

**Liberal Mission Fund**

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**A NEW ERA, OLD FEARS:**

a liberal's view of Russia

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## 1. SUMMARY

### ***A new era***

Russia has changed enormously since December 1999. President Yeltsin, who was synonymous with an era of crisis and revolutionary transformation, political confrontation and a weak state, has gone.

Our new president is young and healthy and has the new parliament on his side.

Yeltsin took over a Russia on the threshold of catastrophe and in the throes of destroying the institutions of a totalitarian regime. He saw the country through the manifold cataclysms that befell it, and handed over to his successor a Russia on the verge of a new, crisis-free era.

Things are a lot simpler for Putin than they were for his predecessor. He can wash his hands of a major part of the damage and miscalculations that the country has suffered, simply by default, and nobody will protest. The economy is growing and appears set to continue doing so for the next one to two years. As president, Putin has proven his decisiveness, and his actions - strengthening the state, curbing the powers of the regional governors and the oligarchs, tax reform, balancing the budget (for the first time) - have all brought success. Everything is working out ideally and it seems that nothing could possibly shake popular confidence in President Putin.

This is an ideal opportunity for Russia to enter a new era - an era of dynamic growth and recovery from our national depression. But how do we ensure that we do not miss out on that opportunity?

### ***The fears of the liberal intelligentsia***

A large proportion of the liberal intelligentsia is still dissatisfied. This dissatisfaction stems from a lack of confidence in Putin's ability to do with the required tact what the intelligentsia considers necessary: liberal reform of the economy, the establishment of the rule of law, and the creation of an equitable justice system. It also stems from what may be a reflex reaction - the feeling that it may not be right for liberal and democratic leaders to co-operate with him - a KGB man: "A KGB agent in the Kremlin: what a nightmare!"

Putin's decisiveness is impressive: we needed to see the regional governors and the oligarchs reined in, and the issue of tax reform was long overdue. On the other hand, the army is not sparing its bullets in Chechnya: there is no end in sight to that conflict. There also appears to be an element of threat to freedom of speech and information in the actions of the authorities, and suspicion is growing that they are prepared to use the law-enforcement agencies to resolve political objectives.

There is a clear contradiction within the government's policy: energetic action vs. unscrupulousness.

But is it really like that? Are these fears justified?

## ***Russia - a democratic country***

Both President Putin and the parliament were elected in democratic elections. Of course one can complain about the weak nature of Russian democracy, the fact that the Russian public is not used to democracy, or its susceptibility to manipulation by spin doctors. However, while such complaints may be justified, it must be remembered that democracy grows with time.

Sociological research has shown that the majority of the Russian electorate remains hostile to liberal and right-wing politicians. Liberals and the right-wing politicians currently enjoy the support of a mere fifteen per cent of the electorate. Any party that espouses liberal and democratic values must contend with this fact.

On the other hand, surveys have revealed that up to fifty per cent of Russians would like to live in a democratic Russia with a market economy. This was borne out by the results of the parliamentary elections in which approximately fifty per cent of the electorate voted for parties that support those objectives (the Union of Right Forces, Yabloko, Unity, and Fatherland All Russia, or OVR). This is no coincidence, but rather a historic expression of the will of the majority.

However, a majority within the fifty per cent prefer the so-called "parties of power" over the liberal parties: Thirty-seven per cent of the electorate voted for Unity and OVR.

An additional twenty-five per cent voted for the communists out of nostalgia for the socialist past. Another seven to eight per cent voted for nationalist parties with notions of empire. Thus, a clear trend is visible that has little to do with electioneering or election fraud. This is how our country is. Democrats must rise to the call of the majority of the population, i.e. to the results of a democratic system. An if democrats and liberals want to see things happen their way, they must convince a majority to vote for liberal politicians.

## ***Recent events: gale force democracy***

Democrats must not see recent events as a defeat for the liberal cause. On the contrary.

Only fifteen years ago, communist Russia was the "evil empire", Andrei Sakharov was under house arrest in Gorky, and the newspapers were reporting that he was being beaten by his wife. Few people doubted that the then-current order was unshakeable.

Mikhail Gorbachev drew on the malaise of sections of the Soviet elite that had sensed the imminent collapse of the Soviet system to open the valves of freedom, glasnost, and human rights and create a wave of democratic revolutions that brought new, decisive and uncompromising faces to the fore.

The democratic movement was radicalised at an early stage by such leaders as Andrei Sakharov, Boris Yeltsin and Galina Starovoitova. Their radicalism accelerated the collapse of the communist regime and provided fertile ground for market reform. However, the gale of democracy gathered too much force and became more than people could withstand: it exceeded what they were prepared for. Nobody expected that the reforms would lead to a deep and lengthy crisis, and so at the very first hurdles the wave of democracy broke and dwindled into numerous little currents. Some democrats simply refused to accept responsibility for this, others were deeply disappointed.

Russia, as it turned out, is a conservative country with an attachment to the traditional order of things. Russia is simply not willing to turn European at the blink of an eye. However radical Bolshevism may have seemed in its day, it turned out to be not very far removed from the autocracy it replaced or from a feudal system. The question now is, will this new democratic revolution be enough to overcome our inertia as a nation and to cure us of our propensity to limit freedom and dispose of power arbitrarily. The answer is far from clear. Hence our main worries.

### ***The trials of the economy***

The extreme economic problems that followed the initiation of radical reform measures were, of course, the main reason for the abatement of the wave of democracy. In 1992, prices rose twenty-six-fold, savings were wiped out, and industrial output dropped by fifteen per cent. Russia's GNP fell by forty per cent during 1992-98, while industrial output decreased by fifty per cent, household incomes by twenty-five to thirty per cent, and consumer spending by fifteen to twenty per cent. A clique of rich people emerged, but the majority went from poor to poorer. Having seen their lives turned upside-down, many people were obliged to change their social status and situation.

There are two ways of explaining the crisis. The first argues that the reforms were inappropriate and were implemented wrongly. A more gradual approach should have been taken and privatisation should not have taken place so abruptly. While nobody disputes the need for the market reforms *per se*, the majority of the population opts for this explanation without going into details.

The second explanation argues that the collapse of the Soviet economy with all of the attendant gruesome consequences was inevitable. It is pointless to look for someone to blame, because no leader, and no group of professionals, no matter how able, could have headed off the crisis once the early 1980's had passed. If we had started our reforms in the 1960's like Hungary or Czechoslovakia, if we had not halted the reforms of Kosygin, we could have followed a more gradual path. We wasted time, and collapse of "the System" inevitably led to a spontaneous uncontrollable crisis that swept away both the structures of communist utopia, such as the planned economy, and the fruits of the work of several generations. That was how things really happened.

The first explanation is emotional and impulsive: it has a ring of the truth about it. It has had an impact on the popular perception of the reforms and the actions of the reformers, and it contributed to the collapse of the democratic movement. Any rational and unprejudiced judgement will be based on the second explanation, however, in spite of the fact that errors and compromise did have a role to play.

It is crucial that public opinion should accept this explanation, as the transition period is far from over and people need to understand the reasons behind the country's economic woes.

The first and foremost reason concerns massive structural imbalances. Sixty per cent of industrial output in 1990 related to the military-industrial complex. Defence spending fell by a factor of six during the period 1992-1996. Clearly, if industrial output fell by half, then the fall in output in the military-industrial complex accounted for at least 30 to 35 per cent of the drop in overall production. What remained of our military output was, however, still enough to allow us to export approximately USD 2 billion worth of arms a year.

Our closed economy failed to encourage effective management, with the result that our consumer goods were generally of extremely poor quality, and the cost of production was high. The onset of competition brought by an open economy, the arrival of consumer choice, and reduced

consumer demand led to a fall in output of poor quality goods. This contributed at least another 10-15% to the fall in production, bringing the total to fifty per cent. According to official statistics, imports also fell during the period in question (from USD 81.8 billion in 1990 to USD 26.8 billion in 1993 - the lowest level since the reforms began). The 1993 statistics should be increased by approximately one third to allow for undeclared imports.

The same failure to encourage effective management also made the Soviet economy highly wasteful. Hence the disproportionate role of mineral extraction and raw materials production.

For many years Soviet economists had been calling for increased investment into the manufacturing and consumer goods production. It would now seem that market reforms have only increased the slant towards the mineral extraction industries. This is a weakness that has been turned into a strength: raw materials, fuels, metals, and fertiliser have formed the basis of Russian exports, brought the country foreign currency earnings, and supported its credit rating.

The second reason for the severity of the crisis concerns the total institutional incompatibility of the planned and market economy systems. Nothing could be used as legacy. What was needed was a fresh start. Combining components from the two systems only impairs their integrity and effectiveness. I studied this issue long before the reforms and set forth my findings in a 1989 publication. I foresaw the inevitability of radical reform in Russia.<sup>1</sup>

The third major reason for the crisis was to be found in the sea-change that the Soviet era provoked in people's mentalities and in their values and system of motivation. The new breed of Soviet people- "Homo sovieticus" - were irresponsible and undemanding, with a poor labour morale and a high degree of dependence. In East Germany socialism lasted less than 40 years. Over the ten years following reunification, the eastern regions of Germany received USD800 billion in investment. Productivity in the east remained at 70 per cent of western German levels, unemployment climbed to 20 per cent, and 30 per cent of the electorate voted communist. Such is the "mighty strength of communism". What then is this compared to Russia, which is ten times bigger, spent 75 years under communism, and received only USD 22.5 billion in loans from international financial institutions over the same period. Plus the USD 63 billion that was lent to Gorbachev. The brain disorder that Mikhail Bulgakov spoke about has not yet been cured.

The factors described above have made the adaptation to market conditions a lengthy and arduous process. The process of establishing the institutions of a market economy, including institutions of state power, has been lengthy and characterised by abuse, corruption and organised crime. For seventy years we trained the militia to chase after underground entrepreneurs, and now we suddenly declare the importance of respecting private property.

Leszek Balcerowicz, the Polish reformer, once said that building socialism from capitalism is like trying to make fish soup from a bowl of goldfish, and that building capitalism from socialism is like trying to make a blow of goldfish from that same fish soup. His hyperbole is of course not far from the truth, particularly in the case of Russia.

Arguments against shock therapy are easily understand. Russia definitely underwent shock therapy, and not in its traditional form as an approach to combating inflation, but in the form of economic liberalisation with the aim of solving the economic problems described above in as short a period of time as possible. While the result was not out-and-out success, I would say that it was a blessing, or rather luck, that a mass democratic movement, even if short-lived and removed from the grass roots, created the conditions for a breakthrough: for major market reform concentrated

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<sup>1</sup> Y.G. Yasin, *Economic Systems and Radical Economic Reform*, Moscow, Ekonomika, 1989, p. 182

within a short period of time (approximately 500 days) and for Yeltsin to entrust those reforms to Yegor Gaidar. If it had not been for this coincidence of historical circumstances we would still be tormenting ourselves with "intractable" problems that we have already forgotten existed. We are now faced by other problems that we either refused to face in the past or that we were prevented from resolving by overwhelming opposition.

In any case, this inevitable and extraordinarily deep crisis, which was caused by communism and only triggered by the liberal reformers, has been the predominant issue of the past decade. It has determined the mood of society and the political evolution of the country as a whole.

Of course it was inevitable that the dogs would be let loose on the reformers. The reformers have even to a certain extent become rejects of society. One young businessman who would appear to be a natural follower of Gaidar said to me "Oh, not him!".

These people knew what they were doing and they can be satisfied with their work: Russia has changed, for the better. Russia is open to new possibilities.

We have nothing to be ashamed of: the deed is done, communism is dead, and we now have a developing market economy. And we are the ones who did it!

### ***The distribution of forces***

Now let us consider the layout of social and political forces in Russia at the last elections. It is, after all, this factor that will determine the manner in which the country will develop in the coming years.

If Marxist doctrine is to be believed, then Soviet society was a classless but caste-based, hierarchical society. A person's social status depended on his or her position within the party and state hierarchy. Wealth, property and background carried little weight. Voslensky called the upper reaches of the Soviet hierarchy the "nomenklatura", and the term stuck. The nomenklatura was the Soviet elite. Lower down on the social ladder were the labouring masses who were supposed to be happy because in addition to their miserly salaries, the state gave them free housing, education, healthcare and many other benefits.

Those who worked in priority areas of the economy - the military industrial complex, the atomic industry, etc. - were better off than others. Retail trade was a particularly strange area. Those working in retail "sat on their shortages", gave priority to the nomenklatura, and didn't forget to help themselves. The retail sector also sheltered the remnants of entrepreneurialism and the shadow economy.

The nomenklatura, who one would have thought would have been committed to maintaining the status-quo, in fact became one of the major initiators of the reforms with the intention of retaining their privileges and removing the restrictions on accumulating and inheriting wealth. The nomenklatura was aiming for bourgeoisie status. The rest of the population was supportive of the reform initiative. The unanimity that existed with regard to this issue by the end of 1991 provided the social basis for the mass movement towards democracy.

However, when the reforms actually started it became clear that businessmen who appeared out of nowhere would be the only ones to benefit initially. The entrepreneurial class began to emerge openly with the passing of the Law Concerning Co-operation (1988).

The nomenklatura, for its part, soon realised that it would have to abandon many of its privileges, that its position in this new world was no longer guaranteed, and that it would have to fight to win back its former status. And not all were capable of that. The very values of the Soviet elite, including their ideas on Russia's state interests, were put in question and so the majority of the former nomenklatura went into opposition.

The labouring masses, on the other hand, suffered the greatest losses from the very outset of the reforms and experienced the greatest disappointment. It was for this reason that two parliaments (the Liberal Democratic Party of Russia - 1993 and the Communist Party of the Russian Federation - 1995) found themselves in opposition to the regime of Boris Yeltsin.

By mid-1992 the reform-process had lost the support of the public and Yeltsin found himself obliged to use his enormous authority to support the reforms. The situation was untenable: Yeltsin's authority melted away, and his ratings fell.

Entrepreneurialism was a natural pillar of the market reforms, but it was a pillar that had weak foundations in society as a whole. The entrepreneurial class that emerged was made up of the successful, those who got rich quick (often by manipulating the budget) and who then began to yearn for influence over state policy. The state had to rely on this new entrepreneurial class initially, a class that later became known as "the oligarchs".

At the same time, the civil service - the last remaining element of the old administrative hierarchy - began actively to recruit new people, including democrats, and this diluted the remaining vestiges of the nomenklatura. Only a few of the new recruits were guided by an idealistic desire to serve their country. Given the miserly nature of the salaries of Russian civil servants, most dreamt of using their positions to enrich themselves. This led to corruption and to the convergence of functions of state with business interests that saw an opportunity to prosper at the expense of the state. Thus was born the new nomenklatura - senior civil servants plus businessmen who received favours from the civil servants in return for payment.

Russia's industrial priorities also changed. The military industrial complex and the atomic industry, which hitherto had been subsidised by the state, suddenly found themselves poor. The people who these industries had supported also found themselves suddenly deprived. These people, who had once constituted elite groups, suddenly lost their financial weight. They were replaced by representatives of the exporting industries - oil, gas, aluminium and nickel, and trade, banking, and the infrastructural monopolies. Thus, over a period of three to four years, Russia saw major upheaval in its social structure. The new face of Russia has not yet been fully formed.

At the level of the elite groups, however, and their political representation, the main forces have already been defined:

**The old nomenklatura**, represented by the Communist Party of the Russian Federation which claims to represent the suffering masses, patriots, and proponents of a strong state.

**The new nomenklatura**, whose political representation changes with the establishment of each new "party of power" (Our Home is Russia, OVR, and, now, Unity). Unity is currently striving to acquire the image of a centre-right party of liberal proponents of a strong state. In reality, however, Unity is merely a magnet for people with a desire to be close to those in power. The new nomenklatura is further riven by competing groups. Hence the manifold rivalries between various movements on the one hand, and the frequent attempts at political consolidation on the other. Their basic tactic is to target wavering voters who are easier to seduce with populist slogans.

Russia's **middle class** consists of small, medium and large entrepreneurs who have no access to state resources; qualified workers and professionals, and others who have adapted to life in market conditions and are objectively committed to living in a democratic free-market economy, if the term "middle class" can be used to describe collectively these categories of citizens. Major entrepreneurs may also be termed "middle class" provided that they do not benefit from privileges acquired from the state. Their natural political representatives are liberal and democratic political parties and movements such as the Union of Right Forces and Yabloko.

Of course, the foregoing is only a basic outline. In real life, things tend to be more complex, ill-defined, and fluid. Nevertheless, it is an outline that provides a reasonably clear explanation for the current contradictions and conflicts of interests that exist within Russian society and the political forces that will be deployed for their resolution.

### ***The main conflicts***

The principle conflict of the 1992-1997 period, which took place against a background of market reforms, was between the old nomenklatura on the one hand and a coalition of the new nomenklatura and the liberal reformers on the other. It was a conflict that postulated a return to a Soviet-type economy, based on the Lukashenko model in the best scenario, against the continuation of market reforms and democracy. Boris Yeltsin's re-election for a second term with the help of the oligarchs signalled victory for the coalition, a victory that we now see as definitive. It also led to the collapse of the coalition.

The information wars waged in 1997 by the oligarchs against the young reformers - Chubais and Nemtsov - signalled the shift to a new phase in which the conflict between the new nomenklatura and the middle class became all-pervading. This conflict was essentially between nomenklatura, or crony, capitalism, which is very dangerous for any country since it places state policy subject to the mercenary whims of lobby groups, and the free-market economy and democracy that would give the country hope.

It should be noted that the factors that led to this conflict are not necessarily short-term in origin. It may turn out that the new president will throw out the oligarchs, take on the regional governors, promote market reforms, and thereby undermine the position of the new nomenklatura. In that case, the conflict between the middle class and the new nomenklatura will calm down. Things may very well turn out this way. Unfortunately, however, things are never so simple. The current actors will inevitably be replaced by others in the same roles. Civil servants will benefit from the weakened position of "their" businesses, or vice-versa. The very structure of the new nomenklatura will change. The new nomenklatura is proving extremely tenacious in the face of the will of the president, and will become even more entrenched if he decides to seek their support. The very fact that the president requires a broader support base than what the liberals can currently provide will oblige him to seek the support of the new nomenklatura. Indeed, the new nomenklatura is the natural choice: it is malleable, obedient (or gives the appearance of being so), and adapts well.

So far the balance of power lies in favour of the new nomenklatura, especially given the fact that its conflict with the old nomenklatura has abated. The new nomenklatura has won wavering, easily manipulated voters to its side. The forces of liberal democracy are now much weaker within the executive bodies, the parliament and the regions.

It is generally unclear where liberal democrats should now turn for support, for all factions are now contending for the support of the middle class. Liberals are prepared to renew their coalition with the new nomenklatura for the sake of continued reforms. However, times have changed, and it looks likely that they will continue to be forced into opposition.

Indeed, their experience in opposition is likely to prompt them to unite forces and jointly promote their policies as the natural consequences of policies devised to favour the new nomenklatura become apparent. They achieved a breakthrough during the parliamentary elections, despite the fact that they were forced to fight among themselves for the vote of the democratic voter. The democrat-rejection syndrome that was so apparent during the reform period appears to be weakening, and this is a real and important victory. A victory that can be used as a foundation stone.

## 2. Today and tomorrow

### *Putin's mission and strategy*

That is the nature of the country governed by our new young president. Before praising him, judging him or cautioning him, it is important that we should try to understand the problems that he is faced with, and to appreciate the difficulty of the choices he will have to make.

Russia has only finished phase I of the market reforms, and quite dramatically so - with the crisis of 1998. These first stage reforms have pre-empted worse disasters, placed the country on the rails that lead to a market economy, and opened up the way to economic development. Objectively they have led the country to the epitome of crisis; subjectively they have thrown the country into a nationwide depression. While opening up the way to economic development, the reforms are in themselves no guarantee of a rosy future: they do not provide an easy remedy to the problems that now beset Russia.

Phase II of the reform process must now begin. The main aim at phase II is to restructure and modernise the economy, and to spark growth. All previous government programs have envisaged a transition to phase II based on the following hypothesis: liberalisation and macroeconomic stabilisation must be followed by growth in industrial output and investment.

The truth of that hypothesis has been apparent since 1997, with the exception of the 1998 crisis period. The crisis worked to the overall benefit of the economy, especially in the production sector. The rouble devaluation and improved competitiveness of Russian goods were of course important, but equally important were the reforms that enabled the emergence of a market sector that is prepared to make use of the opportunities on offer. The proof of this is to be seen in the increase in investment that began in the autumn of 1999.

Nevertheless, it is generally accepted that the current positive trends in the economic situation are mainly the result of external factors. Investment comes nowhere near the levels required by an economy that has been starved of investment for decades. Macroeconomic stabilisation has been achieved at a very low level that is seen by society as a dramatic decline. In view of the specific situation in the post-communist Russia, far-reaching institutional reforms on a scale that has not been fully appreciated since the beginning of the reform process will be needed if we are to achieve sustained economic growth and a favourable investment climate.

Vladimir Putin is young and determined. He is capable of making a sober assessment of the situation and of his understanding of his mission: if he carries it through, he will secure to himself a glorious place in the history of his country, having reaped the fruits of the work of his predecessors who were forced to go before those fruits had ripened; if he fails to carry his mission through, he will make an inglorious exit and Russia will be beset by further upheaval.

His threefold mission is quite straightforward:

1. To drag the country out of its crisis and improve living standards;
2. To restore Russia to her position within the world order, and to restore the confidence and national pride of the Russian population that was destroyed by the fall of the USSR and the crisis;
3. To ensure that Russia develops along democratic lines by respecting human rights and freedoms, civil society, and the rule of law.

There is, of course, no guarantee that Vladimir Putin understands his mission in exactly these terms. There are however grounds for believing that this is not far from the mark. He proposed to develop a long-term strategy - a convincing program that was put together by Gherman Gref's Centre for Strategic Studies.

Vladimir Putin's program can be summed up as follows:

- 1) A strong (or "efficient", if "strong" sounds ambiguous) state. These are his own words. However, unfortunately it is not yet clear exactly what he means by this;
- 2) Liberal market reforms aimed at mobilising private initiative to promote economic growth.

Given everything that has happened in this country over recent years, no right-thinking person could possibly oppose these objectives. One can only seek clarifications.

### ***The economy: dragging the country out of crisis***

The restoration of order, the strengthening of the state, the stemming of the influence of private lobby groups and the elimination of corruption are all goals that are supported across the political spectrum. Even inveterate liberals, who seek a drastic reduction in state spending and the withdrawal of the state from the economy, agree that the state must be capable of effectively carrying out its functions, and that today it is not.

The need to continue with the liberal reform process is less obvious at first glance only. Clearly, rapid economic growth is imperative if we are to head off approaching threats, remedy our country's social and political problems, and strengthen democratic institutions. There are two logical ways of stimulating economic growth. The first, proposed by left-wing, academic economists, and proponents of a strong state, implies an active role for the state in the economy, major state spending (and the resulting high taxes), and protectionism. Our recent past, current circumstances, the need to integrate Russia into the world economy, and our realistic possibilities (our budget, the corrupt state of our civil service) force us to reject this approach. Curiously, the most successful national development programs envisaging a major role for the state have generally been carried out within market and semi-market/semi-feudal economies, and never in seventy year old planned economies. It is nonsense to assume that a collapsed planned economy can be remedied with a weaker form of the same methods.

The second approach involves facilitating private initiative, removing restrictions to the maximum possible extent, equalising the competitive playing field by removing privileges and exemptions, and reducing taxes and state spending. This approach promises the best chances for success for the Russia of today, especially given the fact that a measured role for the state can be envisaged where necessary.

Included in this approach is the long-overdue issue of social reform. Social reform is quite a sensitive matter. It involves changing the way in which people have become used to living their lives, rather than directly invoking improved standards of living. Social reform must have the aim of establishing a more productive system of values - one based on individual responsibility, one that overcomes the current culture of dependence.

The guiding philosophy behind the program developed by Gherman Gref's Centre for Strategic Studies, or the "business idea" as it is now termed, is outlined in figure 1.

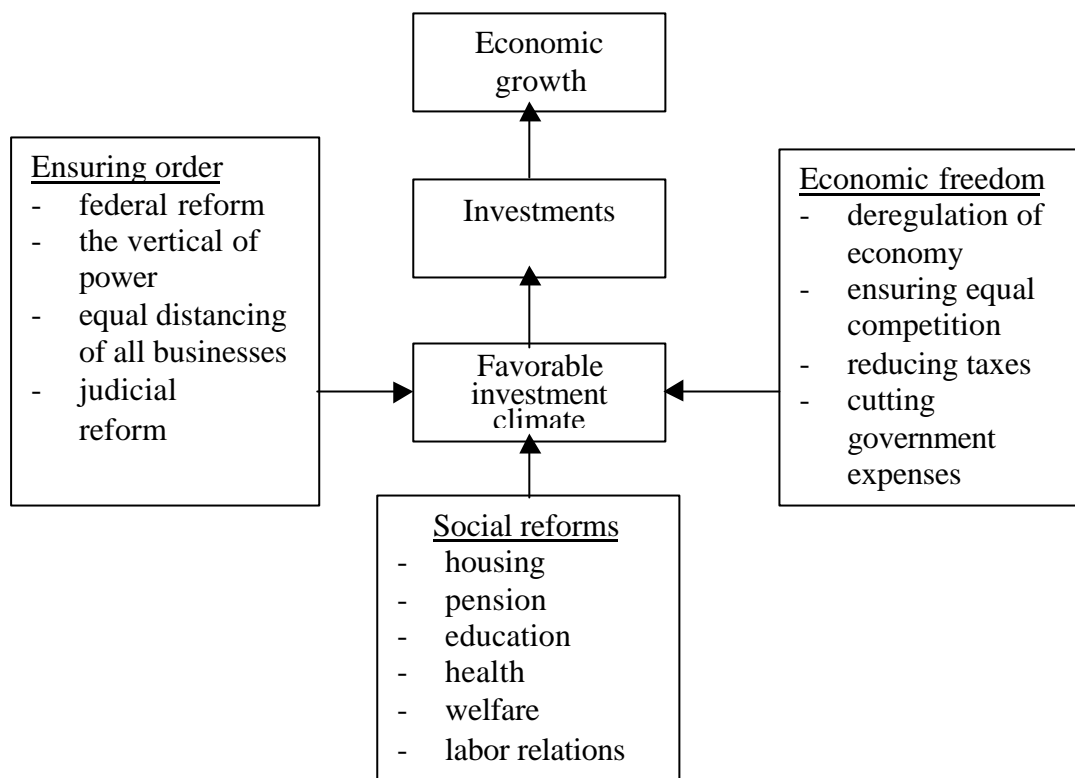


Figure 1 A conceptual framework for economic growth (the Gref program)

The government has only adopted the part of the Gref program that concerns the economy. The other part, which deals with reform of government, has been placed on hold for the moment, despite the fact that it contains the most important component of the reform program - judicial reform. It also deals with state management and methods of implementing the program.

The economy section of the Gref program is a direct descendant of the young reformers' 1997 program and its predecessors. Generally, it sets forth the tasks that need to be accomplished in order to establish an effective market economy in Russia.

The most important issue, of course, is how the program will be implemented. It is important in this regard to establish the correct priorities, to evaluate the risks, to define clearly the key problems to be solved, and then to concentrate all resources on resolving those problems. The methods selected to implement the program will depend directly upon these factors.

The two main threats to the successful implementation of the program are poverty and economic backwardness.

### ***Threats: poverty***

Despite certain improvements over the last two years, living standards remain 15-20% lower than pre-crisis levels. Living standards followed an identifiable cycle over the decade of reform: a noticeable fall following each crisis to be succeeded by a gradual recovery not quite reaching pre-crisis levels, and then another fall with the onset of the next crisis. This was the case in 1992, 1994 and 1998. Living standards remain in decline on the whole, especially if one takes into consideration the drastic gap in incomes and material wealth between various sections of the population. Few Russians have the resources to take advantage of the bountiful consumer market to

improve their quality of life. A third of the population is existing on less than the survival minimum.

Past experience has shown that inflation is the main culprit in falling living standards. Inflationary episodes in 1992, 1994, and 1998 caused by budget deficits, the reckless printing of money, and a falling rouble led to dramatic falls in incomes, rendered savings worthless, and widened the gap between rich and poor.

While the federal budget currently runs at a surplus, this has been mainly thanks to high oil prices, the devaluation of the rouble, and the elimination of many items of budget expenditure. It is also important to note that following 1998 Russia defaulted on a range of international obligations. Thus, the current budget surplus cannot last indefinitely. Many regional budgets are in dire straits. The current tax reforms, while necessary, are fraught with risk: what if the economy fails to respond to reduced rates of taxation with an increased taxable base?

While the danger of inflation remains, there remains the danger of new falls in living standards. The situation as it currently stands means the denial of the benefits of modern civilisation to a large proportion of the Russian population, denial of the opportunity to develop their human potential, and reduced competitiveness on the labour market. The danger is one of the further degradation of human dignity and the destruction of a unique and great culture.

A temporary decline in living standards during a period of reform is always a possibility, and often an inevitability. However, if that decline becomes long-term due to an extended crisis, the resulting changes can be irreversible. Vladimir Putin expressed particularly strong, even perhaps exaggerated, concern to the Federal Assembly over this issue, specifically, with regard to the demographic forecasts.

### ***A backward economy***

**The second major comparable threat** is closely related to the first and concerns **growing technical under-development**.

The USSR was far from the forefront of world technological advances, with the exception perhaps of the arms industry and certain related sectors. Certain industries such as nuclear technology, space technology and the arms industry were particularly strong, and many industries had their own research and design institutions which could under the right circumstances be competitive on world markets. In this sense it is reasonable to speak of Russia's considerable scientific and technological potential, even if that potential was created at a disproportionately high cost to the economy.

It is important to note the difference between Russia and other second-tier countries such as Brazil and Korea that are striving to join the ranks of the first world: Russia has the necessary scientific and technological potential to trigger growth in these sectors.

The second-tier countries that have achieved the highest levels of growth over the past decades have been those that have pursued strategies of seizing upon the technological innovations of the leading economies, reproducing those innovations at minimum cost, and then targeting market niches from which the developed countries have withdrawn. Second-tier countries rarely succeed in becoming independent centres of technological innovation. Japan, a clear success story and in many areas a leading centre for technological innovation, is in fact not such a centre at all. Japan's success lies in the remarkable speed with which it masters new technologies and then uses those technologies to develop new devices with meticulous attention to detail.

Russia still has a core group of people engaged in the development of technological innovations. The frightening thing is that the core has been in sharp decline over recent years and that it won't be long before it disappears altogether. If that happens, it will be a long time before Russia regains the potential to join the leading innovative nations.

Russia has always been a pioneer of manned space-flight. With much effort we succeeded in creating the Zvezda living module for the Alpha international space station. I fear that within three to four years we will have lost the ability to build the Zvezda module independently.

We have already lost our potential in many other sectors: we have lost qualified professionals, production of materials has stopped, and we have been neglecting advanced technologies for years on end.

The foregoing, coupled with the deterioration over many years of our asset base and inadequate levels of investment, threatens to impair production, even assuming the presence of demand, simply by force of the absence of effective production facilities.

Temporary setbacks in the technological sphere are always a possibility in a time of crisis. However, they cannot be allowed to last indefinitely. There is only one solution to the problem: economic growth creating increased demand for innovative products and opening up the way for increased funding to research and development.

### ***Resistance mechanisms***

In addition to the above threats, the Putin-Gref program runs the risk of encountering other problems to which the program does not provide adequate solutions.

The following idea, I remember, was popular within cybernetics in its day: if a well designed piece of machinery is performing poorly, it is because another piece of machinery is impeding its performance. The government needs to identify that other piece of machinery, study it, and take it apart. The government's objective must be not merely to remedy certain individual weaknesses, but rather the whole inter-dependent, mutually-supporting system that is offering the resistance to reform.

Does such a thing exist? Undoubtedly! Figure 2 contains a schematic representation of the resistance mechanisms. The network of problems that forms the resistance mechanism is illustrated in the centre of the diagram. The right-hand side of the diagram illustrates how those problems manifest themselves, and the left-hand side illustrates the negative consequences of the failure to provide remedies. I believe that the non-market sector of the economy, the shadow economy, and our weak banking sector represent the core of the change resistance mechanism.

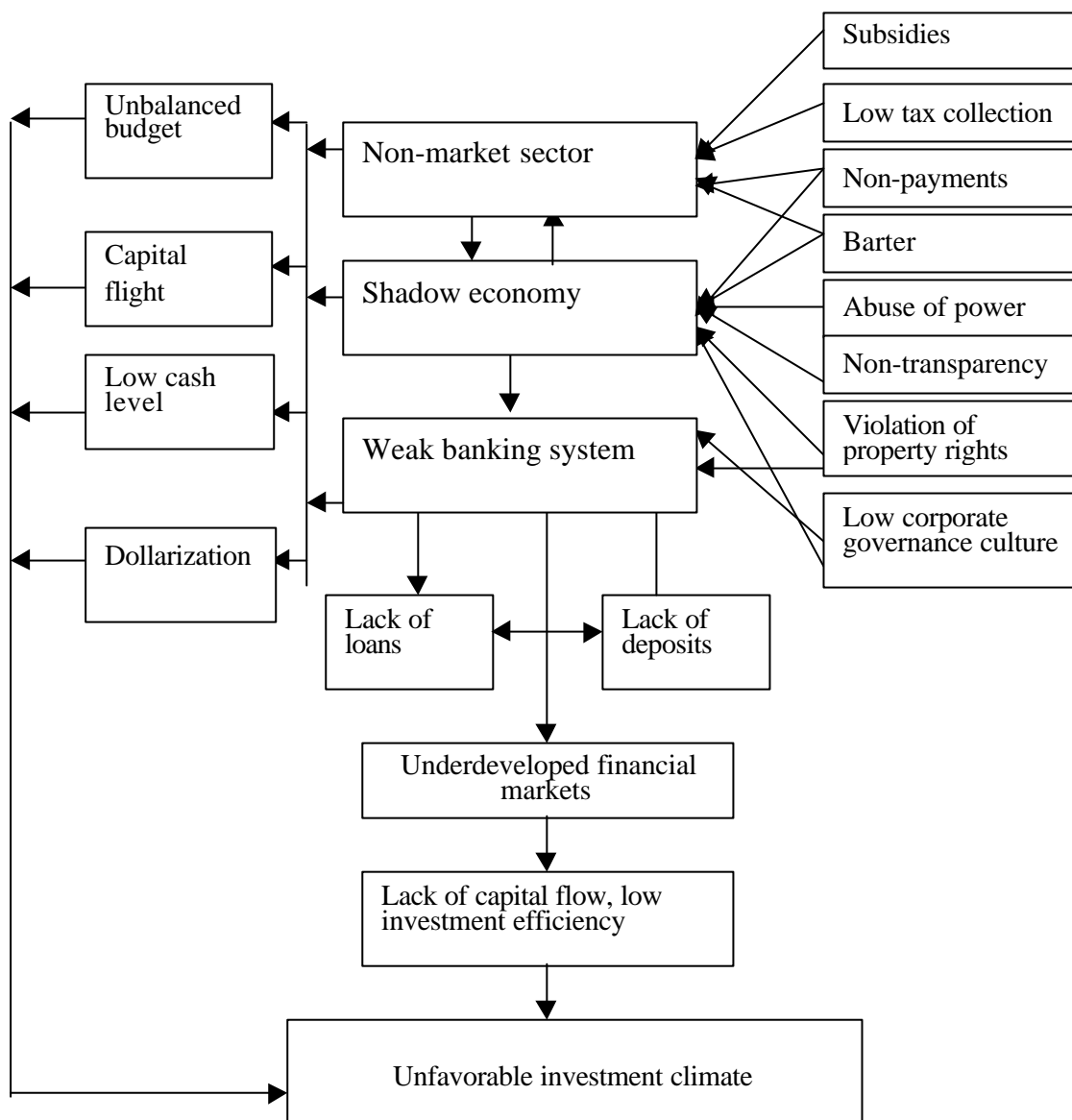


Figure 2. The resistance mechanism

### ***The non-market sector***

By "non-market sector" I mean ineffective and loss-making enterprises producing negative added value. This sector has been inherited from the Soviet system.

The root of the problems of the non-market sector lies in the fact that from the very outset of the reforms it sought and found ways of surviving using covert and overt subsidies, tax evasion schemes, barter, mutual offsetting of debt, etc. The government acquiesced in order to avoid adverse social consequences of intervention, and also because the continued existence of such enterprises was beneficial for certain lobby groups. The non-market sector sucks up a significant proportion of the resources that could feasibly be used to develop other sectors. This state of affairs constitutes a serious obstacle to investment and economic growth. The non-market sector is cloaked in an unhealthy cloud of secrecy and mutual connivance: "the fault lies with the reforms, not with us". Fenced off by debts and barter, the non-market sector continues to live a quasi-Soviet

existence, refusing all attempts at serious restructuring and preventing others from restructuring. By its very existence it seems to say: "scheming is more profitable than to work productively".

Differing opinions exist with regard to the urgency of the problem and even the size of the non-market sector. Officially, 40 per cent of Russian enterprises are loss-making. Until the 1998 crisis, that figure stood at 60 per cent. The reduction was principally a result of the devaluation of the rouble. Unfortunately, however, there have been no improvements in the quality of goods produced, the quality of the production facilities, or the quality of corporate management.

Another body of opinion suggests that the non-market sector has retreated to a large extent over recent years and that the problem is no longer so urgent. For the most part it is enterprises that take cover behind various illegal schemes that tend to be loss-making. The genuinely loss-making firms have already closed up shop. Sharper definition of property rights, increased control, pressure from creditors and the real threat of bankruptcy quickly yield results: money suddenly appears and debts are gradually paid off.

This is borne out by the success achieved by the Ministry of Railways, RAO UES Russia and Gazprom in increasing the proportion of cash payments collected for products and services sold. Tax collections have also increased. There has been a considerable decrease in non-cash payments, barter, and mutual offsetting by major taxpayers and monopolies. In June 2000, 67.7% of settlement carried out by such organisations were cash payments, as opposed to 47.1% in December 1999. Barter settlements fell from 11.5% to 3.4% over the same period, and mutual offsetting - from 25.8% to 16.8%. While the official data may be understated, the Russian Economic Barometer also bears out the above hypotheses: barter transactions fell from 34% to 21% between July and October alone. This may point to a breakthrough. We can only hope so! Although it may simply be that one set of well-known survival strategies is simply being replaced by another without any real improvement in the overall health of the economy.

Yet another body of opinion holds that many companies, including some that are profitable on paper, only continue to exist thanks to overt or covert subsidies. These can include reduced and fixed prices for electricity, heat, gas, or rail transport. Transactions settled by barter, also a form of "subsidy", usually involve higher prices than equivalent transactions settled in cash. Furthermore, many barter transactions are never reflected in accounting records and therefore the above statistics, and indeed any statistics that compare cash with non-cash settlements, should be disregarded as unreliable. Thus, transparency suffers as a result of the wideness of the gap between reality and its reflection in accounting records. If the specific weight of the non-market sector within the economy can be said to be falling, then it is happening at a very slow pace and possibly as a result of current economic situation: falling oil prices or a stronger rouble could very well turn that process around and send the non-market sector back into expansion. The Russian economy must undergo full-scale modernisation before we can talk of any real progress in this area. That modernisation is only just beginning, and the non-market sector represents an obstacle.

Which of these positions is correct? We cannot say for sure. I would say that both are to a certain extent true. Research needs to be carried out in order to determine the scope of the problem.

My hypothesis is as follows: 40 per cent of businesses are loss-making. If it is accepted that both positions are correct, then this figure is more or less accurate. In 1992, the non-market sector accounted for between 80 and 90 per cent of Russia's industrial output; today that figure has fallen to ten to fifteen per cent. Thus, the elimination of the non-market sector will inevitably lead to a slump in output, which may, possibly, be compensated by growth in profitable and competitive businesses. The non-market sector also accounts for between 25 and 30 per cent of all jobs in

Russia, which means that the full-scale modernisation of the economy will have serious social implications.

Inherent in the Gref program is the elimination of the non-market sector. The program aims to level the competitive playing-field for business by eliminating subsidies and exemptions. The only question remaining concerns the methods to be used to achieve that goal. So far we only have a general idea of how to go about that task, although it is clear that we cannot simply turn around one day and cancel all subsidies in the way that the president threw the regional governors out of the Federation Council. Whichever way the rouble goes, it is clear that we simply must upgrade our production facilities and technology, we must overhaul our management cadres, we must free up and retrain our workforce, we must provide proper motivation for employment, and we must adhere strictly to the limitations imposed by our budget. For this we will need a strong banking system that will be capable of lending to viable businesses to cover their working capital requirements at least. If we don't have that, we will go nowhere.

### ***The shadow economy***

The shadow economy is closely linked with the non-market sector. This is primarily due to the fact that the shadow economy and the non-market sector are inter-dependent carry-overs from the Soviet economy. The non-market sector fosters a culture of non-cash payments, barter, and mutual settlements, since it has no other way of earning money. The shadow economy exploits this, and carries non-market settlement practices well outside the non-market sector in order to turn illegal earnings. The shadow economy also feeds the non-market sector by making available various illegal methods of redistributing financial flows and property rights.

The shadow economy is also closely tied with state interference in business and the influence of bureaucracy. Bureaucracy is a breeding ground for corruption that impairs business and compels companies to avoid contact with government agencies. Notwithstanding the economic liberalisation that took place in the first half of the 1990's, bureaucracy, especially in the regions, continues to have a stifling effect on business.

According to the most conservative estimates, Russia's shadow economy accounts for 20 to 25 per cent of total national GNP. Practically all businesses in Russia now carry out illegal transactions to one extent or another. The shadow economy is now too profitable for too many people to be easily eradicated.

Of course any statistics on the shadow economy are by their very nature approximate. Perhaps the only reliable source of information is sociological research. Klyamkin and Timofeyev<sup>1</sup> found that 53 per cent of those surveyed who had had occasion to avail of consumer services (car repairs, television repairs, apartment decoration, etc.) had paid for the services in cash and had not received a receipt. Only 37 per cent of those surveyed had settled by bank transfer or credit card (p.15). Fifty per cent had paid at least once for medical services in state hospitals that are formally provided free-of-charge. Forty-seven per cent understand or approve of the actions of managers who pay their employees in cash unregistered in the payroll schedule and another 16 per cent had no opinion on the matter. Only 22 per cent of those surveyed condemned such practices, and only

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<sup>1</sup> I.Klyamkin &L.Timofeyev, *Life in the Shadows*, Russian State University of the Humanities, Moscow, 2000.

7 per cent of entrepreneurs did so too. Thus, from Soviet times till now the majority of the population has been accepting the existence of the shadow economy as normal.

An unwritten set of rules seems to have emerged that millions of people are following. This unwritten set of rules is a major contributing factor to the lack of transparency in the Russian economy. It provides fertile ground for corruption and other abuses. The shadow economy is an intractable institutional trap. If we fail to break free of it we can forget about any massive inflow of investment or strong economic growth. There appears to be a certain unwillingness to discuss the issue, even though it is clear that economic measures such as tax reform, and force, will not be sufficient to provide a solution. Force, if it is not applied completely within the law, tends to yield the opposite results to those sought.

### ***A weak banking system***

Up until the 1998 crisis, our banking system appeared to be at the forefront of our fledgling market economy. In actual fact, it was then and continues now to be weak for a number of objective reasons.

Total bank capitalisation at July 1, 2000, stood at RUR 206.6 billion (USD 7.4 billion at an exchange rate of RUR 28 per dollar), this following 23 per cent growth in the first two quarters. All of the world's one hundred largest banks have higher levels of capitalisation.

Table 1 illustrates details of lending by Russian banks.

### **Bank investments into lending 1998 - 2000 (RUR billions)**

Table 1

		Of which:			Previous year's GNP in RUR billions	Lending as a % of GNP
		RUR	Foreign currency	To banks		
January 1, 1998	276.1	163.3	112.8	36.9	2521.9	10.9
January 1, 1999	421.6	123.2	298.4	58.1	2696.4	15.66
January 1, 2000	596.8	292.7	304.1	89.7	4545.5	10.9
July 1, 2000	701.9	383.5	318.4	83.0	6450**	10.9

\*) source: *The Central Bank's Bank Statistics Bulletin*

\*\*\*) as forecast for 2000 in the draft of Budget 2001.

Despite strong growth in rouble lending, total lending has fallen: the foreign currency and interbank lending markets are in stagnation. Growth in bank assets is leading to increased balances on banks accounts at the Central Bank rather than to increased lending. Despite Viktor Geraschenko's hale and hearty pronouncements to the effect that the banking sector is stronger than he expected, the situation is critical: strong growth will not be possible without increased bank lending.

The weakness of the banking sector stems primarily from the overwhelming size of the non-market sector and shadow economy.

Banks cannot lend to the non-market sector: it does not repay its borrowings. Deposits are also low, and this has a dampening effect on bank lending resources and capitalisation. With such

low capitalisation levels, banks are unable to take risks. Hence the weak role of cash in the economy, low demand for the rouble, non-payments, and barter.

The shadow economy, for its part, prefers shadowy schemes and laundering to normal banking transactions. This attitude is fuelled by the fact that the government simply will not let go of the Leninist idea of turning commercial banks into agents of state control. It would be interesting to see what percentage of total revenues from trade passes through the banking system. I would be surprised if it was more than half.

I asked a prominent western banker if he intended to begin lending to Russian businesses and to invest in Russian banks. As a long-time friend of Russia, this particular banker was aware of the importance of this issue for us. His answer to both questions was "no".

The first "no" was followed by "we will lend to Russian businesses if they agree to adhere to our standards of transparency. But unfortunately they prefer the shadow economy".

The second "no" was followed by "Russian banks are prepared to work with Russian businesses on their own terms. For that reason they do not inspire trust".

The banking system is a major cause for concern to both the government and the Central Bank. Unfortunately the plans drawn up by the said institutions do not inspire confidence.

Financial and capital markets cannot exist without a developed banking system. The logic behind this is simple: apart from risk speculation, the most profitable investments are investments into current assets (investments covered by short and medium-term loans). At the moment supply is not sufficient to cover demand in this area. There is further room for banks to profit from short term loans. Other investments, both direct and portfolio, will continue to have a negligible effect upon the economy notwithstanding the attempts to present any securities as blue chips.

There is a law in economics that says "do what is simple and effective first, and then move on to large-scale, more sophisticated projects". We need to understand that.

It follows therefore that if we take too long establishing a viable banking system, we will no longer have a capital market and the economy will be deprived of the massive investments it requires. This is hardly likely to favour economic growth.

Finally, if we continue to fail to establish a viable banking system capable of carrying out the functions of a banking system in a market economy, then the state will move into the vacuum by raising taxes and increasing expenditure with or without the support of the liberals. The need will be too strong. This will give rise to a simple choice: spend state money on so-called "effective" investment projects, on short-term loans to businesses, or continue to subsidise the non-market sector. The resistance mechanism remains in place and the danger therefore remains also.

The vicious circle has closed. We need to work out how to break it.

### ***Task number two - restoring Russia's international position***

Our second most important task is to restore Russia's position in the world, and to eliminate one major threat in particular: the risk of Russia's isolation from the rest of the world. This risk stems from internal rather than external factors - the xenophobia, chauvinism and imperialist ambitions that are common currency among certain sections of our population.

If we are to resolve this issue, we must learn to perceive our problems in an international context. Russians in general tend towards egocentrism, or national self-obsession, and we often do not realise that we are interested only in ourselves. I noticed at the World Economic Forum in Davos that despite the amazing variety of interesting political, economic, and professional discussions going on, Russians were only to be seen where Russia was the subject of discussion.

While we continue to wallow in our problems, the world is moving on. Indeed, global economic growth has stepped up in recent years.

Twenty years ago the USSR was the second superpower, with an abundance of those former symbols of technological advancement - nuclear and rocket technology. We were assured of markets for our arms and medium-quality equipment by our zone of political and military influence. We aimed for total self-sufficiency, and practically everything we had was our own. Our industrial machine, which was created in the 1930's following the Ford model (narrow specialisation, mass production, economies of scale), rolled along in its rut. The enormous might of the awkward and haughty dinosaur that our country had become nourished our pride and inspired fear in our neighbours. Meanwhile, outside our borders, economic development was measured not in millions of tonnes of steel or thousands of nuclear warheads, but rather in density of telephone networks and numbers of Internet subscribers. If these criteria are applied, we fail.

It is the most difficult thing in the world to part with an illusion of former greatness. The natural reaction is to look for someone to blame, to punch somebody up. However, these types of emotions only prevent us from drawing sober conclusions and creating realistic policies. Thus, the conclusions to be drawn are the following.

1. The dinosaur, as was to be expected, is dead. We wasted colossal resources on "bodybuilding", on developing impressive pectorals, on creating an illusion of strength, and in vain. While we were occupying ourselves with this past-time, other countries were making use of the opportunities provided by the market economy to develop in a real and solid manner. The result is that we now lag behind our neighbours, we lack energy, business initiative, and will. Of course, excessive self-flagellation is not the answer - we are, after all, the tenth largest country in the world in terms of GNP. The Russian Empire in 1913 was in the fifth place. Such is the end result of the communist experiment.<sup>1</sup>

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<sup>1</sup> *Both radical reformers and communists quote Russia's GNP using a market dollar exchange rate in order to demonstrate the appalling state of our economy. This yields a GNP of USD 180-200 billion, and a federal budget of less than USD 20 billion, making the Russian economy smaller than that of New York or the Chinese province of Guandong. In fact, international organisations recommend using a purchasing power parity value to convert GNP figures.*

*The World Bank's World Economic Indicators for 2000 give the following adjusted (in brackets) GNP figures for the world's major economies for 1998:*

USA	- 8002 (7944)	billion dollars
China	- 3846 (4067)	billion dollars
Japan	- 2940 (2887)	billion dollars
India	- 2035 (1510)	billion dollars
Germany	- 1819 (1772)	billion dollars
France	- 1246 (1309)	billion dollars
UK	- 1201 (1220)	billion dollars
Italy	- 1185 (1176)	billion dollars
Brazil	- 1098 (1085)	billion dollars
Russia	- 948 (605)	billion dollars
Mexico	- 738 (847)	billion dollars.
Canada	- 715 (760)	billion dollars
Spain	- 638 (642)	billion dollars
South Korea	- 625 (579)	billion dollars

2. Russia is an extremely large, sparsely-populated, badly-governed country at a medium or lower level of development. Massive investment will be required to develop the country in view of the high cost of transportation, our poor infrastructure, and the disproportions we have inherited. On the other hand, we are failing to participate fully in the processes of globalisation and global economic development. Major flows of capital are passing us by as investors do not find us an attractive investment destination. The Russian market, once so attractive, has actually contracted. It is also characterised by unusual practices that tend to scare away normal business.

Erstwhile one of the centres of a bipolar world, the Russia of today has shifted to the periphery. The issue of increasing Russia's weight within the global economy and encouraging investors to turn their attention to us is not one of prestige. It is a question of prosperity for our citizens, a question of access to modern civilisation, and a question of Russia's very survival and the survival of her unique culture in a changing world.

3. There is only one solution - maximum integration into the global economy. Protectionism, however useful it may seem, is a dead-end that will only lead to further stagnation. We have pulled ourselves out of a slump and placed ourselves on the rails to a market economy and democracy. While this is an enormous achievement for Russia, it still does not guarantee continued progress. It is merely a ticket to take part in the race.

If we are to move to the front of that race, we must learn to be much more adept with our hands and our heads; we must shed our habitual slackness; we must rid ourselves of our "perhaps, probably, somehow" attitude. We must encourage initiative and thrift, we must promote good organisation and orderliness. So far we only export natural resources, the less processed the better, and arms - Kalashnikov rifles, S-300 anti-aircraft systems, MiG and SU fighter/bomber planes. These are the brands by which we are known on the world markets.

We need to find our niche on the market for finished products, be that medium-range aircraft, heavy machinery, power-generation equipment, or software. We need to throw ourselves into the competitive environment, lose, sell ourselves, and lose again if we are to learn how to hold our own against our competitors.

4. The West politely agrees that Russia is a great country, that the crisis will pass, and that we will once again occupy a worthy position within the world order. The euphoria that followed the victory over communism has passed, and we must acknowledge that we made poor use of our honeymoon with the rich nations. For these countries, Russia is passing into the background. Their newspaper reports on Russia refer only to scandal after scandal.

The need for Russia to integrate into the global economy makes friendly relations with the developed world an imperative. There can be no place for superpower ambitions or acts. We must be friendly, but firm, in our affirmation of our national interests. These may be summed up in three points:

To open up our markets, and most importantly, to join the WTO;  
To attract investment;

To totally restructure our foreign debt so that we can create the conditions for concentrating our resources on modernising the economy in the coming decades.

We may have to make a lot of sacrifices to achieve those objectives.

At the same time, the West has a strategic interest in having a strong Russia on its side in the potential conflicts of the twenty-first century - a Russia that can stand on its own two feet, help others to stand on the feet, and carry its fair share of the burden of maintaining the free world. We must take advantage of this strategic interest, right now, from what unfortunately is not a very strong position.

A different type of attitude also exists in the West: keep Russia down, don't let her get back on her feet, or she will eventually become a competitive rival. Compromise with Russia, for example in the area of foreign debt restructuring, only in exchange for political concessions. This is a short-sighted viewpoint and it is the task of our diplomacy to unwearyingly point that out. We must overcome such attitudes, with obstinacy and intransigency if needs be, all the while remaining consistent, predictable and worthy of trust.

The damage done to our national dignity over these past years has undoubtedly been a bitter experience for our citizens. Indeed, it has often coloured our foreign policy. Russia's foreign policy goals often seem to consist of restoring the prestige and might of our country and forcing other countries to respect us, if only for our military might, our rockets and our nuclear warheads; we want to be accepted on equal terms in the rich men's club, despite our shabby, torn trousers. The image of Chancellor Gorchakoff hovers over our diplomacy: just as he tried to maintain Russia's status as a Great Power with worldwide interests during the temporary period of weakness that followed the Crimean War, we also believe that one day we will be able to speak from a position of strength. Chancellor Gorchakoff's ambitions did not come true. Where is the guarantee that ours will?

I do not wish to cast doubt over the fundamentals of our foreign policy. I am, however, convinced that we must make our economy the primary subject of our foreign policy. We must aim to overcome this crisis by integrating with the global economy and neutralising the threat of international isolation. And without making an inordinate fuss about it.

### ***Who is for what? The new configuration of forces and interests***

This is the objective situation. But the above description is by far incomplete and does not cover many factors that can cause social and political tension.

On what forces can the president rely in carrying out his mission? Who will support what, and who will make alliances against whom?

The distribution of forces described earlier in this article is the result of the Yeltsin era, a rather stable social structure of the post-Soviet Russia. However, from Putin's initial determined steps it is becoming clear that there will be major changes in the political order under his presidency.

The situation at present is so favourable from the government's standpoint that it feels there are no forces it cannot take on. The government's mandate of trust and high popularity ratings allow it to act decisively without worrying about lobby interests. This state of affairs will not, however, continue indefinitely. As soon as oil prices fall or the government attempts to embark upon some

unpopular economic restructuring measures, that trust will melt away. In that case the government may very well find itself needing the support of various elite groups or socio-political forces.

It would appear that the outcome of the parliamentary and presidential elections has been favourable to the new nomenklatura, and especially to those sections thereof that enjoyed favour under Yeltsin. Indeed, it was with that goal in mind that they undertook "Operation Putin": to ensure that the government remained on the same track and, most importantly, to retain their positions. It was the new nomenklatura that scuppered Yevgeny Primakov's chances of a victory, as he would have altered the course of government and other sections of the new nomenklatura would have come into favour.

However, Putin spoke out in favour of liberal economic reform during the election campaign. One of his first acts as president was to walk on the interests of the regional elites and major business, and at the same time to attack the media. These are the forces that make up the new nomenklatura, including groups that support or are loyal to Putin.

So, what is happening? Could it be that Putin's liberal economic pronouncements are indicative of a shift in the priorities towards creating a free market economy, a middle class, and equal competition, with the liquidation of the "in-pocket business" which is equal to the liquidation of oligarchs? Or are the populist slogans, walkabouts, and attacks on the rich intended to attract the support of the dispossessed? Or could it be merely a routine shuffle in the ruling coalition of bureaucracy and business, with new actors taking on existing roles in old plays? That would be confirmation of the forecast made earlier in this article concerning the major conflict to take place in the coming stage of Russia's evolution: between oligarch capitalism/new nomenklatura on the one hand, and the free market economy/middle class on the other. Or is what is happening quite simply a vulgar assertion of personal power?

I think that this uncertainty is all part of Putin's current policy, despite the contradictions. He is keeping his options open.

His options and how they he will act upon them depend primarily on Vladimir Putin himself.

Will he opt for his mission, or for power for the sake of power?

Of course it is to a certain extent true that one needs power in order to fulfil a mission. However, we are now approaching that dangerous area where the end begins to justify the means.

The choices the president makes will determine where his support will come from and the attitude towards him of the country's strongest socio-political forces. Putin's political choices may be described in terms of the two points of his program:

A strong state;  
Liberal economic reform.

The issue of a strong state is a sore point, as it can be understood in two different ways:

- A strong state in which all are equal before the law;
- Or a strong state in which the authorities manipulate the law to protect state interests. There exists in Russia a vertical power structure in which instructions from above carry greater weight than the law.

Although Vladimir Putin has announced a liberal economic policy, we are nevertheless obliged to consider the possibility of increased state interference in the economy given the vested interests of his potential support bases and their attitude towards Putin and possible swings in his policies.

Furthermore, the effectiveness of his liberal economic policies will depend on how serious he is about restructuring the non-market sector, stifling the shadow economy, and strengthening the banking system.

Figure 3 illustrates the political options facing Vladimir Putin at this moment in time.

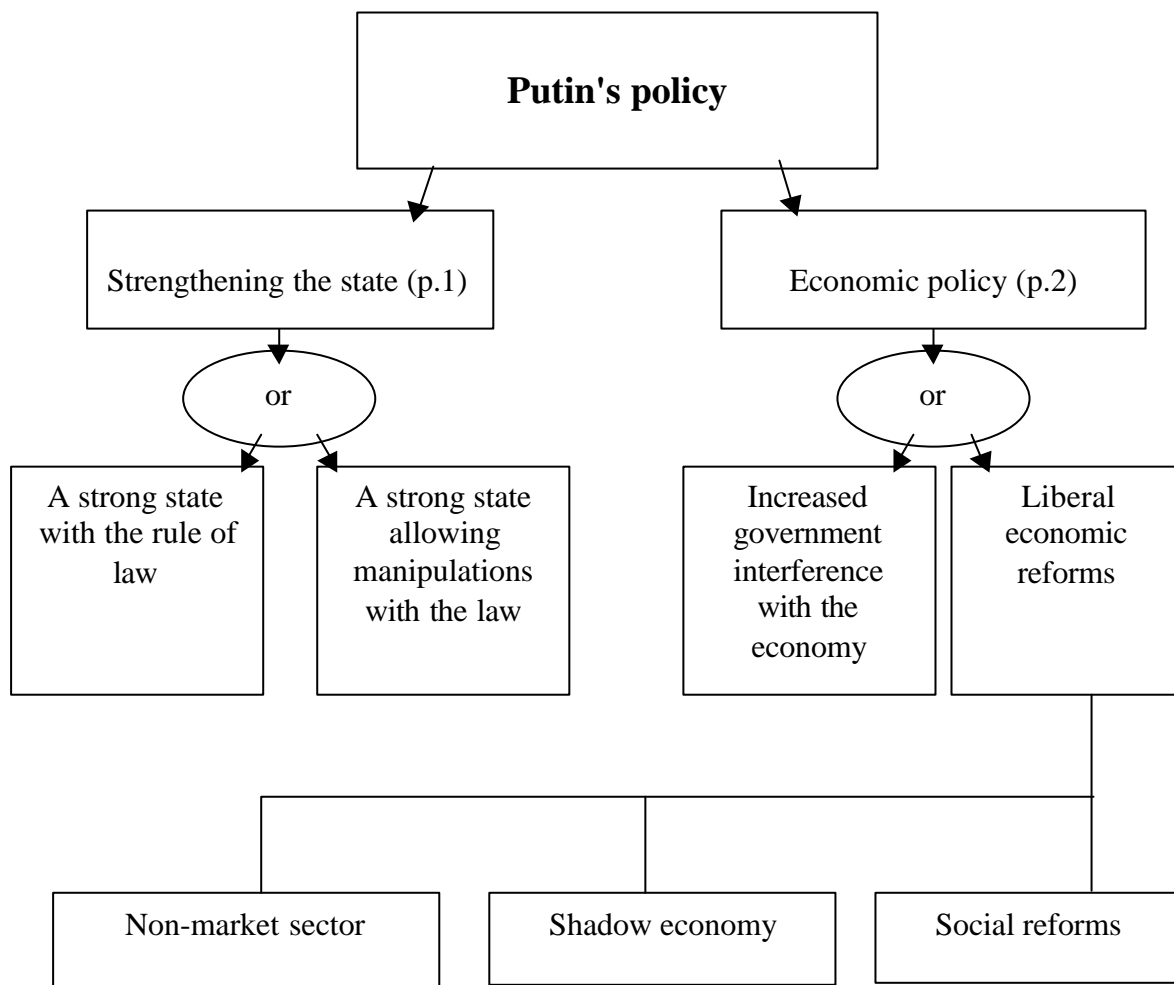


Figure 3. Vladimir Putin's political options.

It is against the background of the political choices illustrated above that post-communist Russia's socio-political forces will emerge, seeking to influence the president, to exert pressure on his policy decisions.

It is important to note that the forces in question are not homogenous.

The rightist-liberal forces may be divided into two camps: the "reformers" and the "upholders of rights". The reformers see liberal economic reform as the most important issue on hand, and are willing to co-operate with a government that is prepared to carry such reforms through, even if it means closing their eyes to certain excesses, violations of civil rights, etc. Gennady Seleznev said that the Gref program is a direct follow-on from the Gaidar program. He

was right. Similarly, the reformers' support for Putin will be merely a follow-on from their support for Yeltsin and will be inspired by the hope that Putin will actually carry out the reforms in question. Their basic tenet is that democracy will be deprived of its socio-economic basis if liberal market reforms are not carried through. The business community, traditionally a natural well-spring of support for rightist political movements, is more or less in the reformers' camp. The reformers can be further subdivided into two camps - the moderates and the radicals. The radicals hold the opinion that the model adopted by Pinochet, the "father of liberal economic reform", could also be applied to Russia.

The upholders of rights see rights and human freedoms as the most important issue. They are unwilling to tolerate human rights abuses and believe that an effective market economy should be founded on civil freedom.

The differences should not be exaggerated, however. Any serious abuses of human rights and democratic norms or failure to implement reform measures will unite the rightist liberal forces, with the exception of those who, in view of their government positions, opt for the quieter pastures of a place within the new nomenklatura.

Thus, business, the middle class, and the rightist-liberal forces will support a strengthening of the state within the parameters of the law, and will speak out categorically against any form of arbitrary abuse of authority by the state. They are especially likely to voice opposition to the KGB tactics for which the law enforcement authorities currently seem to have a propensity. They are against state interference in the economy and for the continuation of liberal reform and for social reform. On the other hand, the moderate reformers and upholders of rights in particular are for moderation in the liquidation of the non-market and shadow economy.

It is important to note that much of the middle class, including most of Russian business, exists in today's Russia thanks to the shadow economy. Given the authorities' propensity for heavy-handed actions, any sudden movements in the fight against illegal business will be met with caution, if not downright hostility. The rightist forces will have to contend with that fact: the "clean sheet" slogan (amnesty on illegal activities carried out during the years of runaway capitalism) will sooner or later become part of the right's political agenda.

The new nomenklatura emerged to occupy positions of power during the Yeltsin era and for that reason it is likely to resist change. At the same time, however, it is extremely heterogeneous and does not have a single unifying ideology. Its primary objective is to subjugate the authorities and to usurp their powers.

The new nomenklatura may be divided up schematically as follows.

The federalists - the federal bureaucracy and power structures. This section of the new nomenklatura is clearly in support of the idea of strengthening the state, and it has no qualms about the methods used. They see democracy, human rights, and the rule of law as mollicoddling: an obstacle to decisive action and success. This attitude finds an echo among ordinary people: "Don't stand on ceremony with us", as a citizen from the village of Putino in the Bryansk Region wrote to the president.

The power structures are playing a particular game all of their own: they believe that their time has come. This is giving rise to strong nationalist and imperial feeling and to negative attitudes to reform and private business. General Shamanov expressed those feelings well when he said that he wanted to help the president restore the order that was destroyed in 1985.

Subordination and personal dedication are what the federalists value. Hence, the attitude that "although we do not particularly like your liberal reforms, we will go along with them to the best of our ability as you're the boss".

The federalists see the shadow economy and corruption as the symptoms of the destruction of a state. They are hostile in equal measures to illegal business and to legitimate business, which they see as the source of the disease. Notwithstanding, the ranks of the federalists include many people who are themselves mixed up in shady dealings, who have converged with business interests, and who act on behalf of various lobby groups. The goal of the latter is to place their own people in prominent positions of power. This significantly complicates the relationships.

The regionalists - the regional elites and local administrations. This group is basically in the same camp as the federalists, but with the distinction that they support regional devolution and stronger powers for regional leaders. They are also for order at any price, with the proviso that they get to decide on how that order is administered. They are wary of any movements towards strengthening the federal centre, and this may prompt them to become supporters of the rule of law.

The strength of their opposition should not, however, be exaggerated. The centralised state has not yet passed into history, and even during the tsarist era they were able to have their way as long as they maintained their positions of power. Few regionalists can be said to be proponents of liberal economic reforms and the suppression of the non-market and shadow economy. On the contrary: given that they will have to deal with the negative consequences of such policies, they are more likely to offer resistance.

The oligarchs - the embodiment of the convergence of business interests and the authorities, including the regional administrations. The oligarchs built up their wealth through shady dealings with budgetary funds, and now they are worried about their futures. The oligarchs are prepared to carry on as before, especially if it will prove profitable for them. They are also prepared to join the ranks of legitimate business as long as no-one looks too closely at the origins of their wealth. Corporate Russia is more than willing to dance to the tune called by the state and to buy its way out of trouble: it is well aware of the state's capacity to destroy any business it chooses. The threat of pressure or a redistribution in favour of bureaucrats may force the oligarchs to present a united front.

If corporate Russia is separated from the authorities it is likely to lend its support to the reforms process and the rule of law, despite the fact that hitherto it has failed to support either fairer competition or the suppression of subsidies and exemptions. Corruption has been the instrument with which it has built its influence over the state. The situation will only change if the oligarchs are forced to pay taxes instead of bribes.

Thus, the new nomenklatura is inherently contradictory as a socio-political group. The federalists, and in particular those in the power ministries, are hostile towards the oligarchs and the regionalists. Hence the fact that Vladimir Putin's first measures as president, clearly supported by the federalists, were directed against the other two groups. The feelings are mutual to the extent that the vested interests of the groups diverge.

There is scope for conflict within the new nomenklatura. However it is likely to become serious cause for concern only in the event that the authorities become seriously weakened.

The old nomenklatura, having lost its former position, is likely to be willing to co-operate with the authorities, right up to merging with the new nomenklatura. However, given its social base

and its mentality, it will be forced to oppose the authorities to one degree or another. It is even likely that it will stand up in favour of democracy and human rights if its interests are threatened.

The old nomenklatura is strongly committed to opposing liberal reforms and the liquidation of the non-market sector. It is for state protectionist policies and an enhanced role for the state in the economy. It is also a well-spring of imperialist sentiment. The old nomenklatura is in many respects similar to the federalists.

Table 2 illustrates the attitudes of the groups described above to the main components of Vladimir Putin's policies.

Table 2

**The attitudes of the main socio-political groups to the president's policies**

Major social & political forces	Strengthening the state		Economic policy				
	Rule of law (real democracy)	Law is manipulated by authorities (controlled democracy)	Increased government regulation	Liberal reform	Liquidation of the non-market sector	Liquidation of shadow economy	Social reform
Middle class, legitimate business, liberals, democrats	Yes	Now	Now	Yes	Yes, but cautiously	Yes, but cautiously	Yes
New nomenklatura:							
- federalists	Rather no, insufficiently	Yes	Yes	No	Rather no	Rather yes	Rather no
- regionalists	Rather no	Yes, if for us, no, if against us	Yes	No	No	No	No
- oligarchs	Rather yes	Rather yes, if for us, no, if against us					
Old nomenklatura	Rather yes, easier than opposition	Yes	Yes	No	No	Rather yes	No

The conclusions to be drawn are as follows: If Putin is intent on carrying out his mission, then his only true support base will be the rightist liberals. However, he cannot rely on these alone, as their electoral base remains limited: they are still blamed for the crisis. It is therefore imperative for Russia's political stability that Putin create a wider, more ideologically diverse coalition that should appear both moderate and centrist. This means that he will have to compromise on his mission, for otherwise no coalition will be possible, even if now his popular mandate allows him to act as he pleases.

If Putin attempts to rein in the bureaucracy, it is likely that the bureaucracy will react by slowing up the implementation of his mission. The new nomenklatura will offer a weak support to the Putin program, and in fact is more likely to offer active resistance.

There is an important conclusion to be drawn here: the Putin victory has made the continuation of the alliance between the liberal reformers and the new nomenklatura possible. If Primakov had won, that would not have been possible. The liberals would have gone into opposition and a definitive line would have been drawn under the reform process.

If however Putin decides to concentrate on accumulating power rather than on his mission, and if he elects to strengthen the state using traditional methods, then he can rely on the support of both the old and new nomenklatura. Moves such as these would also give a boost to his electoral base and force liberals and rightists into opposition. The difference between a Putin and a Primakov as president will thus be negligible.

The authorities now enjoy enough popular support, support that extends even to the reform program, to use force and flex its muscles without having to worry about resistance, on the basis that "the most important thing is for us to achieve our goal by the most effective means possible". Even today, however, with the state of affairs favouring the government, there is creeping doubt as to the correctness of such reasoning.

If the situation deteriorates, Vladimir Putin will be forced into making a choice between his mission on the one hand and power on the other: either uphold the spirit of democratic law and restraint in policy implementation and securing authority, or else opt for the forceful approach by abusing administrative powers and changing policies in order to hang onto power. The rightists will be the only ones to offer any opposition. There is concern here as to whether in such a scenario the structures will still exist that put them in a position to offer political opposition and to possibly carry the victory in democratic elections.

### **3. The Third Basket**

#### ***Is there anything worth fighting for?***

The twenty-fifth anniversary of the signing of the Final Act of the Helsinki Conference on Security and Co-operation in Europe (the Helsinki Accords) was marked recently. The Helsinki Accords were a triumph for Leonid Brezhnev: he managed to obtain international recognition of the inviolability of the post-war international frontiers. Temporary inviolability, as it later turned out. The Final Act included a so-called "Third Basket" whereby the participating countries undertook to protect human rights and fundamental freedoms. This meant that governments could no longer claim human rights to be a domestic matter. Soviet dissidents used the third basket to exert international pressure on the Soviet leadership to comply with the Soviet constitution and respect civil rights and freedoms. While they were of course unable to force the Soviet government to do anything, they did contribute to the downfall of the totalitarian regime.

A conference dedicated to the twenty-fifth anniversary of the Helsinki Accords took place in Moscow on July 28-29, 2000. Neither the government nor the presidential administration was represented. Side-by-side in the conference hall sat human rights activists and the diplomats who worked on the third basket - Dubinin, Kashlev, *et al.* I fear that the significance of the event was appreciated by its participants only, especially given that the third basket is back on the agenda again.

Events are currently developing in Russia in the manner that is to be expected: a period of revolutionary transformation followed by economic stabilisation. Society is reacting to the weakness of the state, weakness that is unavoidable in a time of upheaval and shifting state order. Society is calling for order and effective state institutions. This is an objective necessity.

There is however a hidden threat. We are at a cross-roads once again: will Russia opt for bureaucratic rule with a vertical power structure from the top down? Or will Russia opt once again for "modernisation from above" that in the past has always led to new upheaval? Or indeed will we manage to stick to the path of democratisation and civil society and construct a more flexible and dynamic social system that will be capable of meeting the need for globalisation? Whatever spin is put on the results of the past ten years, the fact remains that they brought the country from a state of complete abjection to a certain, albeit unstable, equilibrium from which Russia is physically capable of moving in the direction of a free, democratic open society. It is a unique opportunity!

The danger is that our inherent inertia and traditional institutions with their massive support bases will push us back to where we were ten years ago. There is also the danger that the new rulers, instead of becoming a major driving force in this area, will also give impetus to a move back towards the past. This danger is just as strong as any of the previously discussed.

Is there anything worth fighting for? It is almost universally believed that Russia is an undemocratic country without a civil society, that the rule of law holds no sway in Russia, and that Russia's unreasonable and thievish subjects need the firm guiding hand of a strong state. A strong state first and foremost, and if democracy obstructs that, then let democracy wait. This idea is supported by the arguments of the radical reformers: first an economic basis for democracy should be created, otherwise democracy will hinder the construction of a liberal economy.

A French colleague has recently asked me whether I really believed that freedom and democracy are conducive to economic prosperity. I want to believe that they are, but I would like to see evidence. Taiwan, Singapore and Korea are definitely not models of democracy, after all. Then there is China - the bane of all democrats - with its communist-organised boom. Democracy after or before reforms - this is in many ways a question of personal opinion and *Weltanschauung*.

In my opinion there is no clear answer. My opinion with regard to the Russia of today is as follows. Firstly, I am convinced that democracy exists in Russia, or at least if one judges on the basis of the minimum formal parameters that determine a democracy. Democracy exists and is valued in Russia. Russia's democracy is not yet complete. It has no strong foundations in the economy or in institutions of civil society, and there is only one way to cultivate it: by consistently upholding civil rights and fundamental freedoms, by applying democratic rules and procedures, and by constantly improving those rules and procedures as we use them. If we do that we will only have to mow the lawn from time to time instead of constantly ploughing it up. The incomplete nature of Russia's democracy and the fact that democracy can be an impediment in many practical situations makes our leaders particularly prone to ploughing up the lawn. Sometimes they do it to resolve strategic issues, and sometimes just to hold onto power, and one can always put a strategic slant onto the issue of holding onto power.

Great is the temptation in a Russia which until recently had absolutely no experience of democracy to say: we'll just bend the rules of democracy one more time, to get this particular task out of the way, and then we'll be good democrats forever more.

Secondly, Russia has always been behind in terms of standards of living, and has always envied her neighbours to the west. We have tried, time and time again, to overcome our complexes: to "catch up with and overtake" our neighbours by modernising from above. And it is not just our ancient way of life or the boyars' beards that we have sacrificed; we have sacrificed thousands, millions of human lives. And to what avail? The answer is slavery, robbery, disregard for human dignity, excess, and violence.

Other countries have already demonstrated that prosperity based on mutual trust and respect, and not imposed from above, is only possible if human rights and fundamental freedoms are acknowledged by all, and if the rules of democracy are observed by all. If that happens, the weeds that are currently strangling the fruits of our people's work and labour will die out, will no longer destroy people's lives. I repeat - this is a unique opportunity for Russia. And it lies in the "third basket".

### ***Recent history: reforms or democracy - the first choice***

Let us look back on the recent history of democracy in Russia.

During the first phase - 1989-1993 - Russia's democracy was spontaneous, chaotic, and unbridled. The elections brought results that the authorities were not expecting: a breath of fresh air following decades living in "the zone", and major conflict that threatened the destruction of the state. The first phase ended with the "attack on the parliament" and the adoption of the Yeltsin constitution.

Many democrats condemned the events of 1993. In my opinion they represented the unavoidable resolution of a constitutional crisis that arose as a result of the multitude of amendments that were made to the Soviet constitution without removing the articles that conferred all power to the Soviet. Thus, the constitution gave the parliament jurisdiction over all issues of domestic and foreign policy, up to and including the right to strip a democratically-elected president of his powers. The president wanted to carry out reforms that the parliament opposed. This was the first time we faced the choice between democracy and reforms. The choice of democracy - or actually the democratic procedures inherited from the Soviet past - would have been ruinous both for reforms and for democracy itself. Boris Yeltsin made the right choice - that is now clear. October 1993 was Boris Yeltsin's great service to Russia: he simply drew a line under the revolutionary chaos. The end of Soviet power had to come and it did.

Some say that Yeltsin acted as he did in order to hang onto his personal power. That may very well be true. However that takes nothing away from the objective result of what he did. The outcome of the crisis was political stability at no cost to freedom and democracy. That was very quickly demonstrated by the success of Vladimir Zhirinovskiy in the elections of December 1993 and of Gennady Zyuganov in December 1995: the results of those democratic elections reflected the will of the people, whether those in power liked it or not.

That was the last time we used force to adjust our democracy. Let it be the last. The reformers have already used up their one chance to put reforms before democracy. A continuation in that vein would signal a return to the type of arbitrary rule that, as we know from our own experience, bodes nothing good.

Following the 1993 events, the political process entered a more tranquil period. The conflict between the executive and the legislature was fought out within constitutional boundaries, despite a number of tense moments from time to time. The difficulties posed by the situation for the president and the executive gave rise to a number of attempts to manipulate the political process.

The pre-1995 election attempt to set up a bipartisan system led by Chernomyrdin and Rybkin represents a case in point. Another case in point was the rapid succession of appointments to the office of Prosecutor General, an institution that the authorities expected would co-operate in the fulfilment of political agendas. Such was the case of A.I. Kazannik, whose primary allegiance was to the law rather than to the president.

### ***The second choice: coup d'etat or controlled democracy***

Nineteen ninety-six, the year of the second temptation, was in many ways a decisive year for Russian democracy. Once again we faced a choice: coup d'etat, or democratic procedure, albeit with non-standard electoral practices. We were faced with the possibility of a restoration of communist power, and we now know that a coup d'etat was not just a theoretical possibility. We came close to carrying one out.

If that had happened, we could have said farewell to Russian democracy. A second breach of the constitution by the government that had written it would have sent out a clear signal to the people that arbitrary rule is here to stay.

Luckily we opted for the second choice. Vladimir Gusinsky, one of the so-called "seven bankers" of 1996 who undertook to secure the presidency for Yeltsin by peaceful means, recently confessed that that was the beginning of "controlled democracy" - the use of questionable practices in election campaigns and domestic policy - and regretted having been a contributor. His repentance only came when the authorities began to apply the methods he invented to himself.

He should not have regretted what he did. Firstly because it offered an alternative to a coup d'etat and a communist victory. Here I agree with V. Tretyakov: controlled democracy is better than these two eventualities.

Secondly, because the oligarchs have an exaggerated image of their own role in the Yeltsin victory. While they were the ones to be rewarded for the Yeltsin victory, I believe that first prize should have gone to Gennady Zyuganov: the communist victory in the parliamentary elections scared a lot of people besides the oligarchs - nobody wanted a return to the past. People voted the Communist Party into parliament as a protest against the government in the full knowledge that the parliament was hamstrung. To hand them the reins of power, however that was another matter. I do not believe that Zyuganov would have won even if the oligarchs had not supported Yeltsin.

In any way, we avoided a coup d'etat, which would have been far more dangerous than the current generation of communists in power. This fact also strengthened our democracy.

What Vladimir Gusinsky should regret is the full-scale smear campaign he carried out with Boris Berezovsky against Anatoly Chubais and Boris Nemtsov out of petty self-interest. That showed that their media empires were not just businesses or instruments of free speech, but rather powerful political weapons that they used to pressure the authorities into carrying out measures in their favour. The techniques used there were much more malicious than any Xerox boxes of cash. We must not now forget that.

### ***Controlled or real democracy***

The next 1999 elections put the ruling clique - "the Family" and their retinue - in danger of losing power. The main enemy this time was not the Communist Party, but rather the OVR in the persons of Yevgeny Primakov and Yury Luzhkov. They posed a threat not only to "the Family", but also to the political course that Yeltsin wanted to maintain. Regardless of whether that course was reformist or democratic in nature, many were worried at the prospects of the turnaround or "correction of errors" that Primakov and Luzhkov would initiate, especially in the light of their political views and the practices of the Moscow government. This was a conflict of a different scale: less dangerous for society as a whole, but nevertheless a conflict.

"The Family" therefore set itself the task of overcoming what seemed a no-win situation, to ensure the victory of forces that would at the very least guarantee its safety and continued influence. This was no coup d'etat: Yeltsin's health precluded a third term, even if the laws could have been bent in his favour.

The only option open was to make use of the controlled democracy tactics that had already been tried out, albeit in much more threatening circumstances. The result was an outstanding victory that was guaranteed by Putin's decisive actions in Chechnya, the organisation of the Putin-led Unity movement, stricter control over financial flows and sackings that that entailed, unbridled use of the "administrative lever", including the gubernatorial lever, and the rallying of the media for propaganda purposes. Neither Media-Most, nor the Luzhkov-controlled media were willing to cooperate, so the authorities decided to teach them a lesson after the elections. So while Dorenko was unmasking Luzhkov, subliminal television images of a bloody surgical operation on a hip joint were used to persuade viewers that they should not vote for Primakov.

Directly after the parliamentary elections the most important thing for Putin was to avoid the election of Primakov as Speaker. The pro-Putin Unity movement therefore made an alliance with the communists, giving them the post of Speaker and control over a range of important Duma committees. Boris Berezovsky of course was constantly stressing that there was nothing shameful or disgraceful about that: this is politics, not some kindergarten or human rights thing; this is a game between grown-up men in which the stakes are money and power.

To be quite honest, at that time I was more afraid of Primakov and Luzhkov/Maslyukov: their victory would have meant a victory for the new and old nomenklatura combined.

I was happy when Vladimir Putin won. I reasoned that if it had not been for the underhanded methods applied to the elections, the election would have been won by those who I have reason to fear. Does this mean that those methods were justified? That the intelligentsia's whining about fair play is simply the whining of the vanquished, of those who failed? In actual fact, given the advantages he enjoyed over his rivals, Putin had no need to resort to underhanded techniques, and the style adopted by the media that supported him actually came to resemble that of a desperate outsider's megaphone.

Following the elections, the victors were faced with a dilemma: the methods used to win the elections worked, so why not continue using them in day-to-day politics? After all, the tasks of day-to-day politics are no less difficult, especially as far as the economy is concerned, than winning an election. How to deal with stubborn regional governors, a mercenary business community, and an independent media? Judging by events, the decision was made to continue using the those methods. Controlled democracy has become the norm and a strengthened state has become its objective.

Once again, what do we mean by "controlled democracy"? What exactly is bad about it? After all, the British and American bipartisan systems also make for moribund political procedures that prevent the resolution of important issues by simple majority voting. Elections are accompanied by dazzling roadshows, that impede spontaneity and aim to "sell" the candidates as expensively as possible. The track record of parliamentary systems with a great variety of similar parties and constantly changing cabinets has been consistently dismal wherever it has occurred.

On the other side of the coin, presidents in the United States are impeached if they contravene the law, and freedom of speech and information is guaranteed and fulfils its social function, despite the stranglehold of the media magnates. The American political parties are not recent presidential creations: they have evolved naturally over time. One can criticise democracy as much as one likes and point out that it allows the manipulation of public opinion and brainwashing,

but one has to agree with Winston Churchill, who said that although it is a bad system, there is none that is better. Churchill's point of view has been borne out time and time again. Any attempt to criticise real democracy should be interpreted as an attempt to dupe us, to confiscate our rights and freedoms to yet another supreme authority all the while telling us how good it will be for everyone.

The essence of controlled democracy in Russia is that the appearance of democracy is maintained while all important decisions are made behind closed doors. We have underhanded games in the corridors of power instead of open political discussion. Most importantly, the authorities immediately silence any attempt by the opposition to bring political discussion into an open arena. The people, the politicians, and the civil service all know the rules of the game and the penalties for breaking them; they know the futility of trying to secure change.

The Soviet era was a perfect example of controlled democracy. At that time it was called "socialist democracy". It has already been re-established in certain regions by governors and regional presidents who are ostensibly proponents of democracy and the free market. The danger now is that their practices will be adopted by the federal centre. If that happens, the president of the day will call the shots in our political party system

And the media will write what the president dictates, just as at the moment the regional leaders call the shots in that regard. Anybody who looks to the Nazdratenko/*Arsenyevskie Vesti* episode for comfort is fooling themselves. That episode is merely proof that Nazdratenko is trying to install controlled democracy in the Primorye region, and that he has not yet quite succeeded. Other regional leaders unfortunately have, and without creating a noise.

V. Tretyakov is constantly expounding the opinion that for Russia, controlled democracy is a step forward, that whatever else can be said about it, it is still democracy and that we should accept it because we need the strong state that unbridled democracy prevents us from having.

The fact is that it is not a step forward. Granted, in 1993 the chaotic development of democracy was threatening to undermine itself and to put an end to market reforms, and in 1996, controlled democracy was a remedy against a possible coup d'etat. The situation calmed down, and the law once again took precedence.

Nothing today prevents the government from developing real democracy. Controlled democracy will not lead to a strong state. On the contrary, in the best-case scenario it will increase the power of certain personalities and institutions, to the detriment rather than the benefit of the state and society. We must stop using dirty tactics in politics; we must stop using the Prosecutor General and the tax police for political ends. It may be easy for the state to act in this way, and it may make people afraid of it, but in no way does it make for a relationship of trust between the state and its citizens. This is why no-one expects the Prosecutor General to act even-handedly and why it is always seen as the political tool of a higher authority even when that is not the case at all. The real danger today lies here: "controlled democracy" is but another *cul de sac*; real democracy, at the end of the day, is simply more profitable.

### ***Freedom of speech***

Freedom of speech is a fundamental issue for all countries, and especially for Russia. The authorities appear to recognise that. From time to time however there occur events that make one doubt the reliability of the government's pronouncements on the issue and the correctness of one's own understanding of the nature of that freedom.

The Andrei Babitsky affair was one of the first signals. The explanations to the effect that he had been in contact with terrorists and was promoting their standpoint can only be convincing for those who believe in free speech for one's own side only. However it may displease the authorities, the public has a vested interest in having the views of both sides. I do not agree with Babitsky's views, but I do think it important that he should be able to write what he feels necessary and to gather information wherever possible. The Babitsky episode was stopped short under pressure from the West.

Then there is the Media-Most/Gusinsky saga that is still continuing, the attempts to wrest control over ORT from Boris Berezovsky, and the removal of Dorenko's program from the schedule.

To be honest, I cannot understand the motivation behind the ongoing attempts to destroy Gusinsky. So what if he refused to be commandeered for the presidential election campaign? So what if his news reports on Chechnya strayed from the official government line? All that is but an innocuous demonstration of freedom of speech that can only be beneficial for a democratic government. Nobody had even noticed Gusinsky: we were used to it. So what's going on?

It is said that politics has nothing to do with the Gusinsky affair, that it all has to do with Most's risky financial policies and the debts it accumulated and now cannot repay. I am not convinced. Companies in full expansion often have major debts. Gazprom is one that springs to mind. If the business is profitable, then debts are restructured, new loans are taken out, and the business grows.

So, are Most's creditors suffering from intransigence? Why? And if they do decide to make concessions, then it will be clear that the orders have come from above, that the puppeteers have decided they have gone too far: it will smack of political machinations.

Democratic opinion in Russia is divided on this issue. One body of opinion, one that is convenient for the government, holds that attacks on Gusinsky and Berezovsky should not be interpreted as attacks on freedom of speech. After all, no-one likes what they did three years ago; everybody sees that it was political blackmail: "if you don't guarantee our borrowings, then we'll criticise you".

Plus there is the fact that the government is carrying out a policy of separation of business and state, and we democrats were the first to ask for that. It just so happens that the media magnates were the first to go; and they *were* followed by Norilsk Nickel, UES Russia, Lukoil, TNK, Avtovaz, and even Sibneft, although in the case of Sibneft malicious rumour has it that it was at the behest of Roman Abramovich himself.

The government enjoys widespread support in this area of policy: it has long been time to take on the arrogant oligarchs. Only one thing gives reason for doubt: why are the prosecutors and the tax police acting as though under orders, instead of acting on the basis of evidence.

The persecution of corporate Russia suddenly ended after its representatives met with the president who told them it was unseemly for them to flaunt their wealth in a poor country and that the good old days were over. In a recent interview with *Le Figaro*, Putin spoke in his characteristic emotional and determined style of the cudgel that the state has already laid its hands on but not yet used, and that it will be used if angered. So what is that supposed to mean?

The interesting thing is that despite the fact that the government has ceased all offensive actions against corporate Russia, it is still trying to gain control of the media.

This leads to another conclusion: that the state has its own understanding of the concept of freedom of speech that is different from the generally-accepted one. It is not a question of the financial difficulties of the independent television stations. One can even ignore the fact that the government is adopting a doctrine of information security at a time when, from the point of view of society, there is no need for it whatsoever; a doctrine which in addition to the usual passages on freedom of speech and press freedom contains suspicious passages that boil down to imminent amendments to one of Russia's most democratic laws - the Law on Printed Media.

However one cannot ignore the fact that senior public servants have recently acquired a propensity towards accusing the media, or rather parts of the media, of all manner of malicious actions aimed at discrediting the authorities and ascribing to them non-existent sins. Their attitude basically is that "our enemy, the journalist, never sleeps".

Nor should one ignore the fact that the now obedient ORT is no longer being pursued to the same extent by its creditors, and that the Audit Chamber, at the instigation of former communist deputy turned auditor, Yury Voronin, has proposed covering ORT's debts using budget resources. And have you noticed how RTR's style has changed? Or how former NTV anchors Revenko and Mamontov have changed, the first when talking about his former colleagues, the latter as the only newsman allowed to report directly from the *Peter the Great* battleship during the *Kursk* tragedy?

These facts are more or less insignificant if taken in isolation, but when taken as a whole they begin to become worrying: society needs to defend freedom of speech.

It is important to try to understand what is motivating the government to act against the media. I cast my mind back to 1997, when the main TV stations lashed out against senior government figures who then found themselves in no position to defend themselves or explain their positions. It was at this time that the idea was born of creating the All-Russian State Television and Radio Company as a powerful state media holding that would be able to compete with the private channels, even if it had to use the administrative lever.

That idea has now been carried through. ORT is gradually falling under the control of the state. The longer this process continues the clearer it is becoming that state media corporations are not there to save the government from criticism or to provide a channel for official information. State media corporations serve one purpose only: to enable the state to distort information, to restrict access to information, and to restrict freedom of speech if it impedes controlled democracy.

There are now only two remaining independent quasi-federal television stations (NTV and TVTs), and these are keeping a very low profile. They are joined by two or three radio stations and ten or fifteen print publications that are almost all Moscow-based. The public tends to prefer local publications, and these, with rare exceptions, are controlled by the regional authorities.

Research into the geography of freedom of speech in Russia carried out in 1999 by I. Yakovenko showed up only one city providing more or less adequate conditions for access to and production and distribution of information. That was Moscow. On a scale of 1-100, Moscow scored 63.1, and St. Petersburg 50.5. No other region scored anywhere near 50. The champions at the other end of the scale were Bashkortostan with 10 points, and Yakutia with 13.7 points.<sup>1</sup>

Citizens living in the more than one third of Russian regions that scored under 30 are effectively deprived of freedom of speech. Therefore the current federal measures represent a

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<sup>1</sup> *Social Study, The Anatomy of Freedom of Speech, Moscow. 1999.*

turning point - will freedom of speech spread into the provinces, or will controlled democracy spread inwards from the provinces to destroy freedom of speech in the capital.

Competition between rival independent media companies is vital to the creation of a mature market economy and open society. All independent media companies will have their own political preferences and influences that may initially be quite strong. If the state refrains from interfering except in cases where the legislation calls for it (market monopolisation), and if it prevents regional bosses from interfering too, then competition and public opinion soon level out the field. The important thing is not whether or not a media magnate has political influence; the important thing is that there should be more than one media magnate. The problem with our media is not that it is privately-owned, but rather that poverty-stricken viewers, readers and enterprises spend too little on advertising. What is needed is time, not government interference. If it is to avoid interfering in natural social and economic processes, the state must guarantee freedom of speech, including a guarantee of non-interference. There is nothing at this moment in time that is more important in the third basket to civil rights and freedoms than freedom of speech.

I have tried to demonstrate in this article that Vladimir Putin's goals and plans are worthwhile, and that I sincerely support them. But Vladimir Putin is set to face many complex problems in the future that will not always be easily resolved, especially using force. Furthermore, an excess of determination, self-confidence and strength often multiplies problems instead of solving them. And earthly glory is transient.

I especially want to stress that Vladimir Putin's mission includes a third basket: he must guarantee to uphold human rights and freedoms and civil society. If he fails, then his mission will have failed. It is even more important from the historical point of view, as this is the first time that the authorities may be likely to become initiators of freedom. As yet no such initiative has been taken. The most important issue - judicial reform - appears to have been placed on the long finger: civil servants with vested interests have been given the opportunity to demonstrate how difficult and dangerous judicial reform would be.

If the government does not yet fully understand this, and if the president sees criticism on the issue of freedom of speech as a personal attack on him and an attempt to subvert the state, then the process of explaining must continue. Pressure is usually resisted by those who themselves are subject to pressure. If these put away their weapons then who will stand up for human rights?

We must mobilise the institutions of civil society, however weak they may be. This is the responsibility and duty of every rightist.

We must be vigilant. However weak and unfortunate the Russian liberal intelligentsia, however indifferent the majority of our population to democratic values, we must not allow freedom of speech to be held to ransom by those for whom it is an impediment. Otherwise we will once again sadly follow the circle of slavery that is the history of our country. We will once again be able only to look on with envy at the prosperity of our free neighbours.