corporate business strategies in many ways. Their internal documents position urban centers as isolated organisms, the missions of which boil down to self-development, the growing

affluence of its residents, and integration into the global economy. These objectives are honorable but the actual sense of the cities' existence and development is much broader. Cities have always had a mission to "gather lands" around them or, in other words, to consolidate the population, to integrate the country's territory and to ensure national development, and not just to take care of their own petty needs. This mainly concerns large cities. The elimination of their territorial influence voids their existence of any sense, regardless of their dominating functions. It is thanks to large cities that regions of a country – one that is characterized by vast natural, climatic, social, economic and cultural diversity – form a coherent functional space. Ensuring this coherence – through the realization of common interests as opposed to pulling at administrative levers – is the basic mission of our cities.

Around Russia



“Christianity. Civilization. Freedom.”
Russian values personified by Russian rulers – Prince Vladimir,
Emperor Peter the Great, and Emperor Alexander II. *Niva* magazine, 1899

“*Russia is not unique, or in other words, as one of Europe’s outskirts it is not more unique than its other outskirt – the United States. Today, Russia and America are very much alike. At the same time, they dramatically differ from Europe, which had an enormous historical impact on them.*”

Europe as the “Center,” and Its “Outskirts”

Vladislav Inozemtsev

148

An Audit of Russia’s Foreign Policy

Ivan Safranchuk

167

Historical Struggle for the Black Sea Fleet

Yuri Dubinin

177

Russia Must Regain the Initiative in Moldova

Zurab Todua

196

Europe as the “Center,” and Its “Outskirts”

Vladislav Inozemtsev

In the early 19th century, within a space of just eight years, two perspicacious Frenchmen – Alexis de Tocqueville and Astolphe de Custine – traveled to what were then two distant territories of Europe. They shared their impressions in two books that made a substantial impact on the educated Europeans. Until the end of the century, *Democracy in America* and *Russia in 1839* were regarded as the main socio-philosophical works about the system of governance in the United States and the Russian Empire – two European powers outreaching the geographic boundaries of Western Europe.

At that time, America and Russia were in fact the only outskirts of Europe. The East was regarded as utterly alien, while the colonies were not taken into account. At the same time, the United States was often considered as a more perfect social system, whereas Russia was associated with a kind of backward system. It seemed that the “outskirts” were as different from the “center” as they could possibly be. But the next 150 years would upset that view.

In the early 20th century, the United States made a dramatic breakthrough, emerging as the world’s most advanced economy and a “promised land” for millions of European immigrants. Soon

Vladislav Inozemtsev, Dr. Sc. (Economics), is Editor-in-Chief of the Russian edition of *Le Monde Diplomatique*; Publisher and Editor-in-Chief of the *Svobodnaya Mysl* monthly; professor at the Higher School of Economics in Moscow.

after that, a revolution took place in Russia, causing millions of people to focus their attention on the Soviet Union. Within the space of just three decades, America and Russia twice dragged Europe out from the bloody wars into which it had plunged itself. As a result, the new geopolitical rivals effectively divided the continent between themselves. In the middle of the century, both superpowers easily overtook the Old World in the technological sphere – first, by creating nuclear weapons and then by traveling into outer space. Perceptions about the “center” and the “outskirts” were changing rapidly, and they were destined to change even more.

The end of the 20th century was as rich in events as it was at the beginning. The Soviet Union, which had laid claim to economic leadership, and had declared the creation of a “new historical communality of people,” succumbed to a relentless arms race that peaked just as the prices of raw materials collapsed. The Communist empire eventually disintegrated along the borderlines between its national republics. As a result, the new Russia immediately lost its former weight in international affairs, while its citizens started to plunder the formerly “public” wealth by hook or by crook. Taking advantage of the situation, the United States gave free rein to its imperial aspirations, its geopolitical perceptions differing little from those that had existed in Europe shortly before World War I. Today, just a decade after America emerged victorious from the Cold War, it finds itself involved in a conflict with almost the entire Muslim world, which, incidentally, is rather characteristic of the United States in terms of its blind religiosity and tunnel vision. The outcome of this confrontation is far from clear yet.

Meanwhile, the Europeans, unlike their neighbors, avoided any rash moves. Yet in the 1990s their integration project produced the best possible results: the EEC transformed into the European Union, the euro was introduced, while the number of EU members more than doubled from 12 to 25. Europe was freed from the danger from the Soviet Union, and, at the same time, overcame its slavish dependence on the United States. As a result, the world of the second half of the 20th century, which was comprised of

“two Europes and one West,” became history. It was replaced by the world of the 21st century with “one Europe and two Wests.” The Europeans looked once again at their continent if not as a military-political powerhouse then at least as a region that generates the boldest social innovations. New books about an early and imminent triumph of the European Dream over the American Dream filled bookstore shelves to overflowing.

As for the Russian Dream, it is practically invisible; the country has yet to recover from the intellectual stupor into which it fell in the early 1990s. Not even the radical change of the economic and political climate at the start of the 21st century has caused any serious changes in the mentality of the Russian political class. Domestic thinkers continue to insist: “We must remain different from everyone else.” Proponents of “Eurasianism” and “*sobornost*” [a notion used to describe society as a body, organically gathered around a common culture, heritage and belief – Ed.] act on the assumption that Russia is different from all other societies, although they would do better to prove this thesis, not take it for granted. This postulate seems erroneous to me, while this article is an attempt to argue that Russia is not unique, or in other words, that as one of Europe’s outskirts it is not more unique than its other outskirt – the United States. Today, Russia and America are very much alike. At the same time, they dramatically differ from Europe, which had an enormous historical impact on them. This is a very difficult argument to prove, so I would just like to point to some similarities, while avoiding the philosophical rhetoric. How substantial are these similarities I will leave up to the reader to judge.

“SENSE OF A NATION”

The first thing that strikes the eye when making a comparison between the United States and Russia is their remarkable similarity as very special people – “chosen” and “messianic.” Of course, the majority of European nations also have their own perceptions of their historic role and mission, which are not always very modest or even tenable. But there is good reason to say that all great

European nations base their unique identity on their history and tradition, drawing on them as a source of inspiration and confidence in the future. The European concept of the nation, built on a common history, ethnic origin and language traditions, evolved as early as the 18th-19th centuries. To date, it remains an undisputed concept in the Old World. Ideological or religious views bear no relation to "Europeanness." Winston Churchill was among the first people to formulate this idea in a pointedly polemical form. Addressing the House of Commons in 1940, he slammed a move to ban the Communist Party of Great Britain, stressing that there were no convictions that could make a Briton "un-British." European tolerance, which sometimes appears excessive, arises from this orientation toward past and present values, but not toward the illusions of the future. And that is unlikely to change any time soon.

The United States is organized differently. Ever since the 17th century, when the first European settlers started to conceive of themselves as a nation, they have regarded themselves as the "best," "God's chosen," who are destined to build a "new Promised Land" across the ocean, a "City upon a hill," and a second Jerusalem, from where the light of the divine truth would spread throughout the world.

This is hardly surprising. The new nation could not have looked for its own unique identity in history (which did not exist), nor could it avoid to set ambitious goals (because such goals were set by all individuals it was comprised of). Throughout the first 150 years of its history, the United States remained a settler society that was in a constant state of mobilization, which also created a sense of mission and chosenness. At the same time, America successfully played on its "opposition" to Europe. Whereas the Europeans sought to "civilize" the world, wasting substantial resources in the effort, the Americans were disingenuously "cleansing" vast tracts of land on their continent from the natives and using them to their own ends. Whereas the Europeans were losing hundreds of thousands of their fellow citizens in colonial wars or emigration, the Americans were evolving as a powerful

nation with a massive inflow of new colonists. This path of development topped out in the 20th century, when by the end of World War I the United States had emerged as the world's biggest economic powerhouse, and after World War II as the world's sole military superpower. All of this strengthened the Americans' belief in their nation's mission.

While recognizing the outstanding qualities of the Americans as a nation, it is difficult to shake off the impression that they owe their main successes to the others' faults rather than to their own achievements.

America forgot that it was not the one to invent the universal principles that it was supposed to bring to the world. Rather, it was a bare offshoot of European civilization. Over time the Americans developed a strong "natural" sense of responsibility for the world: today this is all the more surprising considering that the United States has for 30 years been dependent on the willingness of other countries to invest substantial resources into its economy and supply it with goods in exchange for cheapening greenbacks. The path the country is following is extremely dangerous, but it arises from the Americans' confidence that they will succeed.

Russia also represents an offshoot of European civilization. Its history is no less remarkable than American history, but at the same time is quite similar to it. Russia was twice Europeanized. This happened first in the 9th-11th centuries, when the eastern version of Christianity was adopted as a dominant religion (which put the Russians into the Byzantine "zone of influence"). In the 13th century, Byzantium and Rus (ancient Russia) almost simultaneously underwent trying ordeals (which started in 1204 and 1237, respectively). Importantly, Byzantium did not survive the ordeals, whereas Muscovy, which had acquired the Byzantine tradition of a secular power's domination over religious authority, identified itself as a "third Rome" – that is, almost a direct successor to the ancient civilization.

Russia turned to Europe for a second time when it was clearly lagging behind the main centers of Western civilization, paradoxically attempting to use European practices to defend itself against

the Europeans. The results were quite impressive: Russia emerged as the leading power in the Old World, strengthening its “Eurasian” identity through eastward expansion and once again seeing itself as the divine “savior” of Europe — this time not only from the fierce Mongolian hordes but also from Bonaparte the usurper.

By the late 19th century, Russia had become formally a European country, but remained “outside” Europe in terms of its territory and population. Its people were affected by their self-perception as unique (“Eurasian”) and “God’s chosen” — a perception that, just like in America, obviously had a religious basis. Russia, just like the United States, was a European and at the same time non-European country. Looking back over the years, one is amazed to see that our two countries abolished serfdom and slavery almost simultaneously (but retained social inequality for a long time) and that their search for identity and a role in the world was also very similar (consider the lively debate between the Slavophiles and Westerners in Russia, and the isolationists and expansionists in the U.S.). Everything changed, however, after World War I. At that time, the United States and Russia, which emerged from the 1917-22 upheavals as the Union of Soviet Socialist Republics, showed their global historic aims and prospects.

For the greater part of the 20th century, the essential similarities between the Soviet Union and the United States were not yet clearly understood. The two great ideological powers, resolved to accomplish their historic missions, were the only countries in the world whose names did not contain the slightest indication as to their historical and ethnic roots (the U.S.S.R even surpassed the U.S. in that respect by removing any reference to geographic identity, although we may recall Leon Trotsky’s proposal that the new Communist state should be called the “Union of Soviet Republics of Europe and Asia”). Both powers were equally obsessed with the ideas of a classless and supra-national society (the concept of the middle class in the United States and ‘elimination of class-based differences’ in the Soviet Union; the ‘melting pot’ in the United States and the ‘new historical communality’ in the Soviet Union). They were more or less equally attracted by the power of univer-

sal ideas (freedom and democracy in the United States and the elimination of exploitation and the assertion of social justice in the Soviet Union). They were almost equally enthralled by the opportunities opened by technological progress, as well as by the potentialities of their vast territories. By emerging as winners in World War II, they proved – to themselves, as well as to everyone else – the power of their ideologies and social foundations, and the broad horizons that they had for further development.

Nevertheless, the historical outcome of the 20th century turned out to be a totally different experience for the United States and the Soviet Union. This statement is not in conflict with the postulate concerning the similarities between these two states, suggesting, rather, that they manifested themselves at different periods. The United States, being less etatist (in other words, more “European” than the Soviet Union), had no (nor did it seek any) opportunities to mobilize and overstrain its internal resources – it was partly for that reason that it not so much defeated as outlived the Soviet Union. Presently, it is difficult to predict what is going to happen with Russia in the 21st century. Its territory and population has decreased considerably, while the Communist idea, central to the Soviet Union, collapsed completely with nothing to replace it. Meanwhile, Russia has preserved its “Eurasian identity;” the Europeans do not see it as a natural part of Europe, nor do many Russians for that matter. At the same time, the Russian system of state governance and its instruments have changed little compared with what they were before.

These days, Russia – like the United States but unlike the European countries – does not cast itself as “one of many” states in a diverse world, nor does it search for normalcy in its European sense.

ATTITUDES TO THE WORLD

There is also a remarkable similarity in the attitudes to the world that are typical of the United States and Russia. This seems to be based on the history of the two European outskirts combining, first, prolonged periods of expansion; second, a predetermined

space over which these countries could spread their influence; and third, their political influence, which sometimes substantially exceeded their economic power.

The striving for territorial expansion is a characteristic feature of almost all European states. Their territorial gains can only be compared with the nomadic invasions of the 4th-13th centuries. Furthermore, as Asian expansion subsided (the last military expeditions by the Arabs occurred in the 7th-10th centuries and by the Turks in the 15th-17th centuries), European empires continued to gain momentum.

From this perspective, there are two similarities between Russia and the U.S. that set them apart from West European countries. On the one hand, their expansion did not occur at the expense of European possessions. Russia smashed the Ottoman Empire, defeated Sweden and Prussia, vanquished Napoleon, and took control of the Caucasus and Central Asia only in the "European," post-Petrine period of its history. The United States was essentially a European country, asserting its domination in North America by using European experience and immigrants from the Old World.

On the other hand, unlike European countries — Spain, France, and Great Britain — neither Russia nor the United States established global empires in the European meaning of the term. By constantly expanding their own territories, they evolved as continental powers, seeking little control over territories lying far beyond their borders. This predetermines one of their most fundamental differences from Europe: Old World countries have already passed the peak of their expansionist drive, whereas many in Russia believe (while in the United States they are even convinced) that they have yet to reach their zenith. The opposition between the European and "periphery" approaches is reflected in current political rhetoric.

Unlike the European countries, Russia and the United States throughout the 19th century and during the first half of the 20th century had an insignificant global presence. Until World War II, they remained continental powers with no experience in building overseas empires. It is noteworthy that as soon as the Soviet

Union and the United States strengthened militarily, their rivalry sparked serious armed conflicts in the global periphery – from the Korean Peninsula and Indochina to Mozambique and Congo, and from Egypt and Syria to Cuba and Chile (it is equally noteworthy that the European countries had not been involved in colonial wars with each other since the late 18th century). They built their policy primarily on their geopolitical interests and ideological goals, whereas the Europeans were looking for economic advantages, and when the latter disappeared, colonialist practices swiftly discontinued in the 1960s-80s. Neither the maintenance nor the loss of colonies caused economic upheavals in Europe. On the other hand, the striving for global leadership bled the Soviet Union dry, thus leading to its collapse, while today the United States continues to enthusiastically follow this path.

Such a historical legacy seriously distorts Russia's and America's attitude toward the world. Both tend to exaggerate the role of force in modern international relations and the possibility of defeating an adversary with state-of-the-art weapons. Russian and U.S. strategists act on the premise that the enemy must be destroyed, not put under control. Both Russia and the United States consider themselves to be centers of global politics, treating the rest of the world as an area where they can find allies but not any models to replicate. They are often plagued by the question: "Who are our allies?" but never ask themselves: "Whose allies could we become?"

The modern European countries have none of this arrogance, and this fact makes them far more adaptable to the political realities of the 21st century. Both Russia and the U.S. regard the outside world above all as a source of threats; the rhetoric of their incumbent leaders makes this abundantly evident. The Europeans, on the contrary, regard the world, rather, as a source of challenges than threats, and are acting accordingly.

Finally, unlike the United States, which is attempting to impose its values on the world, and Russia, which since the Soviet times has been laying claim to a unique vision of the future, the Europeans have no interest in exporting their model of development to the rest of the world.

It is also important to note that the economic development not only of Russia but also of the United States is lagging behind their political aspirations. During the imperial era, Great Britain and France were the largest net exporters of industrial goods and capital, while the European continent was the world's largest exporter of people. Today, Russia and the U.S. are far away from these trends. It is also important that the Europeans (it is essential to remember in this context that Russia shared all of their hardships) rebuilt their continent twice after the two world wars, so the claims that the U.S. showed higher economic growth in the 20th century have little relation to reality. The fate of the Soviet Union shows how dangerous the gap between political and economic capabilities can be. The U.S. is also beginning to appreciate the danger.

INDIVIDUAL AND SOCIETY;
CITIZEN AND THE STATE

Indicative of the similarities between the outskirts and their difference from the center are specific problems – e.g., the social structure, relationships between the individual and society and the citizen and the state, and the level of socialization – although they can be less pronounced than in the geopolitical realm.

The only point on which there seems to be no direct similarity between Russia and America is the relationship between the individual and the state. In the U.S., government and political authority appear to be forces that are separate from society, although not hostile toward it. A political career is less prestigious than a business career, while politicians do not enjoy much public credibility. This is partly due to the dual attitude toward government on the part of the American people: on the one hand, the country was built as a model of self-governance, while political authority was limited until the early 20th century; on the other, the present status of the United States, and the status of the decisions made in Washington require strong governing authority with broad powers. The right balance has normally been struck via judicial rulings; this is why modern America is rather a country of courts and precedents than of laws. The ruling authorities are so

concerned by domestic security that the U.S. could be described as a land of criminals (2.09 million individuals are behind bars in prisons and jails, which makes 715 people per 100,000 – that is to say, 600 percent higher than in the EU with 103 per 100,000).

In Russia, the state is a kind of an antipode to society – “a society within society,” which is effectively separated from it. The governing authority has never been perceived as originating from the will of the people or as representing it. Although the prestige of the civil service is high, bureaucracy has minimal public credibility. The system of governance is not balanced with either the individual economic autonomy or an independent judiciary; at the same time, there is little opposition to “strong government” on the grassroots level. As is well known, strict Russian laws are counterbalanced by their loose observance. This reality is somewhat similar to the American practice of optional law enforcement through well-debugged system of defense counseling. But just as in the U.S., the ruling authorities in Russia are not particularly concerned with assisting its citizens. Instead, they readily seize on the opportunity of shifting the focus from economic to security problems (as in the U.S., 0.53 percent of Russia’s population is in prison, while up to 15 percent of the working-age population are employed in the Armed Forces, state security organizations, law enforcement or private security agencies).

Unlike the U.S. and Russia, the state in the EU countries plays a different role in society’s life, performing different functions. First, the share of GDP re-distributed through the budgets of the 25 EU countries stands at 47.8 percent, as compared with 28 percent in the U.S. and 29 percent in Russia. Second, the share of spending on external and internal security programs in the EU is 3-4 percent of GDP, whereas in Russia and America it is close to 10 percent. Third, the Europeans tend to respond more aggressively to any attempts by the state to infringe upon their rights (in Europe, participation in demonstrations, strikes and other protest actions is 14 times higher than in the United States, while there is no way this indicator can be reasonably compared with the situation in Russia). Fourth, EU governments are more socially orient-

ed than in the U.S. or Russia: fifteen EU countries spend up to 60 percent of their budgets on social programs, as compared with 38 percent in the United States and a mere 18 percent in Russia. Over the centuries, the Europeans have developed a respect for the law, treating their rulers as community's servants. In the United States (to a lesser degree) and in Russia (to a greater degree), the state is separated from society, telling it how to act. The majority of the people in those countries do not expect any help from the state, seeking to reduce the scale of their obligations to it by any means.

The place of the state in society is predetermined above all by the nature of relations between the people, and here the differences between the center and the outskirts become increasingly pronounced. Reality belies the purported collectivism and communality of the Russians/Eurasians. What does collectivism have to do with a society where fences are built not only around luxury country homes, but also around poor men's graves at village cemeteries? A society that has long lost the ability to formulate its interests unless being prompted by the state-controlled media? A society where glaring social inequality arouses no protests? A society whose members are almost not involved in any forms of social activism except for purely formal membership in officially allowed political parties? Probably the most reliable communality indicator is known as the Gini coefficient [a measure of inequality of wealth distribution], which is virtually the same in Russia and the United States. Today, according to official statistics, 10 percent of Russia's wealthy possesses 16 times as much national wealth as the poorest 10 percent (in the United States, it is 14.8 times higher, while in the EU-15 it is 7.6).

America and Russia are rigid individualistic societies going through — for different reasons — a phase that Europe passed if not in the late 19th century, then soon after World War II (this is not to suggest that France or Italy are model collectivist societies, but rather that Europe, where the state has assumed the role of a social protector, has found a counterweight to wild individualism).

This of course is rooted in the attitude to religion where the Europeans are heading into one direction whereas the Americans

and Russians are moving in the opposite. Before World War I, the level of religiosity of all three societies was quite comparable. Today, people in the majority of European countries (except perhaps for Poland) who describe themselves as religious are clearly in the minority. However, in America and Russia, the share of citizens saying religion occupies an important or very important place in their life is steadily growing. In contrast with Europe, the ruling elites inside Russia and the U.S. are increasingly using religion as a means for reaching their political goals.

It will never occur to any head of state in a European country to explain his foreign policy decisions by directives received straight from God (as does George W. Bush). Nowhere in Europe will a pontiff consider it fitting (as does Patriarch Alexy II of Russia) to thank his president obsequiously for the wonderful life that his flock enjoys under his wise leadership. The United States and Russia are far ahead of the rest of the world according to the scale on which religious sermons and services are broadcast live, as well as in the frequency and duration of presentations by religious figures on the radio and television (in this respect, only Islamic states can compete with them). Both countries are seeing the vigorous development of “nationally specific” trends of Christianity (Orthodoxy in Russia and Protestantism and Christian sectarianism in the United States). Finally, both the U.S. and Russia are effectively competing in invoking and tapping the supreme forces to deal with economic problems: the Americans remind every bearer of U.S. dollars that “In God We Trust,” while top corporate executives in Russia sincerely hope that the domestic automotive industry will perform better since St. John the Baptist’s relics were brought to the AvtoVAZ car-making plant.

One can argue about the specifics of American and Russian religiosity, but it is clear that while the population of Europe is becoming increasingly indifferent to religion, both outskirts rely on religious-messianic rhetoric to strengthen their identities.

In closing this section, I would venture to suggest that Europe is gradually turning into a kind of a community of personalities, whereas the United States and Russia are not only preserving but

are also consolidating a society of citizens (or even subjects). The cohesiveness of the Europeans is built on natural social solidarity, whereas the cohesiveness of the Russians and Americans is based on extolling their not entirely indisputable values, as well as on the mobilization of efforts to attain some equally dubious goals. Without suggesting that one model is better than the other, I only attempt to show the differences between them.

ECONOMIC REALITIES

Money as a measure of economic success is perhaps one of the most notable things that the two outskirts have in common, setting them apart from Europe. In America (and nowadays also in Russia), money is an object of worship, a yardstick of personal success, and a basic criterion of social value. The effect of such an attitude is, on the one hand, growing social stratification and, on the other, an economy that is oriented toward the immediate pocketing of profits as opposed to the maximization of public benefit. It would be appropriate in this context to recall, for instance, the lack of any effort to make a more effective use of resources in the United States or managerial decisions in Russia that are reckless from the standpoint of social benefit but "useful" for individual businessmen and government officials. Unlike Europe, where the incomes of corporate executives rarely exceed those of their employees by more than 30 times, in the United States executives at major corporations can make 160 to 250 times (some experts argue this ratio exceeds 400 times) as much as their employees, while in Russia the gap is even more glaring.

The formation of narrow groups of individuals receiving excessive incomes leads to the merging of business and political elites, which is less pronounced in Europe. In the United States, a country with longer and more stable entrepreneurial traditions, the general movement is from business to politics: for example, many officials in the Bush administration formerly held positions in businesses whose interests they openly lobbied for in government. In Russia, the trend is rather the reverse: government officials use every opportunity not only to enrich themselves, but also to

acquire effective control over commercial structures. In Europe — unlike America and Russia — access to society's upper levels depends not so much on one's financial status as on one's social, cultural or intellectual proximity to members within these elite. The merging of corporate and state governance functions is rare and usually purely formal, without much real control.

Such differences between the economic priorities of the outskirts and the center have manifested themselves in the imbalance and ineffectiveness of the Russian and American economic systems. Today, the EU produces 10 percent more cars than the U.S., 60 percent more chemical products, 75 percent more pharmaceuticals, and 100 percent more steel, while in the textile and light industries the disparity is even wider.

As for Russia, in the 1990s it ceased to exist as an industrial power, becoming instead a “pipeline economy.” Needless to say, this scenario has little in common with the United States, but it has to be recognized that in the late 20th century both outskirts effectively dismantled their industrial facilities. Today, U.S. imports exceed exports by \$800 billion a year, while Russia's trade surplus is based on high prices for raw materials, which will be shaved off if the price of oil falls to \$37 per barrel. There are growing signs of parasitism: the rapid increase in immigration as the primary source of a workforce has been equally characteristic of the United States since the late 1980s and of Russia since the early 2000s. The governments of both countries strive to control not the production of goods, but rather the transport, information, and financial infrastructures. In the United States, this manifests itself in the increasing role of financial, banking and brokerage services in the economic realm, as well as in control over global information networks. Russia, following the strategy of an “economic superpower,” positions itself as a network of oil and gas pipelines, and is obsessed with the idea of becoming a “bridge” between Europe and Asia in the new century. However, historical practice shows that not a single great nation has ever managed to retain its political influence amid a lack of competitiveness and declining production.

This does not mean that the outskirts are now lagging behind the center that is far in the lead. But the fact remains that Europe's economic development today seems to be more balanced than that of Russia or the United States. This is apparent by Europe's greater focus on intensive economic growth, steady reduction of working hours, tighter environmental standards, and the balance of trade, as well as, e.g., the degree to which high-tech products, initially developed in the U.S., penetrate American and European consumer markets. It is an open secret that the percentage of people who use mobile communication technology in the United States is about 56 percent, as compared with almost 100 percent in the EU. Meanwhile, only 19 percent of new American cars are equipped with GPS systems, as compared with Europe's 65 percent. The U.S. maintains a lead only in the use of the Internet (which is regularly used by 56.7 percent of the Americans, as compared to 44.2 percent of the Europeans). As for Russian inventions that gained recognition in the West while being ignored in Russia, it is impossible to make even a rough estimate here.

In other words, although the Europeans' creative potential may be inferior to America's or Russia's, the Europeans are unrivaled in implementing technological achievements to improve the quality of their daily life.

CONSUMER PREFERENCES

Many social, economic and even political processes in the modern world are reflected in consumer preferences and behavior stereotypes. There are also some differences between Europe and its outskirts that have evolved over decades.

In the United States and in Russia, the individual is perceived (and perceives himself) above all as a consumer. His principal preoccupation is to buy more and buy cheaper and, if possible, of better quality. This process has assumed the most exaggerated forms in America. Suffice it to consider the main idea of most advertising campaigns: now the consumer can get more for the same price (a second hamburger, 30 percent more of coca cola, 50 percent more of detergent, etc.)! When a consumer boom runs

out of steam, large-scale lending programs feed it; the principal message is that there will always be enough money. Meanwhile, the greatest threat for the consumer is “pleasure denied.”

In Russia, almost all of these trends are reproduced in those social groups that are approaching Western consumption standards. Today, Russia is the most lucrative and dynamic market for Western retail chains and supermarkets. Sales on credit are growing 30-40 percent each year, and sales of luxury cars are growing at the same rate. At the same time, wealth in Russia has acquired cult status, regardless of its source. Print and electronic media are promoting this image: “New Russians” are the masters of life, whereas all other people – those who cannot afford such a lifestyle – are just a gray mass slavishly following the new elite. Spiritual poverty is even becoming an object of pride. A middle-aged Russian woman who visited Paris on a very cheap bus tour described the French capital as “nothing special – in Moscow, the cars are much cooler.” It does not even occur to people that those “cool cars” were bought with money that was stolen from them. Many Americans, too, do not realize that America’s “grandeur” is a peculiar trait that the people in a majority of countries do not want to reproduce.

While developing as consumer societies, America and Russia are similar in their bigotry for luxury, which oftentimes becomes the only thing that distinguishes the “elite” from the “masses,” which otherwise are like two peas in a pod. In the United States, the word “luxury” is applied to makeshift houses in Florida, giant gas-guzzling SUVs, the seats of which look more like couches from the past century, any clothes except blue jeans, and almost all hotels except those located along major highways. In Russia, “luxury” became equated with “elitism” (which emphasizes the importance of wealth and status in the public eye). “Elitist” is applied to everything from gold-plated jewelry to cosmetics, from restaurants to cars, and from apartments to country homes. There are even advertisements for the wholesale shipment of “elite toilet paper.” It seems that almost everyone, except for the really poor, can partake of this “elitism” without even stopping to think about the real meaning of the word.

All of this is at odds with the European approach, where the word “elitist” is never used in advertising, while the word “luxury” is used very rarely (being substituted with “upscale” and “private” – e.g. for advertising nightclubs).

Yet another distinguishing feature of the United States and Russia that is alien to Europe is the level of deception, large and small, that confronts any first-time visitor to either of the two countries. For example, in the U.S., all prices are indicated without taxes, so real price of an item may be up to 25 percent higher. “Suggested gratuity,” which adds up to 20 percent to a restaurant bill, can be especially baffling. And then a cab passenger who pays \$5 on top of the \$15 shown on the meter is asked for a tip; this scenario has become rather commonplace. Given that the sphere of the services industry (where a consumer comes into direct contact with a service provider) generates about two-fifths of American GDP, the volume of unregistered financial transactions can in fact account for as much as 8-10 percent of GDP.

In Russia, the role of American cab drivers and bartenders is played by clerks and civil servants: it is an open secret that in addition to the official price, the cost of services provided by the so-called ‘state unitary enterprises’ also includes kickbacks, gratuities, and so on. According to some estimates, this low-level corruption in Russia is put at 10-15 percent of GDP.

Whenever I visit the United States after traveling in Europe, I have a sense of provincialism clumsily hidden by beautiful packaging. Foreign visitors coming to Russia also get this feeling – not immediately though, but as they start judging it beyond the appearance of the store shelves.

* * *

In conclusion, I would like to point to yet another circumstance that speaks volumes about America and Russia. There is a common belief that the United States was made into a great country by people who were driven by the American Dream. The popularity of this dream explains why America has been unaffected by public movements that are so typical in Europe: the Americans in

their majority eschew the European tradition of striving for income equality in favor of the equality of opportunities. It is noteworthy that Russia (except for the late 19th-early 20th centuries, when it built the closest rapprochement with Europe) also has not seen egalitarian movements. Can it be that this passivism stems from the same illusion that so successfully immobilizes public movements in the United States? It seems to me that some parallels could be drawn between the American and Russian dreams insofar as it concerns the principles underlying the organization of their societies.

The American Dream glorifies success much more than those who have achieved it. At the same time, the Americans praise the capitalist system based on personal liberties, economic independence and freedom – as the core element of their society. Does the Russian Dream resemble the American one? Yes and no. As distinct from the Americans, the Russians perceive society as centered around the state, rather than the market. It is indicative that nothing arouses so much contempt and hostility in Russian society as corrupt and inefficient state and government officials, but at the same time the president, who appointed many of them and effectively placed them above the law, has huge public credibility as a symbol of the state. Is this not reminiscent of the Americans' attitude toward successful capitalists and capitalism in general?

So, up to a certain point, the Russian approach is similar to the American one: yes, the governing authorities in Russia are indifferent to their citizens, but a substantial part of these citizens also naively believe that they can eventually join them, just like a street vendor in a provincial American town hopes to become a millionaire. Even the Russian democrats in the early 1990s drafted an essentially authoritarian Constitution – in part because they wrote it to suit themselves, not the country as a whole. It is this harboring of rosy illusions, as opposed to a degree of normalcy, that characterizes both the Russians and the Americans, and establishes the striking difference between themselves and the Europeans.

An Audit of Russia's Foreign Policy

Ivan Safranchuk

How much does Russia's foreign policy cost? This seemingly simple question is actually very difficult to answer. First, foreign policy comprises a huge number of many diverse processes and factors, and these are not easy to evaluate in terms of money. Second, many parts of Russia's federal budget that concern foreign policy are either too general or they are classified. Finally, the amount of available information on different foreign-policy sectors differs considerably.

Nevertheless, this article is an attempt to analyze Russia's budget spending on foreign policy. A generalization of these spending figures has produced interesting and, at the same time, contradictory results, making it difficult to draw any unequivocal conclusions on their basis. Yet an analysis of the situation, presented with diagrams and graphs, is very useful and provides much food for thought.

SOME METHODOLOGICAL EXPLANATIONS

Russia's budget spending is classified into three categories. These include functional (budget allocations for national defense, police, state security, education, etc.), departmental (allocations among government agencies) and economic.

First, there is no item listed under "foreign policy" in the functional distribution of spending. Rather, it is financed from a sub-

Ivan Safranchuk, Doctor of Science (Politics), is director of the Moscow office of the World Security Institute.

item category called “International Relations and International Cooperation” (before 2005 it was called “International Cooperation”), which is included in the “General State Spending” item. However, business trips abroad and international contacts of all state organizations, such as the Audit Chamber, the Federal Tariffs Service, the Ministry for Regional Development, etc., are financed from the same source. So, as regards functional classification, allocations for foreign policy and diplomacy merge with other spending.

It would be logical to assume that the “cost” of foreign policy will be apparent from the departmental classification. Theoretically, the budget of the Foreign Ministry (in former years also the Ministry for CIS Affairs, the Ministry for Cooperation with the CIS Countries, and the Russian Center for International Cooperation in Science and Culture under the Foreign Ministry) must reflect all foreign-policy allocations. But things are not that simple. For example, allocations for the Foreign Ministry in 2000 in the open (unclassified) variant of the federal budget stood at 589 million rubles; in 2001 they made 706 million rubles, and in 2002, 1,065 million (all the sums are given in current prices).

Apparently, everything seems clear: the budget of the Foreign Ministry is small but growing (even if adjusted for inflation). However, if we look at the budget execution report for 2001, we will find the figure of 13.5 billion rubles (instead of 706 million). The point is not that the spending proved to be much greater than planned, although such things happen and we will discuss that scenario below. The point is that not all foreign-policy allocations were made through the Foreign Ministry. For example, the international organizations’ dues and other expenditures involved in foreign-policy activity were for many years paid through the Ministry of Finance. (In 2001, part of the expenditures was paid from the budget of the Ministry of Finance, although the budget execution report attributed this spending to the Foreign Ministry’s budget.) For this and other reasons, in 1995-2001 the Foreign Ministry received meager allocations in the open variant of the federal budget. It would seem that one could simply look at cor-

responding categories and sub-categories in the departmental classification of the Finance Ministry's spending and add the expenditures specified there to the foreign-policy budget. However, in some years the Finance Ministry was not mentioned in open variants of the departmental classification of spending.

Given these factors, the author has worked out his own method for estimating Russia's expenditures on foreign policy. In brief, these expenditures include:

- allocations under the sub-category of “International Relations and International Cooperation,” received by the Foreign Ministry (minus allocations for “Implementation of Interstate Agreements Within the CIS Frameworks,” also received by the ministry);

- all allocations for “Implementation of Interstate Agreements Within the CIS Frameworks.” Although this budget item is included in the sub-category entitled, “International Relations and International Cooperation,” I have singled it out because allocations for this purpose are not made through the Foreign Ministry alone;

- allocations received by the Foreign Ministry under other categories and sub-categories of the functional classification (for education, construction, etc.).

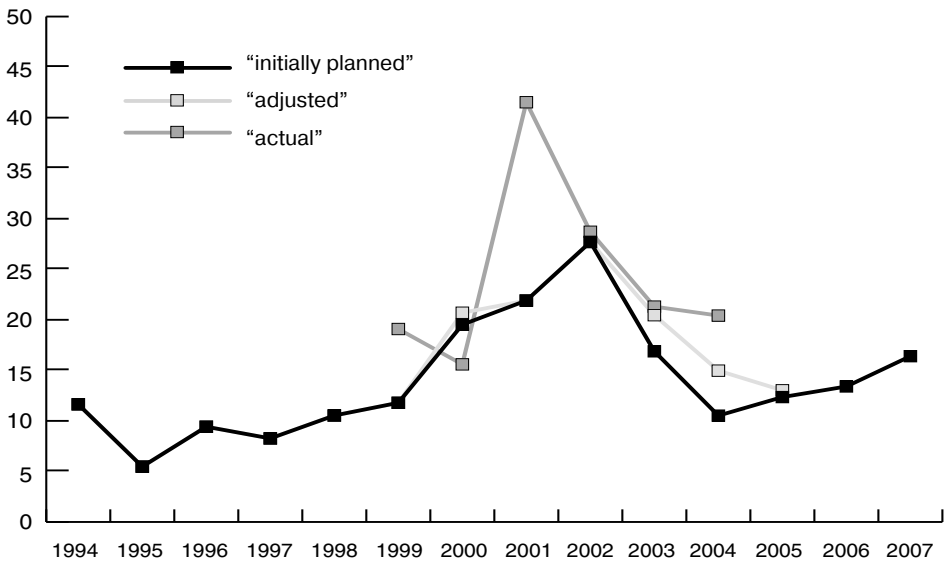
In 1995-2001, the sub-category “International Cooperation” obviously was not fully presented in the Foreign Ministry's budget – a significant amount of funds is paid through the Ministry of Finance. But even there they are not always fully reflected because of the budget structure, as well as for reasons of secrecy. Allocations for foreign policy under the “International Cooperation” sub-category must have stood then at 90 percent of the Foreign Ministry's budget (this is only an estimation, because such a ratio has been in effect since just 2002 when the budget became less classified).

Importantly, the federal budget expenditures under review do not include additional incomes that Russian institutions abroad receive from allowed kinds of activity (these incomes are for the first time fully included in the 2007 budget; however, this data is

inaccessible to the public and is contained in a classified supplement). Throughout the years under review, there have existed such incomes that increased foreign-policy budgets by an unknown value (hardly a significant one, though).

FOREIGN-POLICY EXPENDITURES IN 1994-2007

Graph 1. Russia's Federal Budget Expenditures on Foreign Policy in 1994-2007, in 2003 prices*, trillion rubles before 1997, and billion rubles since 1997



* Current prices for 2003 were converted into fixed ones by means of a GDP deflator, which was calculated by the Federal State Statistics Service (the deflator index for 2006 and 2007 is estimated at 1.09 and 1.08, respectively). Inflation rates differ in different sectors of the economy. Therefore, the GDP deflator used for a particular category of expenditures cannot produce an absolutely precise adjustment for inflation – for foreign-policy expenditures the inflation was probably higher or lower than the GDP deflator. Yet, however notional the deflator index may be, there is no alternative to it. The inflation rate calculated for each specific year may not be absolutely precise, but in any case, the figures produced are commensurable and, at least, must adequately reflect the present tendencies.

Graph 1 shows the following three curves:

1) “initially planned” – allocations approved when adopting the federal budget;

2) “adjusted” – allocations adjusted as the federal budget was being fulfilled (as of the end of the fiscal year);

3) “actual” – actual expenses specified in reports on the federal budget execution (such reports have been adopted only since 1999, and two years after the termination of a corresponding fiscal year; so at the time this article was written only data for 1999-2004 was available).

The three curves do not always coincide. This is a widespread practice: budgets are often adjusted in the course of a fiscal year. Moreover, sometimes they may exceed even the adjusted targets. The years 2000, 2003 and 2004 are particularly indicative in this respect: in those years, the originally planned, adjusted and actual budgets had absolutely different values.

The period between 1998 and 2002 saw a continuous growth in foreign-policy allocations. Interestingly, the 2000 budget provided for an essential increase in these allocations as compared with the previous year. However, the actual expenditures in 2000 were less than planned. The same tendency was observed in other spheres as well: the Defense Ministry and security services, for example, whose budgets for the 2000 fiscal year had been considerably increased (due to additional budget incomes), did not utilize all the funds allocated to them.

Allocations reached their peak in 2002, while actual expenditures (according to budget execution reports) peaked in 2001. In 2003-2004, both parameters considerably decreased. In 2004, general allocations for foreign policy returned to the 1998 level. Since 2005, foreign-policy allocations have been moderately growing.

EXPENDITURES ON FOREIGN POLICY MINUS THE CIS

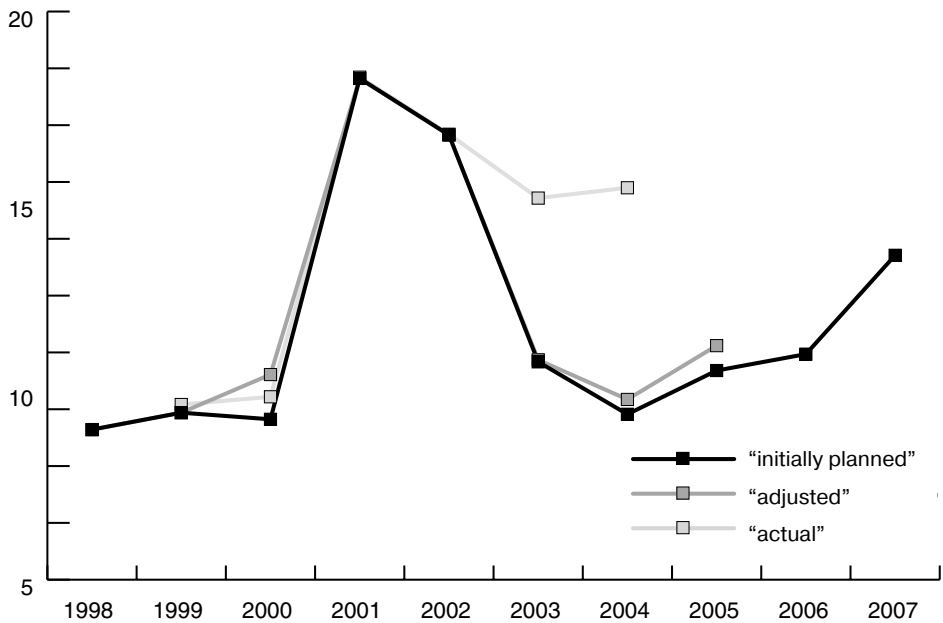
Graph 2 shows that the volatility of foreign-policy expenditures is much less if the CIS is not taken into account. The difference between a planned budget and actual expenditures was insignificant before 2003.

The budget execution curve reflects a minor decrease after the 2001 peak; foreign-policy expenditures remain much higher than

in the late 1990s. One can even say that these expenditures (provided that spending on foreign policy in the CIS is not taken into account) have stabilized at a level that is rather high for Russia.

Therefore, expenditures on CIS policy since 2000 have essentially influenced the dynamics of all foreign policy spending, and in some way actually “distorted” it.

Graph 2. Russia’s Federal Budget Spending on Foreign Policy in 1998-2007 Minus Expenditures on CIS Policy, in 2003 prices, billion rubles



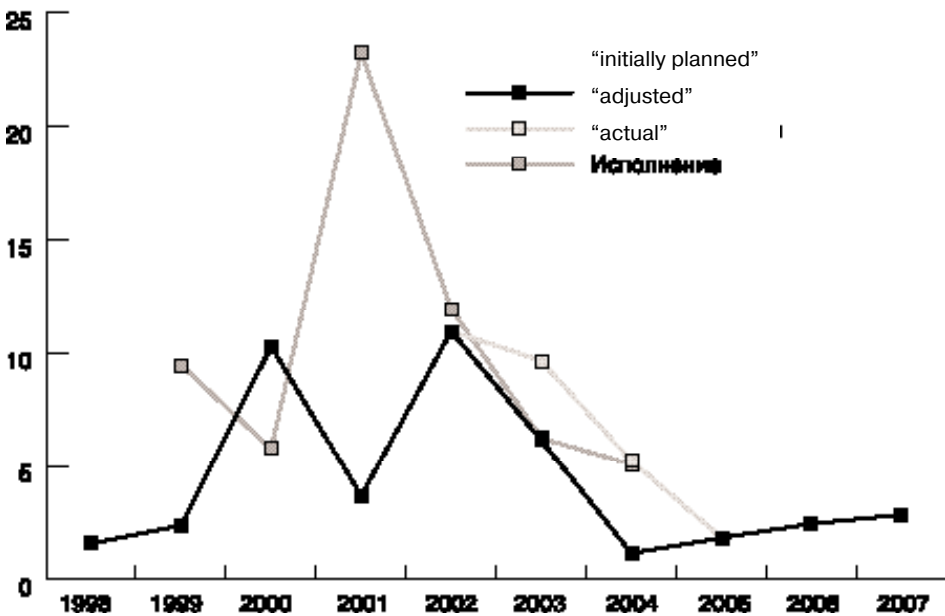
EXPENDITURES ON CIS POLICY

The aforementioned volatility of foreign policy spending is perfectly illustrated in Graph 3. Throughout the last decade, there has been a discrepancy between budget allocations on foreign policy and actual spending: in some years, the spending was more than planned, while in others it was less. Indicative in this respect is the year 2001, when foreign policy spending was planned in lesser amounts than the allocations and actual spending in 2000.

However, actual foreign policy spending in 2001 by far exceeded the figure for the previous year. The year 2001 was a peak year for investment in foreign policy in the CIS.

In subsequent years foreign policy allocations essentially decreased. And although in 2005-2007 the budget has been somewhat growing, still it remains at the level of the late 1990s. In 2004, however, actual spending was more than 300 percent higher than initially planned. Most likely, the same is for the period of 2005-2006 (figures for these years are still unavailable). Nevertheless, spending for 2004-2007 will be much less than it was for 2001 and 2002.

Graph 3. Russia's Federal Budget Spending on CIS Policy in 1998-2007, in 2003 prices, billion rubles*



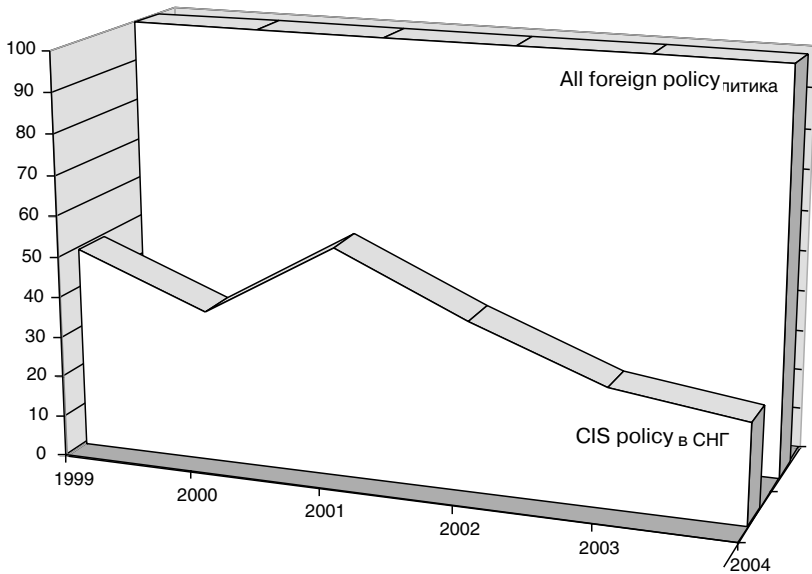
* Spending on CIS policy comprises allocations for the program entitled, Implementation of Interstate Treaties Within the CIS Frameworks. This budget item includes allocations not only for policy toward the CIS proper, but rather for policy in the CIS space, as well as spending on the Collective Security Treaty Organization, the Eurasian Economic Community (EurAsEC) and other organizations. Allocations for CIS policy were for the first time made a special federal budget item in 1998. No precise figures concerning CIS policy in the previous years can be obtained from open sources.

TOTAL/CIS SPENDING RATIO

These figures are given in Graph 4 (it contains only actual spending figures, so it refers only to the period of 1999-2004, for which there are budget execution reports). This factor simplifies the diagram; besides, actual spending figures are more important than planned allocations. We have already seen discrepancy between planned and actual allocations with regard to all foreign policy spending (Graph 1) and spending on CIS policy (Graph 3).

Graph 4 shows that since 2001, funds spent on CIS policy have been steadily decreasing. In the late 1990s, approximately half of all allocations that were set aside for foreign policy was spent on neighboring countries. In 2001, this ratio was repeated due to a sharp increase in actual financing. In subsequent years, however, spending on CIS policy steadily decreased, amounting to just 25 percent in 2004.

Graph 4. Russia's Federal Budget Spending on All Foreign Policy and CIS Policy in 1999-2004, %



After 2004, judging by allocations in the federal budget, the share of funds for CIS policy within the entire category of foreign pol-

icy spending decreased even further to 17-20 percent. In 2005 and 2006, however, spending on CIS policy grew faster than all foreign policy spending (although the 2007 budget is marked by a reverse trend). If actual spending in 2005-2007 does not radically differ from the budget plans, the share of CIS policy spending will stabilize at about 20 percent.

SOME CONCLUSIONS

The abovementioned figures suggest the following conclusions:

- the period 2000-2003 saw unusually high spending rates on all foreign policy projects (it grew particularly high in 2001 but then decreased, although remaining at a high level in the next two years);
- the foreign-policy budget (not including spending on CIS policy) decreased after 2001; yet it stabilized at levels considerably higher than in the late 1990s;
- allocations for CIS policy after 2000 fluctuated violently and eventually fell to the level of the late 1990s. Correspondingly, after 2001 their share in total foreign policy spending steadily decreased to half the figure of the late 1990s.

If we convert these quantitative (budget) parameters into qualitative (political) ones, we can assume that after Russian President Vladimir Putin came to power, he took an active foreign-policy position, backing it with an increased foreign-policy budget. After a sharp growth and subsequent decline, this budget (not including CIS policy) has stabilized at a level that is high for Russia.

The uncertainty and inconsistency of foreign policy in the post-Soviet space brought about considerable fluctuations in spending. In correspondence with statements about the high priority that CIS policy plays for Russia, financing in this field increased considerably in individual years. Of special interest is the year 2001 when actual spending increased to particularly high rates.

Today, statements concerning the high priority of foreign policy in the CIS are still made, but they are not consistent with the continuing decrease in spending on this policy within foreign-policy allocations.

Let's once again return to a factor on which we focused our attention above: it often happens that initially planned, adjusted and actual budget allocations differ essentially. In my view, this is a telltale sign (even though indirect) of the insignificant role that parliament plays in the implementation of foreign policy. The executive branch makes decisions and implements them at its own discretion, without letting parliament in on its plans – even when the federal budget is to be endorsed. Actually, the executive branch spends as much funds as it sees fit.

At the same time, the volatility of foreign policy spending reveals the main problem: political decisions in Russia are poorly translated into budgetary categories and specific plans with a particular price tag. As a result, the executive branch often fails to stay within specific budgetary limits.

The inability to estimate and plan the financial parameters of a particular policy is an adverse factor that may have negative consequences. There is a danger to assume superfluous political and, therefore, financial obligations, or, on the contrary, to be too cautious and leave part of the resources unused unwittingly and without any grounds. In the first case, risks increase; in the second, efficiency decreases. A country seeking to return to the global stage as a major actor must find a well-planned solution to the problem of providing its foreign policy with sufficient resources.

Historical Struggle for the Black Sea Fleet

Yuri Dubinin

Following the breakup of the Soviet Union, Russia and Ukraine were confronted with the pressing problem of what to do with the Black Sea Fleet; the issue took eight long years to resolve. Finally, it seemed that the crisis was confined to the pages of history. However, some forces in Kiev, under various pretexts, are again calling into question the agreement that settled the conflict between the two states.

Given this latest turn of events, it would be helpful to recollect exactly how the unprecedented diplomatic marathon, which was full of dramatic twists and turns, helped to untie one of the most complicated knots that Russia and Ukraine inherited from the Soviet period.

BOLD MOVE BY KIEV

On April 5, 1992, Ukrainian President Leonid Kravchuk signed a decree entitled, *On Urgent Measures to Build the Armed Forces of Ukraine*. The decree placed the Black Sea Fleet of the former Soviet Union under Kiev's jurisdiction and ordered that a Ukrainian Navy be immediately built on the basis of the fleet's forces deployed on the Ukrainian territory (this actually meant the entire Black Sea Fleet). However, Kiev had no grounds to make such a move. Moreover, at that time, the Black Sea Fleet was part

Yuri Dubinin is a Professor of the Moscow State Institute of International Relations, Honored Worker of the Diplomatic Service of Russia. In 1994–1999, he was Deputy Foreign Minister of the Russian Federation.

of the United Armed Forces of the Commonwealth of Independent States (CIS) and part of the CIS Navy, commanded by Admiral Vladimir Chernavin.

Moscow's reaction was immediate: on April 7, the president of the Russian Federation, Boris Yeltsin, issued a decree that placed the Black Sea Fleet under Russia's jurisdiction. To resolve the crisis, the Kremlin proposed holding negotiations and suspending the two conflicting decrees for the period of the negotiations.

FIRST CONTACT

On April 16, first deputy commander-in-chief of the CIS Navy, Felix Gromov, and I traveled to Kiev to make preparations for the negotiations. Yeltsin's instructions were very short and concise: "The final agreement with Ukraine must include, on an interrelated basis, principles and specific parameters for the handover of part of the Black Sea Fleet to Ukraine, as well as accords on terms for the basing of, and support for, the Black Sea Fleet of the United Armed Forces of the Commonwealth of Independent States." In short, the solution of the Black Sea Fleet problem was to include the solution of the problem of its basing.

My Ukrainian counterpart was Anton Buteiko, adviser to the president of Ukraine and head of the presidential International Affairs Service. The essence of his demand was very simple: the Black Sea Fleet must be Ukrainian. This demand, however, was not backed by any serious arguments. In response, we proposed relying on several earlier concluded CIS agreements, in particular the Minsk and Alma-Ata accords, which had a direct bearing on the Black Sea Fleet. I attached particular importance to the protocol of a working meeting of the CIS heads of state on naval symbols, which was signed in Moscow at the summit level on January 16, 1992. The protocol stated that the Navy of the former Soviet Union was part of the CIS Strategic Armed Forces; also it included a specification that was very important for the solution of the fleet problem. It stated, in part: "... except for the part of the Black Sea Fleet which will join the Armed Forces of Ukraine." Ukrainian President Leonid Kravchuk wrote down this

phrase in the document with his own hand. Then followed a provision stating that the handover of part of the Black Sea Fleet to Ukraine must be resolved on the basis of an agreement between Russia and Ukraine. So the discrepancy between the claim to the whole of the Black Sea Fleet, and what the Ukrainian president had written in the protocol, was striking.

We continued to raise the issue of the basing of the Black Sea Fleet, but the Ukrainian officials avoided discussing it. The issue remained unresolved even after I referred to the Agreement on the Establishment of the Commonwealth of Independent States of December 8, 1991, which was signed by the president of Ukraine. The agreement said: “The member states of the Commonwealth... shall jointly guarantee necessary conditions for the deployment, functioning, and material and social support of the Strategic Armed Forces.” This had a direct bearing on the Black Sea Fleet. However, references to the CIS documents only drew a negative reaction from our partners.

Finally it was agreed to hold negotiations on the Black Sea Fleet and set the starting date of the talks. The first meetings showed, however, that Moscow and Kiev approached the negotiations from directly opposite positions.

In the meantime, the situation in the Black Sea Fleet became increasingly aggravated due to the unilateral actions of Kiev, which exerted pressure on the fleet personnel in a bid to cause the sailors to take the Ukrainian military oath and thus de facto “Ukrainianize” the fleet. The fleet, commanded at the time by Admiral Igor Kasatonov, did not yield to the pressure; nevertheless, the political problem remained very acute.

On April 29-30, state delegations from Russia and Ukraine met in Odessa for their first official meeting on the Black Sea Fleet. The delegations were headed by vice chairmen of the two countries’ Supreme Soviets (parliaments) – Yuri Yarov of Russia and Vassily Durdinets of Ukraine. The parties agreed only on the introduction of a moratorium on unilateral actions with regard to the Black Sea Fleet, which Ukraine did not observe. The meeting failed to introduce any prospects for solv-

ing the issue, while the Ukrainian side displayed no interest in a settlement on mutually acceptable terms.

THE CONCEPT OF A POLITICAL TREATY

The aggravation of the entire range of Russian-Ukrainian relations necessitated their discussion at summit level. On Russia's initiative, the leaders of the two countries met in Dagomys, a suburb of the Russian city of Sochi, in June 1992. I was instructed to prepare proposals on the political concept of the negotiations.

I proceeded from the following premise. The liquidation of the Soviet Union brought about many moot points and even conflicts between Russia and Ukraine. Progress in resolving them was slow or failed to make any headway at all. This created the impression that relations between the two countries were troubled and had no future. I was confident that such a dire situation did not meet the vital interests either of Russia, or Ukraine.

The Black Sea Fleet problem was particularly acute. The obvious differences in the countries' approaches to its solution were augmented, while extreme nationalist forces in Ukraine aggravated and even stirred up problems. These forces would have gladly reduced relations between the two countries to those difficulties, thereby making them hostages to the conflict over the Black Sea Fleet. Of course, such a scenario would have had serious international consequences.

Kiev was reluctant to solve the fleet problem on a mutually acceptable basis, apparently in the belief that time was on its side. At the same time, Moscow, despite its legally correct position during the Black Sea Fleet negotiations, and its readiness for a balanced decision, did not have a negotiating resource that could interest Kiev.

Moscow needed to unite all of the main problems into one package, formulate the concept of its relations with Ukraine, determine a vector for their development, and enter the Black Sea Fleet problem into this context. I turned to Russia's diplomatic experience of the past when this country invigorated relations with major states. Those efforts were based on the interplay of the following key elements: the broadening of contacts at all levels, together with regular summit meetings; the extension of the con-

tractual basis of bilateral relations and the creation of necessary negotiating mechanisms to this end; combination of efforts in various fields of interstate relations; etc.

The conclusion of a general political treaty was set as the main goal of the initial stage for building Russian-Ukrainian relations. This goal, quite natural for building relations with any other state, in this case acquired special meaning. This was because historically Ukraine did not have formal borders, and the need to formalize them was obvious and pressing. This factor inspired hope for Kiev's special interest in concluding a political treaty with Russia as an important step in fixing Ukraine's territorial status internationally.

Naturally, Russia was interested in normalizing relations with its largest neighbor in Europe, as well as determining the nature of those relations. More importantly was that the preparation of a general political treaty could be combined with negotiations on the Black Sea Fleet. Then Russia would possess the diplomatic resource to find a solution to the Black Sea Fleet problem. I believed this to be the only hope for a mutually acceptable settlement, and the Russian leadership eventually approved these considerations.

On June 23, the presidents of Russia and Ukraine, together with parliament chairmen, heads of government, and ministers, met in Dagomys. The main results of the negotiations were fixed in an agreement on the further development of Russian-Ukrainian relations.

President Yeltsin proposed to the Ukrainian party a plan to work out a full-scale political treaty that would reflect the new quality of relations between Russia and Ukraine. The Ukrainian guests accepted the proposal. The very first provision of the agreement signed in Dagomys was to immediately begin preparations for such a document.

The agreement contained the following phrase: "In view of the creation of their own Armed Forces, the Parties have reiterated the importance for continuing the negotiations on the creation... of the Navy of Russia and the Navy of Ukraine on the basis of the Black Sea Fleet." And further on: "They [Russia and Ukraine – Yu.D.] have agreed to use the existing system of the basing and material and technical support on a contractual basis." After

Dagomys, this accord became fundamental in other negotiations on the Black Sea Fleet.

However, even after the Dagomys summit, it proved impossible to speed up the solution of the Black Sea Fleet problem. So, the presidents of Russia and Ukraine, at their meeting in Yalta on August 3, 1992, agreed to postpone the settlement until the end of 1995. Meanwhile, the Black Sea Fleet was withdrawn from the structure of the CIS United Armed Forces and subordinated directly to the heads of both states. A year later, on June 17, 1993, at a meeting in Zavidovo, near Moscow, the two presidents agreed to accelerate the division of the naval fleet on a fifty-fifty basis. Yet the agreement signed in Zavidovo was never ratified.

In September 1993, yet another Russian-Ukrainian summit took place in Massandra, in the Crimea. There, the presidents signed a protocol on the settlement of the Black Sea Fleet issue, which stated that “the state delegations of the Russian Federation and Ukraine shall within a month work over all the issues pertaining to the drafting of the Agreement, according to which the whole of the Black Sea Fleet with all its infrastructure in the Crimea will be used by Russia and will bear Russia’s symbols on the understanding that the Russian party will make corresponding payment for the half of the Black Sea Fleet, including infrastructure, which was to become Ukrainian under the previous accords.”

I was appointed to head the state delegation of the Russian Federation at the negotiations on the Black Sea Fleet problem. Boris Tarasyuk headed the Ukrainian delegation.

The difficult negotiating process was complicated still further by a hostile act on the part of Ukraine. On April 8, 1994, the Ukrainian military made a bold attempt in the port of Odessa to detain the Cheleken hydrographic vessel, which was conducting routine assignment to service navigational equipment. On the night from April 10 to April 11, about 120 Ukrainian troops seized the 318th battalion of the Black Sea Fleet reserve ships, together with a coastal base, a communication center, property and armaments. The coastal base personnel were taken to the village of Chebanka, 10 kilometers from Odessa. The move sparked a crisis situation. I was sent on urgent

orders to Kiev to discuss the situation with the president of Ukraine, and we were able to reach a verbal understanding concerning the basing of Russia's Black Sea Fleet in Sevastopol.

A M B A G E S

On April 15, 1994, the presidents of Russia and Ukraine met in Moscow and signed an agreement on a stage-by-stage settlement of the Black Sea Fleet imbroglio. The agreement provided, in particular, that Ukraine would have 15 to 20 percent of the fleet's ships and that the Russian and Ukrainian fleets would be based separately.

The defense ministers of Russia and Ukraine, Pavel Grachev and Vitaly Radetsky, met in Sevastopol on April 21 to discuss mechanisms for fulfilling the agreement. There, the ministers were able to reach a mutual consensus with regard to the division of Black Sea Fleet ships between Russia and Ukraine. However, Radetsky, breaching the verbal understanding that had been previously reached with then President of Ukraine Leonid Kravchuk, disrupted the question over basing rights of Russia's Black Sea Fleet.

By July 1994, when the presidency in Ukraine passed to Leonid Kuchma, a solution to the fleet problem had still not been found. It became increasingly obvious that this lingering question needed to be linked to the conclusion of a political treaty between Russia and Ukraine. However, Ukraine sought to avoid such a bilateral declaration and conclude a political treaty, while leaving the Black Sea Fleet problem hanging in midair. Kiev made every effort to have Yeltsin pay an official visit to Ukraine, but Moscow insisted that such a visit should take place only after the preparation of a political treaty was completed and the Black Sea Fleet problem was solved.

On August 11, 1994, preparations began on the draft of a general political treaty between Russia and Ukraine. I headed the Russian delegation, and Alexander Chaly was the head of the Ukrainian delegation. By the end of autumn, the delegations had three meetings and there was general agreement on the text of the document, which was entitled, *Treaty of Friendship, Cooperation and Partnership Between the Russian Federation and Ukraine*. On Russia's initiative, the draft treaty was supplemented with a provision that both coun-

tries, as friendly powers, would base their mutual relations on strategic partnership and cooperation. Both sides pledged to refrain from any actions that were harmful to the interests of the other side, nor to use their territories in such a way that could be detrimental to each other's security. The document emphasized the need for a common economic space between the two countries. On the whole, the draft treaty laid the legal groundwork for developing friendly relations between Russia and Ukraine, provided both nations showed respect for each other's territorial integrity and reiterated the inviolability of the borders that existed between them.

The work on the draft treaty proceeded very rapidly; yet, it was far from complete when Leonid Kuchma essentially raised the status of the Ukrainian delegation: Chaly, as the head of the delegation, was replaced by Vice Premier Yevgeny Marchuk, one of the most influential and rising Ukrainian statesmen at the time, who would later become prime minister. I, in turn, was appointed deputy foreign minister.

When Marchuk arrived in Moscow for the negotiations, he conveyed to me President Kuchma's wish that the draft treaty be initialed. Obviously, Kiev wanted the initialing procedure to be followed by Yeltsin's official visit to Ukraine and the signing of the treaty. I replied that we could not do that until work on the draft treaty was complete and the Black Sea Fleet problem was solved. Kiev was not happy with that response.

On January 24, 1995, Kuchma arrived in Moscow and asked Yeltsin to appoint Oleg Soskovets, Russia's first deputy prime minister who was quickly gaining prestige in federal and political life, as the head of the Russian negotiating delegation. Soskovets was immediately summoned to the Kremlin where he was given corresponding instructions in Kuchma's presence. Simultaneously, it was decided that I would be his deputy at the negotiations.

The newly composed delegations met in Kiev where the negotiations began with opening statements by Marchuk and Soskovets. The latter concluded his speech on a bit of a strange note: "Diplomats are accustomed to conduct negotiations for the sake of negotiations; the very process is the most important thing

to them. We have arrived to achieve solutions,” he said with emphasis, half turning to me and smiling. Later, our delegation had a meeting with President Kuchma; negotiations were held on the text of the treaty, which we failed to fully agree on; and, finally, a conversation on the Black Sea Fleet took place, which showed the total unwillingness of the Ukrainian party to move forward. Then Marchuk and Soskovets met tête-à-tête, after which Soskovets summoned the delegation and declared that he was prepared to immediately initial the political treaty.

That news came as a bolt from the blue. Russia’s strategic line at the negotiations with Ukraine could be ruined since the linkage of the two issues – the political treaty and the Black Sea Fleet – would be disrupted, and the future of the Black Sea Fleet and chances for its basing in Sevastopol would remain obscure. That was unacceptable to Moscow.

“If we initial the treaty now,” I exclaimed, “the Ukrainians will not care a damn about the negotiations on the Black Sea Fleet!”

That was a genuine cry from the heart. But it was all in vain. An hour later, the initialing ceremony took place – and with much pomp.

The Ukrainian delegation was in a state of euphoria: the treaty had been initialed, the Black Sea Fleet question remained hanging in midair, while Russia now depended on Kiev’s will. The Ukrainians believed the way to President Yeltsin’s visit to Kiev was now open. Kuchma hurried to declare that the visit would take place in early March 1995.

Meanwhile, the media both in Russia and Ukraine flew into a rage. Russia’s *Segodnya* newspaper of February 18 carried an article under the bitter headline: “Sailors Believe They Were Sold for a Song.” The description of the events, provided by the article, was very close to the original: “On the eve of the latest round of negotiations on the Black Sea Fleet, recently held in Kiev, the composition of the Russian delegation was essentially changed. The group of diplomats, who had for several years been working under the direction of ambassador at large Yuri Dubinin, received a new head – Deputy Prime Minister Oleg Soskovets, whose

scope had never included naval affairs. Rumor has it that it was the head of the Ukrainian delegation, Vice Premier and influential policymaker Yevgeny Marchuk, who insisted on this replacement in Moscow. Marchuk wanted to negotiate with his peer. The subsequent events showed that Mr. Marchuk made the right choice: he received from the hands of Mr. Soskovets what he had been unable to get from Moscow for three years. ‘Unlike Dubinin, Soskovets is a man one can do business with,’ Mr. Marchuk said in a brief comment on his achievement. ‘This is a victory of Ukrainian diplomacy!’ Ukrainian Foreign Minister Mr. Gennady Udovenko said with pleasure.”

In an open letter to President Yeltsin, the officers of the Black Sea Fleet expressed their discontent. The commander of the Black Sea Fleet, Admiral Eduard Baltin, issued a harshly critical statement. Meanwhile, Russia’s Foreign Ministry was in a state of bewilderment: How could the treaty be initialed without its corresponding approval?

On February 24, the Embassy of Ukraine in Moscow conveyed to Russia’s Foreign Ministry a letter from Leonid Kuchma to the Russian president. The letter, full of flagrant contradictions, made no mention of the Black Sea Fleet – despite the numerous negotiations! At the same time, it said: “Let me express once again my satisfaction with the results of the Kiev round of negotiations between the state delegations of Ukraine and Russia, whose major result was the initialing of the text of a major Treaty of Friendship, Cooperation and Partnership. In this connection, I have the pleasure to invite you, Mr. President, to pay a state visit to our country at any time that is convenient for you.” Further on, Kuchma expressed his wish that the visit take place before March 12, that is, as soon as possible.

On February 28, Yeltsin sent a brief yet succinct reply: “Thank you for your letter of February 17, 1995, and for the reiterated invitation to pay an official visit to Ukraine, to which I assign exceptional importance... In our view, the draft of the political treaty should be further worked on in strict compliance with the Memorandum on Guarantees of the Security of Ukraine, which

we together signed in Budapest late last year. The Declaration on the Black Sea Fleet problem, which we are going to sign, must ensure, immediately after the visit, implementation of all measures to be taken during the first stage of this problem's settlement without any additional negotiations. It is also important to prepare by the time of my visit an agreement on the rescheduling of Ukraine's state debt on loans provided by Russia. I am confident that there will be no difficulties in setting a specific date for the visit." Of course, Kiev had expected a different answer.

On April 18, President Yeltsin received Marchuk, who by that time had become Ukraine's prime minister, in Moscow. As Yeltsin aide Dmitry Ryurikov said in an interview with the ITAR-TASS news agency, the conversation proceeded in an atmosphere of "utter frankness." In the language of diplomacy this means that the conversation was far from smooth.

According to Ryurikov, Yeltsin was straightforward about the Ukrainian side's approaches to the Black Sea Fleet issue: "Because of your position, we now agree, now disagree; now make a decision, now go back on it. Friends and neighbors do not behave like that; one must respect one's partner." Yeltsin described the situation when Kiev, having signed an agreement on the rescheduling of Ukraine's debts, refused to take a constructive approach to Russia's proposals concerning the Black Sea Fleet, as "an attempt to outwit Russia." Yeltsin remained unsatisfied with the proposals on the Black Sea Fleet, which Marchuk brought to Moscow, and said, "Russia's position, fixed in the previous accords on the Black Sea Fleet, is fair, objective and moral. Russia will not depart from those accords. There have been concluded enough agreements on the fleet; there have been numerous meetings of experts; yet no progress has been made." Yeltsin suggested that the Ukrainian side draw its conclusions.

Marchuk was taught an object lesson: sophisticated ruses and empty promises are not the best way to conduct serious negotiations. Such methods can only complicate relations between states, not to mention with one's negotiating partner, whose confidence has been undermined.

On May 22, Kuchma sent a letter to Yeltsin, which was fully devoted to the Black Sea Fleet problem; a draft agreement was enclosed with it. As the documents came from the president of Ukraine himself, the Russian leader ordered that they be scrupulously analyzed. Upon analysis, all interested ministries and government agencies drew a unanimous conclusion: the proposals not only failed to settle the problem, but they also negated many of the previous accords. Yeltsin decided to respond to the Ukrainian president's proposals during their private meeting on May 26 in Minsk where both leaders were scheduled to meet for a CIS summit. At this point, tensions over the Black Sea Fleet problem had come to a head.

TURNING POINT

In Minsk, Yeltsin and Kuchma agreed to hold a special meeting on June 9 in Sochi and devote it largely to the Black Sea Fleet issue. On June 6, the Ukrainians handed over to us their draft of a final document – a joint statement, whose subtitle specified that it was only a communiqué. Kiev sought to attach a less binding agreement to the results of the Sochi meeting, compared with the earlier approved Russian-Ukrainian documents on the Black Sea Fleet. Actually, the draft reflected the content of Kuchma's May 22 letter to Yeltsin.

In the opinion of the Russian experts, approval of Kiev's approach would mean the termination of any legal basis for Russia's naval presence in Ukraine. The Ukrainian proposals did not even mention that the headquarters of Russia's Black Sea Fleet must be based in Sevastopol. I proposed presenting the main results of the negotiations in Sochi as an agreement between the Russian Federation and Ukraine on the Black Sea Fleet, making the document as binding as possible. Moscow agreed with this proposal.

The negotiations in Sochi began with a private conversation between the two presidents. Meanwhile, Ukrainian Foreign Minister Gennady Udovenko and I were responsible for coordinating the text of the draft agreement. The instructions given to me were brief: do not insist that Russia would use all naval facilities in Sevastopol, and that the agreement shall specify the location of the Ukrainian Navy headquarters, leaving this issue to Kiev's discretion. There was also a

strong request to prepare the text as quickly as possible. Udovenko and I worked very hard and finally the document was ready. The presidents approved it unamended and immediately signed it.

The agreement, the result of years of intensive joint research, produced a mutually acceptable balance of interests for both countries. In particular, the agreement specified that “the Black Sea Fleet of the Russian Federation and its headquarters shall be based in Sevastopol.” Further on it stated: “The Black Sea Fleet of the Russian Federation shall use facilities of the Black Sea Fleet in Sevastopol and other basing facilities and home stations of ships, aircraft and coastal defense troops, and facilities of operational, combat, technical and logistic support in the Crimea.”

Yeltsin was very pleased. At a specially convened press conference, the Russian president described the signing of the agreement as a “historic event” which opened the way to further development of relations between Russia and Ukraine on the basis of a strategic partnership, mutual respect and trust. Yeltsin said that he and Kuchma had settled all the issues concerning the Black Sea Fleet that had hampered relations between the two countries, and solved the fleet problem “once and for all.”

Kuchma, who spoke next, was more reserved in assessing the accords, saying: “We have made one more step forward” and: “We have untied the knot.” Also, he did not fail to mention problems that remained unresolved.

The presidents not only commented on the agreement, but also spoke about their plans for the future. Undoubtedly, there was still much work to be done, and Kuchma’s views seemed to be more realistic than Yeltsin’s. Yet, generally speaking, it was the president of Russia who was right after all: the Sochi Agreement solved the Black Sea Fleet problem, and on May 28, 1997, the process was completed with the signing of three more major agreements on the fleet: on the status of the Black Sea Fleet of the Russian Federation and terms for its stay on the territory of Ukraine; on parameters involving the division of the fleet; and on mutual settlements with regard to the division of the Russian fleet, together with the basing of the Black Sea Fleet of the Russian Federation in Ukraine.

Making the settlement more binding required ratification of the agreements by the legislatures of Russia and Ukraine. Passions over the future of the Black Sea Fleet were still running high in Russia, and ratification of the agreements was necessary to achieve accord throughout society. It was also necessary to avoid pitfalls posed by the parliament of Ukraine. The ratification process could continue indefinitely and, most importantly, it could fail to produce a positive result, as had already happened to the agreement signed in Zavidovo. Under such a scenario, the situation in the Black Sea Fleet would continue hanging in midair as before.

To avoid such a threat, I proposed using a provision of the Vienna Convention on the Law of Treaties, signed in 1969, according to which a treaty subject to ratification can be applied provisionally upon signing if the negotiating states have so agreed. It was implied that the ratification process would take place at a later date. The proposal was accepted.

Our draft agreements were handed over personally to Kuchma, whereupon the experts began to ponder over them. However, Kiev still wanted Yeltsin to visit Ukraine where they would conclude a general political treaty, without signing basic agreements on the Black Sea Fleet. There were several such attempts, and one of them had good chances for success.

It happened in 1997. At that time, I was Russia's ambassador to Ukraine in the rank of deputy foreign minister. Kuchma met with Yeltsin in Moscow, and upon his return home announced sensational news: the presidents had agreed that Boris Yeltsin would come to Kiev to sign a general political treaty, while the work on the Black Sea Fleet problem would continue. The Russian president had proclaimed a similar statement.

Udoenko and other Ukrainian officials triumphed: the connection between Yeltsin's visit and the signing of agreements on the Black Sea Fleet was finally broken.

Since I was staying in Kiev, I did not know what exactly was happening in the Russian capital. Soon I was summoned to Moscow where Prime Minister Victor Chernomyrdin convened a special meeting to discuss the situation. We met in the Russian

White House where there were assembled the top executives of all interested ministries and government agencies of Russia. The Foreign Ministry officials present at the meeting included First Deputy Minister Boris Pastukhov and myself.

Chernomyrdin announced that he had invited us together in order to discuss our thoughts about a presidential visit to Kiev for the signing of a major treaty with Ukraine at a time when agreements on the Black Sea Fleet were still not ready.

The assembled officials were unanimous in the conviction that before the president pays a visit to Kiev, the two countries must complete an agreement on the Black Sea Fleet and sign it simultaneously with the major treaty – or even earlier. Russia's top leadership agreed with this position.

Chernomyrdin's deputy, Valery Serov, a prominent politician who in Soviet times headed the State Construction Committee, was the head of Russia's delegation at the final stage of the negotiations on the Black Sea Fleet. It was Serov who conveyed our position to Leonid Kuchma.

Later, Serov said his conversation with Kuchma was not smooth, as the Ukrainian president continued to make references to previous statements on the issue. However, Serov explained how things stood at the moment and emphasized the need to expedite negotiations on still unresolved problems. And so this was done. The new commander of the Black Sea Fleet, Admiral Victor Kravchenko, played a major role at that stage.

Finally, on May 28, 1997, Victor Chernomyrdin arrived in Kiev. He and the prime minister of Ukraine signed the three basic agreements on the Black Sea Fleet, which immediately went into effect. Thus, the prerequisites for a state visit by President Yeltsin to Ukraine were achieved. During that visit, on May 31, the heads of both states signed the Treaty of Friendship, Cooperation and Partnership between the Russian Federation and Ukraine.

THE LAST ROUND

Thus, the basic agreements on the Black Sea Fleet came into effect. Did this mean that the problem was finally solved? Not at

all, since the agreements were applied on a provisional basis. At the same time, however, many high-ranking officials in Moscow believed that status to be quite sufficient. But to hold such an opinion proved to be a big mistake: before documents are ratified and instruments of ratification are exchanged, agreements are not considered to be in effect – with all of the ensuing consequences.

The political forces in Ukraine that had failed to thwart the accords understood the situation very well. Now they decided to wage a new, no less important battle – this time against the ratification of the Black Sea Fleet agreements. Their plan was the same as before: to ratify the major treaty separately from the ratification of the accords on the Black Sea Fleet.

There was also a group of deputies in Ukraine's Verkhovna Rada (parliament) who were opposed to ratification of the major treaty. They did not understand the importance of good relations with Russia, or even the state interests of their own country. But that group was small and did not have much influence.

The Verkhovna Rada ratified the treaty by an overwhelming majority of votes. Meanwhile, the accords on the Black Sea Fleet were rather forgotten, although they had been signed even earlier than the treaty. When we asked Kiev why it did not ratify the accords, we were told that the accords needed to be studied by commissions, that Kiev wanted to ratify the accords at the “right” time so as not to agitate public opinion, and so on and so forth.

In the meantime, the process of ratifying the major treaty began in Russia, too. These deliberations triggered heated debates – perhaps, even more heated than in Ukraine. Representatives of the executive made great efforts to win the deputies' support, above all, in the State Duma (the lower house). Then suddenly the government submitted for ratification only the major treaty. Just like in Kiev.

“What about the Black Sea Fleet accords?” many deputies asked.

“Why, the Black Sea Fleet has already been settled; there are no problems there,” high-ranking representatives of the executive answered.

What exactly was behind those answers? Negligence, ignorance, or perhaps delusions – it was not clear. Yet, on December 25, 1998,

the State Duma voted for the Law *On the Ratification of the Treaty of Friendship, Cooperation and Partnership Between the Russian Federation and Ukraine* without linking it with Ukraine's ratification of the Black Sea Fleet accords. A paradoxical situation!

Anti-Russian forces in Ukraine applauded such a turn of events. Now they were absolutely sure that they would be able to avoid ratifying the accords on the Black Sea Fleet, which would thus never enter into force. Boris Kozhin, the first Commander-in-Chief of the Ukrainian Navy and now a deputy, told me this triumphantly when he met me in the Verkhovna Rada.

Such a state of affairs alarmed me. I took note of a public statement by President Kuchma that stated, in effect, that Russia could find a way to link its ratification of the major treaty to ratification by Ukraine of the agreements on the Black Sea Fleet. I immediately sent a telegram to Moscow in the hope that it would think of a way to do exactly that.

The next stage in the ratification of the major treaty was its consideration by the Federal Council (the upper house). The treaty provoked even more questions in the upper house than it did in the State Duma. Senators also heatedly debated the Black Sea Fleet issue, and Moscow Mayor Yuri Luzhkov played an active role in the discussions.

Staying in Kiev, I did not rule out the possibility that, considering the critical situation that had taken shape in Moscow, a proposal by the executive branch to ratify the major treaty could be rejected. Obviously, the consequences of such a turn of events would be extremely negative for the general state of Russian-Ukrainian relations.

In the heat of the debates in the Federation Council, Russian Prime Minister Yevgeny Primakov took the floor. He said that the Treaty of Friendship, Cooperation and Partnership should be ratified; yet, the completion of the ratification process must be conditioned on ratification by Ukraine of the agreements on the Black Sea Fleet.

Primakov proposed the following. The Law *On the Ratification of the Treaty of Friendship, Cooperation and Partnership Between the Russian Federation and Ukraine* must be

approved and submitted to the president for signature. At the same time, the Federation Council's resolution must include the following provision: "The instruments of ratification of the Treaty of Friendship, Cooperation and Partnership Between the Russian Federation and Ukraine shall be exchanged after ratification by Ukraine of the agreements between the Russian Federation and Ukraine on the status of the Black Sea Fleet of the Russian Federation and terms for its stay on the territory of Ukraine; on parameters of the division of the Black Sea Fleet; and on mutual settlements with regard to the division of the Black Sea Fleet and the stay of the Black Sea Fleet of the Russian Federation in Ukraine, signed on May 28, 1997."

An exquisite move, and it changed the mood of the senators. The Federation Council accepted Primakov's proposal. On February 17, 1999, the Council approved the law on ratification and submitted it to the president for signature. On March 2, the head of state put his signature on the law and thus completed the ratification of the treaty. Simultaneously, he told the Foreign Ministry to prepare an instrument of ratification of the treaty "after the Ukrainian party ratifies the Russian-Ukrainian agreements on the Black Sea Fleet."

Thus, Russia showed maximum good will, displaying its aspiration for friendship and cooperation with Ukraine. Now the ball was in Kiev's court.

In my comments from Kiev on what had happened, I wrote with great satisfaction that an international problem had moved from the plane of intra-Russian debates into a natural plane of interstate dialog.

Aside from the outcries of spiteful critics, the reaction of the Verkhovna Rada proved to be realistic and reasonable. The Ukrainian deputies, in a businesslike manner, at once set to work and soon completed the process of ratifying the agreements on the Black Sea Fleet. The agreements will remain in effect until 2017 and can be automatically extended. On April 1, 1999, the presidents of Russia and Ukraine met in Moscow to exchange instruments of ratification of the Treaty of Friendship, Cooperation and

Partnership, and on that very day the treaty entered into force. The ceremony concluded years of strenuous efforts made by both countries. Sergei Usov, an outstanding researcher of the Black Sea Fleet issues, wrote: “The solution of the Black Sea Fleet problem became possible only simultaneously with the settlement of interstate relations between the Russian Federation and Ukraine through the conclusion of the Treaty of Friendship, Cooperation and Partnership in a ‘package’ with the basic agreements on the Black Sea Fleet.”

The coming into effect of the Treaty of Friendship and the agreements on the Black Sea Fleet marked the end of the first, very important period in building relations between Russia and Ukraine as sovereign, independent states. These accords, together with Ukraine’s accession to the Nonproliferation Treaty, helped to prevent crisis situations breaking out into open clashes between the two largest countries in the post-Soviet space. The possible consequences of such clashes would have been difficult to predict not only for the two states but also for the entire geopolitical region.

But the main result was that the accords helped to build a legal basis for the future of Russian-Ukrainian relations – a platform on which these relations could develop for the benefit of the two nations. It also marked a new chapter for peace, stability and cooperation in Europe. Thus, a new stage of bilateral interaction began between Russia and Ukraine.

This historic landmark was not easy to achieve. The success of the difficult negotiations, which was full of emotional outbursts, unexpected turns and slumps, was due to the fact that the leaders of Russia and Ukraine, together with their negotiating teams, paid heed to the respective will of their people who demanded friendship and cooperation.

Russia Must Regain the Initiative in Moldova

Zurab Todua

When the Communist Party of the Republic of Moldova (CPRM) scored a sensational victory during parliamentary elections in 2001, winning 71 out of the 101 seats, there were no signs of a possible crisis in Russian-Moldovan relations.

Indeed, relations between Moscow and Chisinau increasingly strengthened. In the period from 2001 to 2003, Russian President Vladimir Putin and his Moldovan counterpart, Vladimir Voronin, met on 24 separate occasions. The two leaders discussed economic and political problems, among them the state of trade and economic relations between their countries, prospects for Russian business in Moldova, gas prices and, of course, the problem of the Transdnestr Moldovan Republic [a breakaway region of Moldova that declared its independence from Moldova on September 2, 1990 – Ed.]. Both Moscow and Chisinau delivered optimistic forecasts for the future.

COMMUNISM, MOLDOVAN-STYLE

Many politicians in Moldova and beyond, however, were not so sanguine about the rapid rapprochement between Russia and Moldova. The West took a very cautious stand with regard to Voronin and the Moldovan Communist Party, while all programs for providing financial support to Moldova via international organizations were suspended for an indefinite time.

Zurab Todua is a research fellow of the Institute of Religion and Politics (Moscow).

In February-March 2002, the Moldovan opposition launched a massive offensive against the ruling Communist Party: rallies were staged on consecutive occasions, and the opposition camped out in tents on Chisinau's central square. One might say that the protests were a first rehearsal of a "colored revolution" in the former Soviet Union. On several occasions, the crowd, manipulated by the opposition leaders, became so rowdy that it managed to break through riot police cordons and enter the parliament building. The protesters, however, realizing that if they were the first to initiate "military actions" the authorities would have all legal grounds to reciprocate, called off their actions at the last moment.

Meanwhile, the president and his team gave a strict order to the Interior Ministry not to use force under any circumstances, so fortunately there were no broken noses, not to mention more serious injuries. The police that manned the cordons were unarmed and did not even carry batons. When the crowd went into frenzy, the officers simply stepped aside and allowed the crowd the freedom of action.

By March, the protests began to subside. Then, early one morning, the oppositional tent camp was awoken by the boisterous voice of a man who was walking between the tents. He kept repeating: "Hey, wake up, it's time for work. Now say it all together: 'Down with the Communists!' 'Down with Voronin!'" The sleepy protesters did not immediately realize that the man really was President Voronin, who decided to see the conditions in which the protesters lived. In the afternoon, the people in the camp were served soup delivered directly from the presidential canteen.

Thus, the Moldovan Communists not only rebuffed the oppositional attacks, but they remained in power without resorting to violence. They strengthened their authority in the country and showed to the whole world that they did not intend to go back into the past and, most importantly, that they were not going to diverge from the path of democracy. Interestingly, Moldova is the only country in the Commonwealth of Independent States to have three presidents replaced in democratic elections. Moreover, all of the major political groups have been elected to power in that

country: National Democrats, Agrarians, and Communists (Mircea Snegur, Petru Lucinschi, and Vladimir Voronin, respectively). Moldova is, perhaps, the most democratic of the CIS countries in this respect.

Despite appeals from the orthodox wing in the CPRM, the Moldovan authorities opted not to abolish private ownership and launch nationalization. They set out to establish order in the economy and put an end to the embezzlement of public funds.

By that time, the national economy was in a state of ruin. In the previous 10 years, the GDP had plummeted by 68 percent (compared with a 40-percent decrease following World War II). The much-publicized “Earth” program for reforming the agrarian sector had delivered a devastating blow at the agricultural sector: Land had been shared among peasants, but private owners had been unable to cultivate it. Meanwhile, wage, pension and allowance arrears continued to grow; in 2001, for example, people were just receiving their wages and pensions for the period 1995-1997. The population became accustomed to living without electricity, heating and gas. In just one decade, Moldova had gone from being a prosperous Soviet republic, once described as a “showcase of socialism,” into one of the most backward countries in Europe.

In 2001, the situation in Moldova began to improve. The annual GDP growth rate reached 6 to 7 percent. The basic sectors of the Moldovan agriculture – winegrowing, farming, and animal husbandry – were gradually reanimated. The financial system was stabilized. Under the Communists, for the first time since Moldova gained independence, budget revenues began to be planned without depending on foreign loans. The infrastructure began to improve: rolling blackouts became a thing of the past, while the problem of supplying the population with natural gas was solved. People began to receive their wages and pensions on time. Apart from addressing urgent social and economic problems, the authorities found the time and money to renovate old monuments – and even build new monuments – to the many soldiers killed in World War II (no other former Soviet republic, besides Russia, performs this act).

A YEAR OF UNFULFILLED HOPES

This was all well and good. However, Chisinau's main problem continued to be the Transdnestr settlement. In 2003, presidents Putin and Voronin agreed to put an end to the confrontation on the basis of compromise on both sides. Dmitry Kozak, an active member of the Russian presidential team, was instructed to draft an agreement.

The success of the agreement seemed to be very close at hand, and Chisinau expressed its readiness to make concessions. Under pressure from Moscow, Tiraspol, the capital of Transdnestr, also had to take a realistic position. Kozak shuttled continuously between Moscow, Chisinau and Tiraspol, and spent hundreds of hours in negotiations. Finally, an agreement was 90 percent ready, with only a few points open for debate.

The authorities of Bendery [the second largest city in Transdnestr – Ed.] hastily prepared everything for the signing ceremony: the administration building was given a fresh coat of paint, new furniture was purchased, and formal red carpets were laid. On November 24, a so-called “vanguard” aircraft of the Russian delegation arrived at the airport. The city waited in great expectation for the Russian president.

That evening, Voronin looked through the final variant of the memorandum and, much to his surprise, saw that the document did not contain amendments promised to him earlier. In particular, a provision regarding the Russian military base remained unchanged, while Transdnestr was awarded too much power in the planned future federation, which enabled it to secede from the federation at any moment on the slightest pretext.

Kozak tried to convince Voronin that the absence of the amendments was an insignificant issue. But the fact was that Moldova had been offered to sign a document with unacceptable terms. There followed a telephone conversation between Voronin and Putin, a cancellation of the Russian president's visit to Moldova, and Kozak's departure.

According to Moscow's reading of the matter, the failure was due to last-minute interference by the Americans and the Organization for Security and Cooperation in Europe. They did not

want to yield the palm in the settlement efforts to Russia, exerted pressure on Chisinau and forced Voronin not to sign the document.

Anyway, it was haste that played the fatal role. The memorandum fell victim to the parties' desire to expedite the solution of the difficult Transdnestr problem. Too many important issues were left to be decided later and were "sort of" agreed on and "sort of" adopted. When these "sort ofs" reached a critical mass, everything fell to pieces.

Moldova and Transdnestr missed a great opportunity to reach an accord; while for Moscow, the failure represented a serious foreign-policy setback. Had the memorandum-based settlement plan been adopted and signed, that would have been the first real example of conflict settlement with Moscow's assistance. Thus a real mechanism would have been set in place for reconciling conflicting parties. It would have set a precedent that could be applied with regard to other conflicts – Nagorno-Karabakh, South Ossetia and Abkhazia – under Russia's aegis.

A success in Transdnestr would have demonstrated that it could handle a situation that was beyond the powers of the peacemakers from the Organization for Security and Cooperation in Europe and the Council of Europe. U.S. diplomats would have found themselves on the sidelines, while the CIS would have new life breathed into it. However, the reality was just the opposite.

PEACE OR WAR?

After November 2003, Russia's policy toward Moldova radically changed. Throughout 2004, economic ties between the two countries gradually declined. In 2005, Moscow banned the import of Moldovan fruit and vegetables. The next year, the ban was extended to Moldovan wines and brandy. That represented a serious blow to the economy of Moldova, as wine exports make up an important part of the country's income.

Apart from economic sanctions, Russia started to support the Moldovan opposition. Its members began to pay frequent visits to Moscow and promised to the Kremlin their full loyalty and con-

cessions on all issues. These events attracted some Russian politicians and security officials who had close connections with the Transdnestrian regime. Actually, it attracted their attention so much that they overlooked some important points.

First, the opposition leaders – Serafim Urechean, Dumitru Braghis, Nikolae Andronik, and others – were well known in Moldova as nationalists, famous for their anti-Russian statements and actions. The news about their sudden “pro-Russian orientation” perplexed ethnic Russians and Russian-speakers in Moldova.

Second, in the 1990s many of these individuals were involved in various shady dealings, possibly of a criminal nature. So they were very vulnerable in this respect. Finally, it was clear that the opposition had very little chance for success in the struggle for power. So the money spent on their support was actually cast to the wind.

The parliamentary elections in Moldova, held in February 2005, confirmed this conclusion. Despite the impressive support from Russia, the oppositional Democratic Moldova bloc (led by Urechean, Braghis, Dumitru Diacov, Oleg Serebrian, and Veaceslav Untila) failed to offer strong competition to the Communist Party. The Communists again won the majority in parliament, which elected Voronin president for the second time.

The aggravation of Russian-Moldovan relations has not brought any benefits to either country. Moscow’s economic sanctions cost Moldova about 200 million dollars in 2006. The sanctions hit hard Moldovan wineries (ironically, they are owned largely by Russian companies), as well as Russian consumers: along with fake wine, the ban has removed from the store shelves relatively cheap high-quality wine. Finally, Russia’s prestige has sharply decreased among the Moldovan population because of its support for the nationalist opposition. The only party that has gained from all of this is the leadership of the unrecognized Transdnestr Republic.

THE TRANSDNESTRIAN KNOT

For 15 years, a political group led by Igor Smirnov has ruled Transdnestr (on December 10, Smirnov was re-elected for his fourth

term). Throughout this time, the Transdnestrian leadership has been rejecting all proposals from intermediaries, and especially from Russia, for the settlement of the conflict. Every time the negotiating process was about to produce some real result (e.g. when Russia's special envoy for the settlement was Yevgeny Primakov, or later Kozak), Tiraspol launched rash efforts to thwart any chance for a compromise. The main goal of the Transdnestrian leadership is official recognition of Transdnestr independence.

Proceeding from the Kosovo precedent (which still looks obscure), Russia's State Duma and political analysts have been actively discussing proposals to officially recognize the self-proclaimed states of Transdnestr, South Ossetia, Abkhazia and, less frequently, Nagorno-Karabakh. The official recognition of these states by Russia would obviously cause great exultation in Tiraspol, Tskhinvali, Sukhumi and Stepanakert. But what would such an acknowledgement give Russia? Has anyone calmly figured out all of the possible consequences of such a move? It seems that someone is trying to involve Russia into a dangerous, reckless scheme, which may complicate or even put an end to its economic and political revival.

The four abovementioned unrecognized states provide a good analogy to the situation in Serbia in 1914. The belligerence, pertinacity and 19th-century mentality of these four territories can unleash armed conflicts again. Clearly, Russia would be inevitably involved in those conflicts.

Moscow is dedicated to maintaining its peacemaking forces in the conflict zones; it has been waging years-long diplomatic battles. However, it is continuously accused and attacked from all sides – in spite of the fact that due to its efforts the conflicting parties are refraining from resuming military actions.

Tiraspol's unwillingness to compromise has put Russia into a difficult and no-win situation. Russia is now confronted with a unified position of Moldova, Ukraine, the United States, the OSCE and the EU. These parties are in support of a plan proposed by Ukrainian President Victor Yushchenko [an early withdrawal of the Russian peacemaking forces from the conflict zone;

demilitarization of the region; and giving Transdnestr the status of an autonomy within Moldova]. Also, they demand that the peacemaking operation's format and the structure of peacemaking forces in Transdnestr be changed, and seek to deliver democracy to Transdnestr.

Meanwhile, Russia's position in the Transdnestr settlement, which can be described as "defense on the Dniestr," has no chances for success, as political resources for preserving the status quo are limited. This is not just due to Russia pledging to withdraw its military forces from Transdnestr during a summit in Istanbul in 1999. Preservation of the status quo, sought only by Tiraspol and to some extent by Moscow, is against the plans of all the other interested parties: Moldova, Ukraine, the U.S., the EU and the OSCE. In 2007, after Romania joins the EU, Moldova will share a border with the European Union, and Bucharest will constantly raise the Transdnestr issue before its European partners. So the West will only step up its efforts to solve the Transdnestr problem, to undermine the Smirnov regime in Transdnestr, and to weaken Russia's positions in the region.

PROSPECTS FOR RUSSIA

To improve the state of affairs, Russia must thoroughly analyze the real situation in the region and revise its strategy and tactics with regard to the Transdnestrian settlement and Moldova as a whole. First, it must proceed from the fact that Voronin will remain president of Moldova until 2009. The Moldovan opposition has no chances to come to power during this period. The Moldovan Communists will stay in power even if the Russian sanctions worsen the social and economic situation in Moldova.

The anti-Moldovan measures are disadvantageous first of all to Russia. This approach will only result in the complete loss of Moscow's political influence in the region, not to mention economic losses for Russia, considering heavy investments by Russian businesses in the wine-making, brandy-making and tobacco industries of Moldova. Lastly, sanctions may spoil Russia's plans for energy expansion to the Balkans.

Russia's policy of supporting the Moldovan opposition and the Smirnov regime is advantageous, above all, to the West and Ukraine. It has enabled Russia's opponents to gain the initiative in the Transdnestrian settlement. Since 2004, they have changed the format of the negotiations, started monitoring the Ukrainian-Transdnestrian border, and insisted on inspecting defense-industry enterprises in Transdnestr. Finally, they are conducting an active PR campaign in the mass media, presenting in an unfavorable light Russia's position as "support of the Smirnov regime for the sake of meeting the selfish interests of individual groups in the Russian leadership." Against these dynamic actions, Russia's position really looks like stubborn support of the Smirnov regime, without any clear goals and prospects.

Moscow must make moves that would make it again a major factor in the Transdnestrian settlement. These moves are as follows:

- proposing a new plan for the settlement;
- proposing several variants for settling the military issues (the location and prospects of the Russian military force and the arms depot near the town of Ribnita), while using the status of the radar station in Azerbaijan's Gabala as a possible example to follow;
- joining in the monitoring of the border, the mission to assess the level of democracy in Transdnestr, and other measures taken by Western powers in the region;
- appointing a new active and energetic envoy of Russia for the settlement of the conflict, who would enjoy broad powers;
- lifting economic sanctions and restoring trade and economic relations with Moldova (by the way, Moldova has no debt to Russia for its energy supplies).

By revising its policy toward Moldova, Russia could regain a leading role in the settlement of the Transdnestrian conflict and its position as the main intermediary at the negotiating table. Also, it could possibly prepare a settlement agreement once again. In this case, the West would most likely reorient itself to the opposition, which remains absolutely without influence to pose any threat to the Moldovan authorities.

The restoration of normal and mutually advantageous relations with Moldova will help Russia preserve its political, economic and, for some time, military presence in the region. The first step toward this normalization may have already been made: after a meeting between Putin and Voronin during the CIS summit in Minsk, it was announced that Moscow would lift the ban on imports of Moldovan wine to Russia.

Both Moscow and Chisinau seem to have come to this realization. In any case, in late 2006 the first step was made toward the normalization of their bilateral relations: following a meeting between Putin and Voronin during the CIS summit in Minsk, it was announced that Moscow would lift the ban on the import of Moldovan wine to Russia.

Today, the two countries have resumed intensive dialog, and are searching for solutions to the basic problems that hinder their bilateral relations. Meanwhile, negotiations over the question of Transdnestr may soon be stepped up, as well.

Thus, there are grounds for cautious optimism and hope that this time nothing will prevent Russia and Moldova from reaching agreement and restoring mutual relations to their fullest capacities.

EDITORIAL BOARD

- Sergei Karaganov** (Chairman) Dr. Sc. (History), Chairman, Presidium of the Council on Foreign and Defense Policy; Deputy Director, Institute of Europe, Russian Academy of Sciences; Head of the Department of International Economics and International Politics of the Higher School of Economics – State University
- Martti Ahtisaari** (Finland) President of Finland, 1994-2000
- Graham Allison** (U.S.A) Prof., Director, Belfer Center for Science and International Affairs (Harvard University); former Assistant Secretary of Defense in the first Clinton Administration
- Alexei Arbatov** Corresponding Member of the Russian Academy of Sciences; Director, Center of International Security, Institute of the World Economy and International Relations, Russian Academy of Sciences
- Lev Belousov** (Deputy Chairman) Dr. Sc. (History), Prof., Moscow State University
- C. Fred Bergsten** (U.S.A) Ph.D. (Economics), Director, Institute for International Economics, U.S.; former Assistant Secretary, Treasury Department, U.S.
- Carl Bildt** (Sweden) Prime Minister of Sweden, 1991-1994
- Vladimir Grigoryev** (in a personal capacity) Advisor to the Head of the Federal Agency for the Press and Mass Communications of the Russian Federation, former head of the Vagrius Publishing House
- James F. Hoge, Jr.** (U.S.A) Editor, *Foreign Affairs*
- Igor Ivanov** (in a personal capacity) Dr. Sc. (History), Secretary of the Security Council of the Russian Federation
- Karl Kaiser** (Germany) Prof., former director, German Council for Foreign Policy
- Irina Khakamada** Dr. Sc. (Economics), Assistant Professor; leader of the Our Choice party
- Helmut Kohl** (Germany) Chancellor of Germany, 1982-1998
- Andrei Kokoshin** Corresponding Member of the Russian Academy of Sciences; Chairman, State Duma Committee on CIS Affairs and Relations with Compatriots; Director, Institute on International Security Issues; former Secretary of the Security Council of the Russian Federation; former First Deputy Minister of Defense of the Russian Federation
- Mikhail Komissar** Director General, *Interfax* News Agency
- Vyacheslav Kopiev** Dr. Sc. (Law), Deputy Chairman of the Board of Directors, *Sistema* Joint Stock Financial Corporation
- Mikhail Kozhokin** Dr. Sc. (History), Vice-President, VTB Bank
- Yaroslav Kuzminov** Dr. Sc. (Economics), Director, Higher School of Economics – State University
- Sergei Lavrov** (in a personal capacity) Minister of Foreign Affairs of the Russian Federation

Alexander Livshits	Dr. Sc. (Economics), Prof.; Deputy General Director, Russian Aluminium Joint Stock Company; former Assistant to the President of the Russian Federation on Economics; ex-Minister of Finance; former Deputy Head of the Administration of the President of the Russian Federation
Vladimir Lukin	Dr. Sc. (History), Prof., Human Rights Ombudsman; Ambassador Extraordinary and Plenipotentiary of Russia
Fyodor Lukyanov	Editor-in-Chief, <i>Russia in Global Affairs</i>
Vladimir Mau	Dr. Sc. (Economics), Prof., Director, Academy of the National Economy under the Government of the Russian Federation.
Thierry de Montbrial (France)	Director, French Institute of International Relations; Member, Academie des Sciences Morales et Politiques, Institut de France
Vyacheslav Nikonov (Deputy Chairman)	Dr. Sc. (History), Prof., Chairman, <i>Polity</i> Foundation
Vladimir Ovchinsky	Dr. Sc. (Law), Adviser to the Chairman of the Constitutional Court of the Russian Federation; Major General (Ret.)
Vladimir Pozner	President, Russian Television Academy
Sergei Prikhodko (in a personal capacity)	Aide to the Russian President
Yevgeny Primakov	Member of the Russian Academy of Sciences; President, Chamber of Commerce and Industry of the Russian Federation; Prime Minister of Russia, 1998-1999
Vladimir Ryzhkov	Dr. Sc. (History), State Duma Deputy
Nikolai Shmelev	Member of the Russian Academy of Sciences; Director, Institute of Europe, Russian Academy of Sciences
Horst Teltschik (Germany)	Chairman, Teltschik Associates; Head, Foreign Policy Office of the Chancellor of Germany (1982-1998)
Anatoly Torkunov	Corresponding Member of the Russian Academy of Sciences; Prof., Director, Moscow State Institute of International Relations; Ambassador Extraordinary and Plenipotentiary
Lord William Wallace (U.K.)	Prof., London School of Economics
Sergei Yastrzhembsky (in a personal capacity)	Dr. Sc. (History), Aide to the Russian President, Ambassador Extraordinary and Plenipotentiary, Special Presidential Representative for Russia-EU Relations
Igor Yurgens	Dr. Sc. (Economics), First Vice-President, Head of the State and Government Relations Department of the Renaissance Capital Group; Honorary Vice-President, Russian Union of Industrialists and Entrepreneurs
Alexander Zhukov	Deputy Prime Minister of the Russian Federation
Sergei Zverev	President, KROS Public Relations Company, former Deputy Head, Administration of the President of Russia

BOARD OF ADVISORS

Anatoly Adamishin	Dr. Sc. (History), Ambassador Extraordinary and Plenipotentiary (retired).
Olga Butorina	Dr. Sc. (Economics), Deputy Director of the Russian Foreign Ministry's Moscow State Institute of International Relations
Vladimir Entin	Dr. Sc. (Law), Assistant Professor, Moscow State University; Senior Research Fellow, Institute of State and Law, Russian Academy of Sciences; lawyer; Director, Center for Intellectual Property Legal Protection
Leonid Grigoriev	Dr. Sc. (Economics), Senior Research Fellow, Institute of the World Economy and International Relations, Russian Academy of Sciences
Alexander Lomanov	Dr. Sc. (History), Senior Research Fellow, Institute of Far Eastern Studies, Russian Academy of Sciences
Georgy Mirsky	Dr. Sc. (History), Chief Research Fellow, Institute of the World Economy and International Relations, Russian Academy of Sciences
Mark Shkundin	Dr. Sc. (History), Senior Research Fellow, Institute of the World Economy and International Relations, Russian Academy of Sciences
Anatoly Vishnevsky	Dr. Sc. (Economics), Director of the Center for Human Demography and Ecology at the Institute of Economic Problems, Russian Academy of Sciences

BOARD OF TRUSTEES

Vladimir Potanin (Chairman)	President, Interros Holding Company
Sergei Generalov	Chairman, Association for the Protection of Investors' Rights
Andrei Kuzyaev	President, LUKoil Overseas Holding Ltd.
Boris Kuzyk	Corresponding Member of the Russian Academy of Sciences; Director General, New Concepts and Programs Holding Industrial Company; President, Institute for Economic Strategies
Valery Okulov	General Director, Aeroflot Joint Stock Company; member of the State Civil Aviation Authority Council; member of the IATA's Board of Governors; member of Aeroflot's Board of Directors
Ruben Vardanyan	President, Troika-Dialog Group
Simon Vaynshtok	President, Transneft Oil Transporting Joint Stock Company, Member of the Academy of Mining
Victor Vekselberg	President, SUAL-Holding
Vladimir Yevtushenkov	Dr. Sc. (Economics), Chairman, Board of Directors, Sistema Joint Stock Financial Corporation; Member of the Russian Engineering Academy and International Academy of Communications