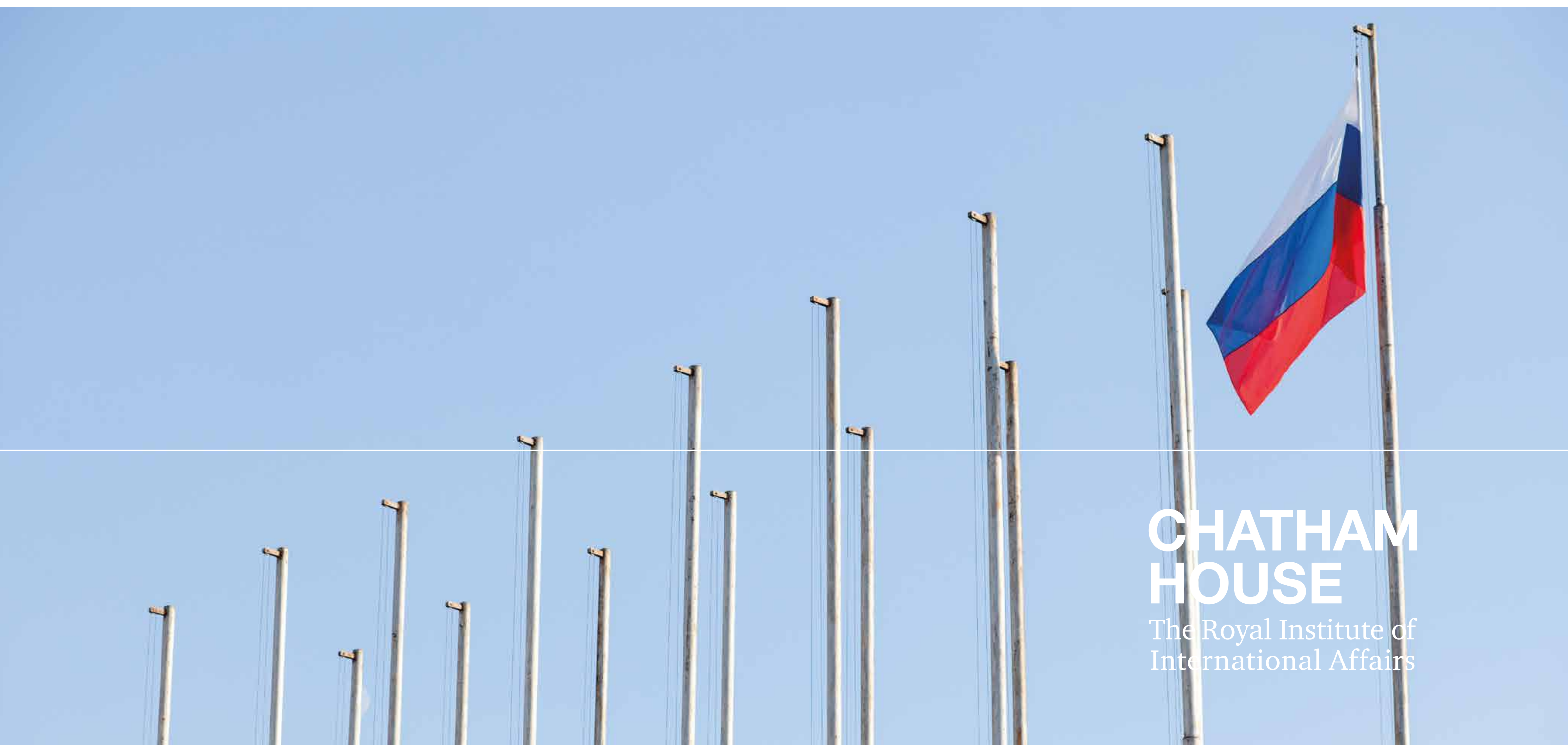
Research Paper

Nigel Gould-Davies
Russia and Eurasia Programme | January 2016

Russia’s Sovereign Globalization
Rise, Fall and Future



Summary

- Two major goals have driven Vladimir Putin's presidency: a controlling state and a prosperous economy. His central dilemma has been to manage the tension between those objectives. He has had to consider how Russia could reap prosperity through globalization while maintaining domestic control and great-power autonomy.

- To achieve that end, Russia evolved a strategy of 'sovereign globalization'. Initially, this involved managing the terms of economic engagement to limit external influence by reducing sovereign debt, circumscribing foreign ownership rights and maximizing the balance of benefits over obligations in global economic governance.

- As Russia's confidence grew, it sought to exert broader political influence by economic means, using its position as the major market of the former Soviet Union and dominant energy supplier to Europe.

- A series of adverse developments undermined that strategy: the decline of energy-export-led growth, global energy market developments and EU responses to Russian policy. Those changes led to a sharp and unfavourable shift in the balance between opportunity and risk in Russia's engagement with the global economy.

- The unravelling of Russia's strategy propelled events in Ukraine and triggered the present crisis in Russia–West relations. As a consequence, Russia's distorted political economy is now under strain; its regional influence is waning; and Western sanctions are depriving it of goods, capital and technology.

- Russia's experiment with 'sovereign globalization' was a highly ambitious attempt to harness interdependence to the pursuit of power-political ends. For the first time, Russia used economic relations – its traditional weakness – as a source of strength. The failure of that strategy encourages pessimism about Russia's prospects but optimism about globalization.

Introduction

> We must learn to use the advantages of the new state of the world economy. It is clear that for Russia the problem of choosing whether or not to integrate into the world economy no longer exists.
>
> – *President Putin, annual address to the Federal Assembly, 2002*[1]

> We must above all understand that our development depends primarily on us. We will only succeed if we work towards our own well-being and prosperity, rather than hope for favourable circumstances or foreign markets.
>
> – *President Putin, annual address to the Federal Assembly, 2014*[2]

The 15th anniversary of Vladimir Putin's rise to the Russian presidency has inspired much reflection on the ways he has changed his country and its place in the world. Most of these changes have been broadly linear. Growth and centralization of state power, pressure on civil society and its institutions, decline in relations with the West – with minor bumps and variations, all these trends have moved in one direction.[3]

Russia's relationship with the global economy has developed quite differently: it has been an arc. In 2000 the Putin presidency began by committing Russia to deeper engagement with the global economy and its governance, a goal actively supported by the West. By 2007, the mid-point of this period, every strand of Russia's relationship with the international economic system had thickened and strengthened significantly: Russia had just chaired the G8 for the first time and was soon to call for 'modernizing alliances' with the West. But today Russia's president speaks of minimizing dependence on the West while, for the first time since the end of the Cold War, the West now seeks to restrict, rather than promote, Russia's integration into the global economy. On no other issue have the outcomes departed so comprehensively from the original intentions of Russia and the West alike.

What explains this remarkable reversal? The answer lies in the working out of a central tension between two fundamental but opposing impulses in the Putin project: to re-establish a strong, centralized and controlling state and to build a prosperous country through integration into the global economy. The first has entailed strong centralized state control over citizens and institutions (in Russian parlance, the *vertikal* of power), while the second has entailed autonomous, *horizontal* flows of goods and money across borders, linking Russia to actors and jurisdictions beyond its formal reach. Much about the evolution of Russia's political economy and of its relationship with the West can be understood through the record of successes, and then failures, of the strategy that Russia developed to manage this tension and of the Western responses it provoked. This strategy can be understood as 'sovereign globalization', a precise functional analogue of the 'sovereign democracy' that Russia has practised internally. Just as sovereign democracy seeks to manage and manipulate domestic political processes to strengthen regime legitimacy and control, so sovereign globalization seeks to manage and manipulate international market processes to extend Russian

[1] See http://archive.kremlin.ru/eng/speeches/2002/04/18/0000_type70029type82912_70662.shtml.
[2] See http://kremlin.ru/events/president/news/47173.
[3] These trends did not all begin at the same moment or take place at the same rate. The decline in relations with the West, in particular, began only after 2003. But the direction of travel of each of them is clear and unmistakable.

influence. In both cases 'sovereign' power coordinates, co-opts and corrupts ostensibly spontaneous activities – and, where necessary, coerces – in order to achieve state-directed political ends.

This is a neglected subject. Few studies of Russia dwell on its experience of globalization, while even fewer studies of globalization dwell on Russia, especially in comparison with the other BRIC countries.[4] In Russia itself, a dominant discourse of 'geopolitics', atavistic and mystical, preoccupies itself with control over territorial space and is often hostile, in principle, to globalization.[5]

But Russia's engagement with globalization is of central importance to understanding the Putin project and its international consequences. It imparts thematic coherence to diverse aspects of Russia's domestic and foreign policy and resolves several paradoxes of Russia's behaviour. It also provides a new frame for understanding the origins of the present crisis in Russian–Western relations as an outcome of shifts in the balance of economic influence between the two sides. This points the way to a political economy of the Ukraine crisis and, ultimately, of the Putin presidency.

These developments have wider significance. They mark the first time that Russia has sought to turn its international economic position – historically, a source of weakness – into a source of strength. They also represent an exceptionally ambitious attempt to harness interdependence to the pursuit of more traditional power-political ends. Russia's experience thus offers important lessons for the future of both the global economy and the country itself. This paper charts the rise and fall of Russia's distinctive approach to globalization and explores the implications both for Russia and for the global economy.

Globalization and Russia: past as prologue

Martin Wolf's definition of globalization is clear and helpful: 'integration of economic activities, across borders, through markets'.[6] Globalization is inherently political: ever since industrialization dramatically increased the benefits of participation in the international economy, states have had to choose how to manage the flows of money, goods, investment and labour across their borders.[7] The choice of policy from among the many available is typically determined by a combination of domestic interests (competition for influence between the winners and losers from greater openness) and leadership ideas about national development. The normal politics of globalization – of both national policy-making and international governance – are shaped primarily by

[4] The two subjects rarely intersect, except in technical analyses of the economic effects of integration (for example, of accession to the World Trade Organization) or the role of energy in Russian foreign policy. Though important, such analyses tell only a small part of the larger story of Russia's engagement with the global economy and its institutions. They are usually detached from their domestic context – from an understanding of how a globalization policy arises from political choices and dilemmas and how it, in turn, produces effects on domestic interests and power. The most important collection of essays on the subject is, in its own words, 'far from being comprehensive' and devotes relatively little attention to the specifically economic aspects that are the focus of this paper. See Douglas W. Blum (ed.), *Russia and Globalization* (Baltimore: The Johns Hopkins University Press, 2008), p. xiii.

[5] More serious Russian scholarly interest in globalization has been periodic rather than sustained. For an overview, see Andrei P. Tsygankov, 'Globalization: A Russian Perspective' in Arlene B. Tickner and David L. Blaney (eds), *Thinking International Relations Differently* (London: Routledge, 2012).

[6] Martin Wolf, *Why Globalization Works* (New Haven: Yale University Press, 2004), p. 14. While this paper does not directly address other transnational flows, such as of information and ideas, which have also influenced Russia's development, it necessarily touches on them. As Russia has always understood, flows of economic value and political values are, in practice, hard to isolate from one another.

[7] Contemporary globalization refers primarily to integration with Western economies, as the most dynamic and successful markets and architects of the major global institutions. This, of course, is changing with the continuing rise of 'the rest'.

cooperation, bargaining and conflict between economic interests within and across states over how wealth is created and distributed by international market activity.[8]

As the least developed of the major powers, Russia has engaged with globalization in a distinct and more fundamentally political way. Its relative economic weakness means Russia has stood to gain disproportionately from access to Western capital, goods and technology. But disproportionate gains entail disproportionate vulnerability: Russia has long feared the emergence of an exploitable dependence on economic partners that might also be political rivals. Thus, historically Russia's politics of globalization have been driven not primarily by the normal politics of competition among domestic interests[9] but by more acute tensions between modernization and security. These tensions sharpened during the 19th century as the economic gap between industrializing Europe and stagnant Russia grew. Defeat in the Crimean War (1853–56) starkly demonstrated the dangers of relative decline, prompting a search for ways to drive modernization through deeper integration with more developed Western economies while avoiding a politically dangerous dependence on them.

Successive Russian regimes managed this dilemma in different ways. Late tsarist reformers accepted an uneasy reliance on trade surpluses, foreign finance and investment as the price of rapid development.[10] Under Stalin, the Soviet Union took a starkly contrary course, eschewing ties with capitalism and mobilizing purely domestic resources for autarkic crash-industrialization at enormous human cost. In a third pattern, the Brezhnev regime tolerated significant dependence on the capitalist world – chiefly via oil exports, grain imports and foreign loans – as the price of propping up a failing model of state socialism.[11]

The collapse of oil prices in the late 1980s laid bare the unsustainability of this model, triggering a solvency crisis and accelerating systemic decline, which Gorbachev's limited economic reforms could not halt. As post-Soviet Russia embarked on market transition in the early 1990s, it addressed, for the first time, the problem of its relative economic weakness in orthodox terms through rapid international integration and domestic adjustment, free from adversarial impulses of security or ideology. The post-Cold War absence of enemies dissipated the fear of dependence-as-vulnerability, allowing Russia to integrate more fully into the global economy and its institutions, even as a weakened state yielded to a roiling struggle of domestic interests over the terms of this engagement. In the extraordinary times of systemic transition, a recognizably normal politics of globalization began to shape policy processes and choices.[12] Russia under Yeltsin aspired to become not only a 'normal great power' but a 'serious economic competitor' within the 'established rules of

[8] For recent overviews, see Dani Rodrik, *The Globalization Paradox: Why Global Markets, States, and Democracy Can't Coexist* (Oxford: Oxford University Press, 2011); and Jeffry A. Frieden, *Global Capitalism: Its Fall and Rise in the Twentieth Century* (New York: W.W. Norton & Co., 2007).
[9] Historically, the pluralist politics of competing interests have exerted far less influence in Russia's highly centralized system than in the more open polities and self-organized civil societies of the West. The major exception, discussed below, was the decade of weak state and international integration in the 1990s.
[10] On the entanglement of economic needs with foreign policy during this period, see Jennifer Siegel, *For Peace and Money: French and British Finance in the Service of Tsars and Commissars* (Oxford: Oxford University Press, 2014). See also David McDonald, 'Domestic Conjunctures, the Russian State, and the World Outside, 1700–2006' in Robert Legvold (ed.), *Russian Foreign Policy in the Twenty-first Century and the Shadow of the Past* (New York: Columbia University Press, 2007) pp. 173–76.
[11] Yegor Gaidar, *Collapse of an Empire: Lessons for Modern Russia* (Washington D.C.: Brookings Institution Press, 2007).
[12] Landmarks of Russia's integration included: joining, and agreeing major lending programmes with, the International Monetary Fund and World Bank; liberalization of trade, inward investment and currency regimes (rouble convertibility on current account was completed in 1996); and application to join the WTO.

the game in world markets'.[13] In a further departure, the weakening of the Russian state led to a 'domestication' of foreign economic policy as domestic interests – oligarchs, governors, organized crime groups and others – influenced or even captured decision-making and implementation.[14]

Although a more assertive, statist great-power posture and rhetoric began to take hold from the mid-1990s onwards, Russia's weakness still obliged the country to adjust to, rather than impose itself on, the international economic system. In 1998, like 10 years earlier, adverse shifts in oil prices and capital markets laid bare Russia's high dependence on the global economy, triggering a financial crash. But by now the foundations of a market economy – however imperfect and controversial – had been laid. The crash thus caused a liquidity and payments crisis, not a systemic one, and forced further painful fiscal discipline.[15] Significantly, it was the government of Yevgeny Primakov, the chief sponsor of a more assertive great-power approach, that imposed this.[16]

The major exception to this new primacy of economic integration over political goals was Russia's policy towards the post-Soviet space. Even in the early 1990s there were strong signs that economic ties would be Russia's instrument of choice in reasserting influence over what it called the 'near abroad'. In the chaos of disintegration and transition such efforts were opportunistic rather than strategic, but they set precedents for the more systematic cultivation and exploitation of such ties once Russia's economy began to revive.[17]

The Putin era: a new concept of globalization

In the aftermath of the 1998 crisis, triggered by what at the time was the biggest-ever sovereign default, Russia's prospects of further global integration seemed bleak.[18] But two far-reaching changes – one in Russia's capabilities, the other in its intentions – created the conditions for recasting Russia's political economy and its engagement with globalization in a wholly novel way.

First, Russia's capabilities were transformed by an economic recovery of remarkable speed and scale. This was driven by the two key variables linking Russia to the international economy: the price of roubles and the price of oil. Devaluation in the wake of the crisis boosted demand for domestic production. Soon after, the price of Russia's major export, oil, began to rise, and continued to do so until 2008. The 15-fold increase in the price of oil during this period brought in

[13] Andrei Kozyrev, 'Russia: A Chance for Survival', *Foreign Affairs,* Spring 1992.
[14] On the evolution of Russia's political economy and interaction with the international economy in the 1990s, see Nigel Gould-Davies and Ngaire Woods, 'Russia and the IMF', *International Affairs*, 75:1 (January 1999).
[15] On the scale and significance of the reforms after 'Black Tuesday', see Anatoly Chubais, 'Russia's Mission in the 21st Century', *Nezavisimaya Gazeta*, 1 October 2003.
[16] See, for example, Timothy J. Colton, *Yeltsin: A Life* (New York: Basic Books, 2008), pp. 417–18; and Anders Åslund, 'An Assessment of Putin's Economic Policy', *CESifo Forum*, July 2008, http://www.iie.com/publications/papers/paper.cfm?ResearchID=974.
[17] As a prescient early study noted: 'Russia cannot afford the burden of financially supporting its empire, as it has done in the past. Similarly, a weakened Russian Army (and guaranteed Western opposition) precludes it from using the military to forcibly reconquer the region.' See Fiona Hill and Pamela Jewett, '"BACK IN THE USSR": Russia's Intervention in the Internal Affairs of the Former Soviet Republics and the Implications for United States Policy Toward Russia', report published by the Strengthening Democratic Institutions Project, John F. Kennedy School of Government, Harvard University, January 1994, especially pp. 75, 86 and 89. Two methods remained available to Russia at that time. One was manipulation of, and disguised intervention in, local conflicts. The other was manipulation of economic ties. As Ukraine's prime minister (later president), Leonid Kuchma, warned in 1993: 'Russia is trying to bring about a full paralysis of the Ukrainian economy … I cannot understand the Russian position. It is not motivated by economics. It can only be seen as some sort of pressure on Ukraine.' Ibid., p. 75.
[18] To take one example: a few months after the crisis, a former senior official at the US embassy in Moscow wrote a searching essay that concluded with the invitation to 'think through seriously and systematically the possibility of a world without Russia' – see Thomas Graham, Jr., 'World without Russia?', testimony to the Jamestown Foundation Conference, 9 June 1999, http://carnegieendowment.org/1999/06/09/world-without-russia.

hundreds of billions of dollars to Russia, almost doubling GDP in a decade and creating handsome fiscal and external surpluses.

Second, Russia's new intentions emerged following the presidential succession from Boris Yeltsin to Vladimir Putin. Though carefully chosen by his predecessor, the new president brought very different formative experiences, instincts and beliefs about the means and ends of power to this office. Russia's intentions under Putin have been characterized by distinctive political and economic vectors.[19]

In politics, Putin's goals and methods have exhibited a strong – and, with time, growing – influence of *silovik* (strong-state security) thinking, reflecting his earlier KGB career. The evolution of his presidency testifies to this: the rebuilding of an authoritarian and 'super-centralized' state, the reflexive suspicion of autonomous organized social and political activity, and the impulse to exert control. The spread of *silovik* practices through political and administrative systems may be the best short-hand interpretation of the course Russia has taken since 2000.[20]

Putin's approach to economic issues has been more complex and surprising. While he has expressed nostalgia for other aspects of the Soviet past, he has shown none for the command economy or its isolation from the global economy. On the contrary: until very recently he has forcefully and repeatedly emphasized that Russia's self-interest lies in international economic integration. This may reflect an unusual degree of exposure for a former Soviet security official to economic ideas and market-oriented reformers.[21] After becoming president, Putin appointed many such reformers to key ministries and displayed an apparently genuine interest in market ideas and readiness to learn more about them.[22]

How did the distinctive political and economic policy vectors of the Putin presidency interact? In domestic policy, the restoration of political control and revival of economic reform initially appeared compatible. Putin established the primacy of central state control (*vertikal*) over oligarchs and governors with a speed and effectiveness that few had foreseen. It seemed plausible that a strong state and 'dictatorship of law' might offer a more transparent, less arbitrary framework in which markets could develop. The Gref programme of economic reform set out an ambitious agenda that recorded significant achievements in the first three years of the Putin presidency – in

[19] A range of actors and interests sought to influence economic, as well as other, policies. Putin's view was always decisive and became increasingly so as he consolidated power in a revived, post-Yeltsin presidency.

[20] For details of the resurgence of *silovik* influence, see, for example, Andrei Soldatov and Irina Borogan, *The New Nobility: The Restoration of Russia's Security State and the Enduring Legacy of the KGB* (New York: PublicAffairs, 2010). Even before he had been elected president, Putin publicly argued that a 'super-centralized state' was part of Russia's 'genetic code, its traditions, and the mentality of its people'. See Vladimir Putin, with Nataliya Gevorkyan, Nataliya Timakova and Andrei Vladimirovich Kolesnikov, *First Person: An Astonishingly Frank Self-portrait by Russia's President* (New York: PublicAffairs, 2000), pp. 182–83.

[21] Putin's *kandidat* dissertation – which he defended in 1997, just three years before becoming president – argued that Russia's development must be natural-resource-led and that large financial-industrial groups overseen by the state should be responsible for it. Before joining the KGB in 1975, he wrote his undergraduate dissertation on the 'The Most-Favoured-Nation Trading Principle in International Law'. Putin's academic supervisor, Anatoly Sobchak, was to become a leading reformer during *perestroika*. As mayor of St Petersburg, he appointed Putin as his deputy for international economic relations, a position that involved close liaison with international firms doing business in the city during the chaotic early years of market reform. From 1991 to 1996 Putin worked closely with the team of influential liberal reformers that Sobchak had gathered round him. For more on Putin's economic thinking and background, see Fiona Hill and Clifford G. Gaddy, *Mr Putin: Operative in the Kremlin* (Washington D.C.: Brookings Institution Press, 2013).

[22] Particularly striking were his discussions with Andrei Illarionov, who was his chief economic adviser from 2000 to 2005. See, for example, Angus Roxburgh, *The Strongman* (London: I.B. Tauris, 2013), pp. 46–50. Key economic ministers included Aleksei Kudrin (who had brought Putin to Moscow) as finance minister and German Gref as minister for economic trade and development.

particular, tax reform, the passage (in the face of vigorous resistance from within the State Duma) of a Land Code and the establishment of a Stabilization Fund to safeguard growing oil revenues.

This synergy between restoring state strength and driving economic reform proved short-lived. Tensions arose between these two impulses and were increasingly resolved in favour of the former. The state's size, strength and influence – and outright ownership of assets in strategic sectors, notably energy – grew. While the principle of private ownership in a market economy was never called into question, it was to be a market where ownership was conditional and dominated by a state with wide discretionary powers applied according to unwritten rules and connections rather than the rule of law.[23] A mutually reinforcing combination of *silovik* reflexes, state-led concepts of development and powerful vested interests effectively stifled further significant economic reforms after 2003. Meanwhile, the rising tide of petrodollars drove economic growth rates, raising living standards and allowing the regime to defer structural reforms.

Thus, in domestic policy, politics trumped economics. But in foreign policy, the situation was strikingly different. Even as domestic market development was being constrained by an increasingly powerful state, Russia's engagement with international markets, actors and institutions was deepening in several ways:

- Foreign direct investment (FDI) into Russia rose every year: it tripled from US$2.7 billion in 2000 to US$8 billion in 2003 and then soared to US$75 billion in 2008.[24] The capital-intensive energy sector led the way, but such investment spread across other sectors too, notably retail and services.

- Portfolio investment was revived, not least by floating Russian companies, typically via IPOs on the London Stock Exchange.[25] Foreign investment in Russian corporate debt and equity grew rapidly, especially after Russia's investment grade rating was restored in 2003, the Gazprom share 'ring fence' was removed in 2005 and the rouble was made fully convertible the following year. From 2000 to 2007 the market capitalization of Russia's listed companies rose from 15 per cent to 115 per cent of GDP. Net capital outflows, which had persisted throughout the 1990s, declined during Putin's first term. In 2005–06 Russia recorded its first annual net inflows.

- Russian outward investment increased rapidly. From 2000 to 2006 total direct and portfolio investment abroad by Russian companies rose from US$3 billion to US$19.8 billion.[26]

- Russia became increasingly integrated into structures of economic governance. In 2002 it was admitted to the G8 as a full member and four years later chaired the group. Putin renewed Russia's bid to join the World Trade Organization (WTO) and lobbied actively for membership of the OECD, to which end an accession roadmap was adopted in 2007. Having been blacklisted by the Financial Action Task Force (FATF) in 2000, Russia took steps to become compliant and in 2003 acceded to the FATF. In 2006 it joined the UN Convention Against Corruption.

[23] For an excellent analysis, see Alena V. Ledeneva, *How Russia Really Works: The Informal Practices That Shaped Post-Soviet Politics and Business* (Ithaca: Cornell University Press, 2006).
[24] See http://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD/countries?page=1.
[25] Financially and politically most significant was the US$10.6 billion flotation of a 13 per cent stake in state oil giant Rosneft in 2006, which was the largest-ever IPO in Russia and the fifth-largest in the world at the time.
[26] Lúcio Vinhas de Souza, *A Different Country: Russia's Economic Resurgence* (Brussels: Centre for European Policy Studies, 2008), p. 65.

There was nothing inevitable about Russia's deepening involvement in the global economy on so many fronts. It was no less a matter of policy choice than was the simultaneous halting of significant domestic reform. Why did Russia choose to escalate its engagement with international markets – whose powerful actors, interests and legal jurisdictions all lay beyond its control – at just the moment when it was stifling further development of its own, far more controllable, domestic markets? How did this deepening exposure to global market forces interact with the *silovik* project of reasserting political control?

The answer lies in the emergence during Putin's first two terms as president (2000–04 and 2004–08) of a strategy that we can call 'sovereign globalization'. Arising from the dual impulses to drive economic growth and political control, this strategy evolved in response to opportunities, learning and practice and became an important part of Russian foreign policy. It can be understood as an analogue of the familiar project of 'sovereign democracy'.[27] Just as sovereign democracy constrained and manipulated domestic political processes to secure the dominance and stability of the Putin regime in Russia, so sovereign globalization harnessed international economic flows to enhance the power and influence of the Russian state in the international system. It worked by maximizing the synergies, and minimizing the tensions, between these dual imperatives.[28] It comprised three elements: increasing national wealth and thus state resources; limiting the political vulnerability inherent in deeper international interdependence; and using that interdependence to create and exploit vulnerabilities in others.

The first of those goals was clear from the start of Putin's presidency.[29] Putin saw Russia's integration into the global economy as an indispensable means of overcoming what he called the 'strategic challenge' of economic weakness. The force of this conviction was striking and consistent throughout his first two terms as president. In a speech to the Ministry of Foreign Affairs in January 2001, he elaborated the role that foreign policy should play in meeting this challenge: 'In the context of growing globalization, which is much discussed, our country has yet to find its place in the world. In this context our strategic course is integration into the world community.' He called on the foreign ministry to 'pay more attention to economic diplomacy', which had 'great untapped potential'. In particular, he called for the building of 'a system of promoting and upholding our economic interests abroad to guarantee the maximum returns on the Russian economy and minimize the risks involved in our integration in the world economy'.[30]

By 2003 Putin was stressing the primacy of international integration over domestic reform. In his annual address to the Federal Assembly, he took issue with those who pressed for further structural reform over economic growth – a clear signal of his declining commitment to such reform[31]– and argued that:

[27] The term 'sovereign democracy' was first coined by Vladislav Surkov, deputy head of the presidential administration, in 2006 and was subsequently used by senior Russian figures, including Putin.
[28] In his recent comprehensive study of Russian foreign policy, Bobo Lo notes that Russia's engagement with the international economy 'seeks the best of all worlds … an economic analog of the "managed democracy" that has defined much of his presidency'. Bobo Lo, *Russia and the New World Disorder* (London: Brookings Institution Press and Chatham House, 2015), p. 84.
[29] For example, at the APEC summit in November 2000 he called globalization 'an opportunity to modernize our economy'.
[30] Remarks at a meeting of top Russian diplomats on 26 January 2001, http://archive.kremlin.ru/eng/speeches/2001/01/26/0000_type82912type82913_136920.shtml.
[31] 'But some people make an opposition between economic growth and reforms. They say it is dangerous to keep pushing economic growth, and that it is more important to carry out structural reforms … I would like to express my point of view on this question, which is that this

> Russia owes its economic growth above all to the favourable world economic situation over recent years. An unprecedented improvement in foreign trade conditions for our economy gave Russia considerable economic advantages and brought in significant additional revenue … No country today, no matter how big and how wealthy, can develop successfully in isolation from the rest of the world. On the contrary, the biggest success comes to those countries that consciously use their energy and intelligence to integrate themselves into the world economy.[32]

He went on to argue that:

> All around us are countries with highly developed economies. We need to look in the face that these countries push Russia out of promising world markets when they have a chance. And their obvious economic advantages serve as fuel for their growing geopolitical ambitions.[33]

Even in the wake of the 2008 financial crisis – the worst global market crisis since the 1930s – Putin rejected the argument that renewed isolation might serve Russia better. Such a path, he said, had 'made the Soviet economy totally uncompetitive. This lesson cost us dear. I am sure that nobody wants to see it repeated.'[34]

Putin's argument combined market means with mercantilist ends. His conviction that participation in the international economy drove economic growth was an orthodox liberal one, but with the twist that it mattered because it fuelled 'geopolitical ambitions'. Deeper global integration, according to this view, grew the economic sinews of political and military strength. Such a contribution of international economic relations to national power is traditionally termed the 'supply effect'.[35] From the beginning of his presidency, Putin fully recognized its importance.

But participation in the international economy entailed dependence on international economic partners. It has long been recognized that such dependence carries a potential 'influence effect', defined as the ability of country A to affect country B's policies as a result of B's dependence on its economic relationship with A. The greater B's dependence on A, the more vulnerable B will be to the manipulation of this relationship by A.[36] Other things being equal, the greater the economic benefit (that is, the stronger the supply effect), the greater the corresponding influence effect. Fear of such vulnerability – in particular, that economic dependence might be used to extract unrelated political demands through a policy of linkage – has been a recurring concern for Russia. Under Putin, the reflexes of *silovik* determination to rebuild a highly centralized state, restore great-power autonomy and reduce Western influences in the country powerfully revived this concern. How was the tension between loosening control of flows across borders and tightening control over the domestic political economy resolved?

opposition between growth and reforms is debatable, to say the least. We do not need reforms purely for the sake of reform. We do not need permanent revolution.' See Putin's annual address to the Federal Assembly in 2003 (available at http://archive.kremlin.ru/eng/speeches/2003/05/16/0000_type70029type82912_44692.shtml). In the same speech, he touched on issues of which reformers would approve, such as the problem of monopoly power; but his clear criticism of further structural reform was significant. And in the same speech, he called for an end to further tax reforms.

32 See Putin's annual address to the Federal Assembly in 2003, http://archive.kremlin.ru/eng/speeches/2003/05/16/0000_type70029type82912_44692.shtml.

33 Ibid.

34 See 'Putin Speaks at Davos', *Wall Street Journal*, 28 January 2009.

35 The classic work that sets out this terminology and related concepts is Albert O. Hirschmann, *National Power and the Structure of Foreign Trade* (Berkeley: University of California Press, 1969).

36 Ibid. See also David A. Baldwin, *Economic Statecraft* (Princeton NJ: Princeton University Press, 1985).

The problem of managing the influence effect manifested itself in three ways: financial indebtedness, foreign ownership of domestic assets and international legal obligations. Russia's indebtedness had its roots in the late Soviet and the early post-Soviet eras. It is thus significant that this is the one area in which Russia's involvement in globalization *declined* significantly after 2000. Between 1998 and 2005 Russia's government debt/GDP ratio fell from more than 80 per cent to less than 5 per cent as a result of a deliberate policy – not merely an inevitable consequence of Russia's oil-fuelled growth and fiscal surpluses. Russia made early debt repayment a priority, even incurring penalties by paying ahead of schedule. This approach reflected a political commitment to ensure that the perceived humiliations of the 1990s – dependence on external financing, the monthly monitoring regime required by the IMF and the crash of 1998 – could not be repeated. Putin's language betrayed sensitivity to this legacy of weakness.[37] Russia, he said, could become 'strong and respected' only once it 'gains economic power and when it no longer depends on the favours of the international financial organizations'.[38] Completing the break with the past, Russia declined in 2001 to sign a new agreement with the IMF.

This determination to wean Russia permanently off external indebtedness drove fiscal rectitude – in particular, the setting up of the Stabilization Fund to protect oil revenues from populist pressures. By reducing vulnerability to external actors and adverse circumstances, fiscal strength clearly enhanced state strength and autonomy. Thus the otherwise diverging strands of liberal economic and statist *silovik* thinking continued to support the same policy. This helps explain why Russia's strong fiscal management, unlike structural reform, was sustained after 2003.

Foreign ownership of assets – the second area of vulnerability to external factors – was acknowledged as a valuable source of capital, technology and skills that could support Russia's growth and modernization. But foreign investment meant foreign investors, whose ownership of assets triggered suspicions of excessive influence. Russia was not unique: in many countries local resistance to FDI is part of the 'normal politics' of globalization.[39] But *silovik* reflexes meant that such concerns, which had first surfaced in the 1990s, acquired a much sharper edge. Before the end of Putin's first term, the Federal Security Service (FSB, the successor to the KGB) was pushing, and liberal reformers resisting, an 'economic security' agenda.[40]

In this, as in other respects, the year 2003 proved a turning point in Russia's development. Two events illustrate the shifting management of the tension between attracting foreign investment and controlling foreign investors. In June, during a state visit to the UK – the high tide of the Russian–UK relationship – President Putin signed an agreement creating the oil company TNK-BP. It was to be the last time that a partnership in the strategically crucial energy sector was formed without a

---

[37] This comes through clearly in Putin's recollection that 'we constantly held out our hand to all international financial organizations for credits' and his satisfaction that Russia was paying its debts ahead of schedule. See 'Transcript of Meeting with Participants in the Third Meeting of the Valdai International Discussion Club', 9 September 2006, http://archive.kremlin.ru/eng/speeches/2006/09/09/1209_type82917type84779_111165.shtml.
[38] Putin's annual address to the Federal Assembly, 16 May 2003, http://archive.kremlin.ru/eng/speeches/2003/05/16/0000_type70029type82912_44692.shtml.
[39] In Western countries, specific asset transactions occasionally raise security concerns, but it is rare for the general condition of external dependence to trigger them. Examples of such concerns include the proposed 2006 sale of US port management businesses to Dubai Ports World and, more recently, US concerns about Chinese telecom company Huawei. In Russia itself, Mikhail Khodorkovsky and other domestic oil interests had lobbied in the 1990s against production-sharing agreements with international oil companies.
[40] Aleksandr Korzhakov, the then head of the Presidential Security Service, and others had warned in the 1990s that growing dependence on foreign investment posed a security threat. See Ed Bacon and Bettina Renz (eds), *Securitising Russia: The domestic politics of Putin* (Manchester: Manchester University Press, 2007), p. 158.

Russian controlling stake.[41] In October, four months later, the arrest of Mikhail Khodorkovsky marked the beginning of the Yukos affair, which led to the breakup of Russia's largest private company. This complex affair had many causes. The dominant narrative, domestically focused, stresses Khodorkovsky's growing political assertiveness and ambitions, his failure to observe the rules of the game that Putin had laid down for the oligarchs and the rising influence of the *siloviki*. But the international context was no less important: a key driver of the timing of Khodorkovsky's arrest was the Kremlin's determination to prevent the imminent purchase by ExxonMobil of a major – and potentially majority – stake in the company. Had it proceeded, this deal would have extended significant international commercial and legal influence over Russia's largest private company and its energy assets. Indeed, the significance of such a potential development was all the greater given Yukos's expected merger with Sibneft, Russia's fifth-largest oil company, and the growing challenge Yukos was mounting to the state monopoly on export routes.[42]

The successful dismantling of Yukos and the return of its assets to state ownership, despite the threat of international legal challenge, appears to have emboldened the Kremlin. The benefits of FDI were never called into question: on the contrary, such investments boomed and were welcomed. But as they did so, and as the international legal consequences of the Yukos affair appeared to recede, Russia became increasingly confident that it could attract investment while limiting the influence of investors – that is, reap the benefits of the supply effect while limiting the influence effect. Some of the rules of the game governing foreign ownership were enshrined in the statute book, notably in the crucial raw-materials sector through amendments to subsoil legislation, while broader restrictions across a range of sectors were formalized in the 2008 strategic investment law. Indeed, Russia went so far as to acquire control of two of the most important foreign majority-owned energy projects. In December 2006, following a campaign of political and legal pressure, the Sakhalin-2 consortium sold a majority stake in the project to Gazprom. The following June, TNK-BP, under similar pressure, agreed to sell the Kovykta field to Gazprom. Portfolio investment, too, was officially welcomed and boomed during these years. But foreign minority investors could face severe sanctions if they were felt to be challenging powerful interests linked to state companies.[43]

The third area of Russia's external vulnerability to globalization was the growing reach of international law and institutions. The logic of growing transnational market relations pushes states towards the harmonization of domestic laws and regulations and, ultimately, subordination to international legal obligations and procedures.[44] Russia's deepening engagement with institutions of economic governance has followed a clear pattern during the past decade. Russia has sought participation in institutions whose prestige and influence are strong but whose formal obligations are weak – that is, in arrangements that are essentially political rather than legal in nature or

---

[41] Unusually, ownership was divided equally between Western and Russian partners – that is, neither side had a controlling stake. For details of the negotiations, see John Browne, *Beyond Business* (London: Orion Books, 2010).
[42] See, for example, Marshall I. Goldman, *Petrostate: Putin, Power, and the New Russia* (New York: Oxford University Press, 2008), pp. 111–12; Richard Sakwa, *Putin and the Oligarch: The Khodorkovsky-Yukos Affair* (London: I.B. Tauris, 2014); and Dmitri Trenin, *Post-Imperium: A Eurasian Story* (Washington D.C.: Carnegie Endowment for International Peace, 2011), p. 168.
[43] One of the most prominent cases was the Browder affair. In 2005 Bill Browder, head of Hermitage Capital, Russia's biggest portfolio investor, was declared *persona non grata* and prevented from entering the country. For more details, including on the subsequent escalation of attacks on the company and its employees, see Bill Browder, *Red Notice: A True Story of High Finance, Murder, and One Man's Fight for Justice* (New York: Simon & Schuster, 2015).
[44] For a clear recent statement, see Dani Rodrik, *The Globalization Paradox: Why Global Markets, States, and Democracy Can't Coexist* (Oxford: Oxford University Press, 2011).

governed at most by 'soft law' and voluntary norms. Examples include the G8, which Russia chaired for the first (and, as it turned out, only) time in 2006; the OECD, which Russia campaigned hard but unsuccessfully to join; and the FATF.[45] Conversely, Russia's commitment has been weakest to supranational legal obligations over which Moscow has little or no control.[46]

What happened when economic benefits and loss of autonomy – the supply and influence effects – pulled strongly in opposite directions? Russia's accession to the WTO best illustrates this. While the gains from membership were significant – estimated at 3 per cent of GDP and more than 7 per cent of consumption[47] – membership required adaptation of domestic laws and practices to WTO rules, while trade disputes became subject to an independent, supranational and binding arbitration mechanism. These strong rules, strongly enforced, greatly diminish the latitude of member states to manage trade for political reasons. The main threat to trade openness typically arises from domestic protectionist interests seeking to resist foreign competition. Such interests, notably in the agricultural sector, lobbied against Russia's WTO accession, although the outcome was hardly in doubt as long as Putin continued to support accession strongly and explicitly.[48] But in Russia's case, there was a further consideration: WTO rules would prohibit the political use of trade relations for foreign-policy purposes too. As discussed below, Russia increasingly manipulated foreign access to its market, typically to punish countries whose policies had incurred Russian displeasure. Such incidents escalated even as Russia's WTO membership bid advanced.

The importance of political considerations in Russia's trade relations was illustrated in 2009, when Putin (now prime minister but still the dominant political leader) announced that Russia would suspend its WTO accession process unless the members of the new Eurasian Customs Union (Russia, Belarus and Kazakhstan) were admitted together. Although Putin later backed down and resumed bilateral accession negotiations, this action showed how Russia's goals for the customs union – that it should be not merely a regional trade agreement but a political project for reintegrating post-Soviet space – could jeopardize even Putin's long-standing policy of deeper economic integration with the West. Russia finally became a member of the WTO in August 2012, some 19 years after submitting its application to join. This was the longest membership negotiation in the history of the WTO (or GATT, its precursor). Before becoming a member, Russia had been the biggest economy outside the WTO. The difficulty of its journey to accession illustrates the inherent tension between seeking prosperity through international integration and aspiring to

[45] On the FATF and 'soft law', see Clifford G. Gaddy and William Partlett, 'Russia's Financial Police State', *National Interest*, 19 July 2013. Russia chaired the FATF in 2013–14.

[46] Perhaps the clearest example was the Energy Charter Treaty. Not only is this a legally binding instrument that provides for international arbitration; it also regulates international governance of the energy sector, considered by Russia a major instrument for exercising influence abroad. In particular, the treaty provides investor protection against non-commercial host-country risks and facilitates a stable, open transit regime. Having signed the treaty in 1994 but declined to ratify it, Russia finally revoked its provisional application in 2009.

[47] David Tarr, *Russian WTO Accession: What Has Been Accomplished, What Can be Expected*, World Bank report, October 2007.

[48] Some major business figures, such as Aleksei Mordashov and Viktor Vekselberg, spoke out in favour of WTO accession, while Oleg Deripaska opposed it. Agricultural interests and banks that were opposed to the concession of branch banking for foreign entities resisted too. The Duma vote in favour of ratification was surprisingly close at 238 to 208 – only United Russia supported it. For more on the domestic politics of Russia's trade, see Anders Åslund, 'Testimony at the Hearing on EU Economic and Trade Relations with Russia, Committee on International Trade, European Parliament, Brussels, November 21, 2006', http://www.iie.com/publications/papers/print.cfm?ResearchId=690&doc=pub.

remain an unconstrained 'great power'. Indeed, within months of Russia's accession, EU voices began expressing concern about Moscow's violations of its new WTO obligations.[49]

Russia's membership of international economic institutions has thus tended to be in inverse proportion to the strength of the corresponding obligations. Much harder to control, however, has been Russian elite access to Western legal jurisdictions to make contracts, pursue claims and protect rights. As secure places to keep assets, families and boltholes, Western countries present an attractive alternative to the insecurity of informal rules and arbitrary power in Russia. Moreover, the Russian state's own record in bringing cases in foreign courts has generally been poor.[50]

In sum, globalization presented Russia with a dilemma: how to reap economic gains and thus strengthen state power while maintaining independence and autonomy in the exercise of that power. A three-fold solution emerged: reduce foreign debt and protect against future indebtedness; circumscribe foreign majority-ownership rights; and calibrate participation in global economic governance to maximize the balance of benefits over binding obligations. As a result, during Putin's first two terms the tension between the 'supply' and 'influence' effects of the international economy was successfully managed. Russia grew far richer, stronger and more globally integrated than it had been a decade earlier, while foreign investors became far more exposed to, but less influential in, Russia.

As Russia prospered from oil-driven growth, the reach of its ambition grew. President Putin and others spoke of making the rouble an international reserve currency and Moscow a major financial centre. The Duma even introduced a draft law (though never passed) to ban denomination of official figures in dollars. The conviction began to take hold that Russia could not only use the international economy to drive domestic growth while managing the associated risks of vulnerability, but could dictate the terms on which external actors engaged with Russia and even shape the rules of the international economic order. Rather than Russia adapting to the global economy, other countries would have to adapt to Russia. From this assertiveness, a new and more striking element of Russia's globalization strategy was forged: the use of economic relations as an instrument of influence over others.

This was a historic departure for Russia. As an economically weak great power, Russia had always been a potential target, rather than user, of such methods. Other developed countries have occasionally manipulated economic relations to pursue non-economic goals, notably through sanctions; but these are specific and exceptional cases. The novelty of Russian policy under Putin lay in making this a systematic part of its management of globalization. Powerfully conditioned by Soviet *silovik* instincts of *kto-kovo* ('who against whom'), its essence was the use of positive-sum economic cooperation to achieve broader zero-sum political goals of influence and domination. For the first time, Russia began to use economic power as a source of strength in its foreign policy.

[49] In December 2012 EU Trade Commissioner Karel De Gucht complained that, 'Since Russia has become a member of the WTO, they are doing exactly the opposite of what they are supposed to do or what they have been promising to do.' See 'Europe cools on Russia's WTO accession', *Financial Times*, 5 December 2012.
[50] On the challenge to Russia's modes of informal and insecure governance (known as *sistema*) posed by participation in the global economy and foreign legal systems, see especially Alena V. Ledeneva, *Can Russia Modernise? Sistema, Power Networks and Informal Governance* (Cambridge: Cambridge University Press, 2013).

Russia honed and applied this growing strength in two distinct arenas – the former Soviet Union and Europe – and sought to insulate the effects in one from those in the other. Initially, Russia focused on the former Soviet Union, where inherited linkages and dependencies offered natural opportunities for influence that had been put to episodic use in the 1990s.[51] Russia's rapid economic recovery after 2000 turned it into a locomotive of regional growth, increasing local dependence on access to Russian markets. As Russia became stronger and more assertive under the Putin presidency, its use of economic means to achieve political influence became, in the words of the most comprehensive study of this subject, 'more sophisticated, pragmatic, rational and well-executed' – that is, more systematically integrated into foreign policy.[52] One method was to exploit Russia's power as a consumer market by banning selected imports (usually foodstuffs) on the pretext of health concerns, thereby imposing costs on the producing countries, in response to specific actions that had displeased Russia. In most cases, these products were of high value to the targeted country but of low value to Russia.[53] A second method was to manipulate energy supplies by cutting, or threatening to cut, flows or by introducing politically discriminatory pricing. Again, the intention was often purely punitive; but sometimes it had the goal of forcing the sale of mid- or downstream energy assets to Russia in order to gain influence.[54] The weak and opaque legal systems of the countries targeted offered ample opportunity to cultivate corrupt relationships that compromised individuals and interests, thus inducing pliancy and extending influence within those states.

But Russia's ambitions to exert economic influence were not confined to the former Soviet Union. As the EU's already-substantial dependence on Russian energy supplies grew, and as other strands of the EU–Russia economic relationship thickened, the Kremlin began to consider how these ties could be used to exert Russian state influence. The challenges were formidable since the EU environment was very different from that of the post-Soviet space.[55] Its economy was many times larger, more advanced and more diversified than Russia's; there were few established economic linkages for Russia to exploit; and member state legal and regulatory systems were generally transparent and robust. Different strategies and methods from those used with former Soviet states were therefore needed to cultivate an 'influence effect'. Russia's use of economic means with the EU was correspondingly softer and more diffuse than with the states of the former Soviet Union. It favoured cooperation more than coercion, co-option more than corruption, inducements more than threats and persuasion more than punishment. It was also longer-term in nature, seeking at its most ambitious not merely to respond to specific events (as with import bans on former Soviet neighbours) but to reshape the dynamics, perceptions and expectations governing the EU's relationship with Russia. This strategy deployed a range of methods. Business relationships provided opportunities to cultivate local influencers and opinion-formers. Foreign investors in Russia were encouraged to lobby their home governments to 'understand' the Russian point of view

[51] There were two years in which such activities spiked: 1992, when post-Soviet arrangements were still being established; and 1998, when Russia sought unsuccessfully to gain control over the Mazeiku oil refinery. See John Lough, *Russia's Energy Diplomacy*, Chatham House Briefing Paper, REP RSP BP 2011/01, May 2011, p. 8. For early post-Soviet examples, see Hill and Jewett, 'BACK IN THE USSR'.
[52] Jakob Hedenskog and Robert L. Larsson, *Russian Leverage on the CIS and the Baltic States*, report published by the Swedish Defence Research Agency, June 2007, p. 113. See also Trenin, *Post-Imperium*, pp. 149–50.
[53] Target countries included Georgia, Ukraine, Moldova, Belarus and the Baltic states – the last-named both before and after their accession to the EU. They also included some non-former Soviet Union countries, notably Poland, whose meat exports were banned in 2007.
[54] Examples include domestic pipeline networks, the Mazeiku refinery and the Ventspils oil terminal.
[55] For example, in several central and southern European states, shell companies and other opaque business practices have been used by Russian entities to secure influence over energy assets. Lough, *Russia's Energy Diplomacy*, in particular pp. 12–14; and James Sherr, *Hard Diplomacy and Soft Coercion: Russia's Influence Abroad* (London: Chatham House, 2013).

and avoid raising more difficult issues like human rights. Shell and BP were reportedly allowed to maintain a minority position in the Sakhalin-2 and Kovykta projects in order to maintain a moderating voice in Western counsels.[56] Individual interests reinforced corporate ones when lucrative positions on boards or as advisers were offered to the well-connected.

The cultivation of influence *within* states complemented growing efforts to exercise influence *over* them. This strategic intent can be understood as 'energy Finlandization', by analogy with earlier patterns of relations on the Continent. During the Cold War, the term 'Finlandization' had been coined to describe how Soviet power could, over time, exert subtle but effective pressure on small neighbours to accommodate the USSR's wishes without making overt threats.[57] Under Putin, Russia's emerging ambition was now to use its role as the EU's dominant energy supplier to cultivate a broader political influence far beyond specific energy issues. Russia's steady fostering of Europe's growing dependence, aided by expensive marketing campaigns, would cause a generation of Europeans to grow up associating Gazprom's supplies – and, increasingly, mid- and downstream asset ownership – with the comfort and security of heat and light in their homes. The implications of any unhelpful developments – a policy here, a statement there – that might cause apparent complications for future energy investment plans or deliveries would be all the more compelling for remaining unspoken. Thus would Russia, through its energy policy, win European 'hearths and minds' and so achieve not only prosperity but power.

As the Russian Security Council developed a long-term 'concept of foreign energy policy',[58] an increasingly confident and assertive Russia sought to set the rules and realities of its energy relationship with the EU. Russia used its G8 presidency to press the case for 'security of demand', negotiated long-term bilateral contracts with individual EU member states and sought to acquire downstream assets in Europe. Gazprom began building the Nord Stream and South Stream gas pipelines to bypass Belarus and Ukraine, thereby increasing those countries' dependence on Russia while reducing the impact of exploiting this dependence on Russia's relations with the EU. Despite creating divisions among the member states of the union, these pipeline projects went ahead, thus confirming the EU's continued inability to agree a coherent policy towards Russia. Gazprom spoke of becoming a US$1 trillion company at an oil price of US$250/barrel, predicted it would capture 10 per cent of the UK market by 2011 and came close to bidding for the UK utility Centrica until warned of the 'robust scrutiny' by regulatory authorities that would follow. Tellingly, in response to this rare rebuff, Gazprom felt confident enough to issue a veiled threat that it could redirect its supplies to China: 'If the European Union wants our gas, then it will have to consider our interests as well.'[59] Putin himself reiterated the warning soon after:

[56] Mark Leonard and Nicu Popescu, *A Power Audit of EU-Russia Relations*, European Council on Foreign Relations, 2007, p. 14.
[57] From the 1960s onwards, the term 'Finlandization' was used in Western security debates to portray the perceived dangers of a declining US commitment to Western Europe.
[58] The Russian foreign ministry's 2007 'Review of the Foreign Policy of the Russian Federation' drew attention to the growing significance of energy in Russian foreign policy, noting that the Security Council had begun work on a medium- and long-term 'Concept of Foreign Energy Policy'. This was the only mention in the document of this key security body. It is unusual for a foreign ministry document to mention the Security Council by name. See http://archive.mid.ru//brp_4.nsf/sps/3647DA97748A106BC32572AB002AC4DD.
[59] See 'Gazprom issues threat to EU gas supply', *Financial Times*, 20 April 2006; and 'Moscow should repudiate gas supply blackmail', *Financial Times*, 24 April 2006.

> What are we to do when we hear the same thing every day? We start to look for other markets ... When people come to us, it is investment and globalization, but if we plan to go somewhere, then it is already the expansion of Russian companies.[60]

This statement conflated the separate issues of energy asset ownership and energy supply. In addition, it passed over the fact that Gazprom had been interested in the takeover of a major energy asset – something that Russia itself was denying to foreign companies. None the less, it was telling that the threat – always implicit in 'energy Finlandization' – to manipulate vulnerability when 'interests' were not respected had surfaced in response to growing EU concerns.[61] This epitomizes the blend of inducements and threats that has been felicitously termed 'soft coercion'.[62]

As Putin's second presidential term came to an end in early 2008, Russia's emerging strategy appeared highly effective. Russia was growing rapidly wealthier – and so stronger – through escalating international economic engagement. It had limited the unwelcome influence that this openness might bring without, it seemed, stemming profitable capital inflows. And it was finding new uses for economic levers of influence over others, especially – a novelty for Russia – over the EU. As a consequence, the Russia–EU economic relationship flourished even as political relations deteriorated. In sum, a coherent 'sovereign globalization' had emerged, controlling the tensions and harnessing the synergies of international openness, bringing both prosperity and, increasingly, power.

The 2008 crash and after

While Russia had worked to limit its economic vulnerability to external actors, its underlying dependence on the global economy had in some respects grown under Putin.[63] The global financial crisis of 2008 should therefore have caused immediate alarm. Instead, as the crisis hit Western economies, Putin was initially emboldened further. Emphasizing Russia's role as a major international economic player, he outlined an agenda for reforming global governance and offered to host a conference on managing the crisis. His rhetoric remained pro-globalization: he explicitly rejected criticism of the market, emphasized the importance of the international economy, called for deeper integration of Russia into global capital markets and proposed the 'transformation of Moscow into a powerful global financial centre'.[64] In a still-mysterious episode soon after, US Treasury Secretary Hank Paulson was told by a senior Chinese official that Russia had proposed a coordinated selling of holdings in the US mortgage institutions Fannie Mae and Freddie Mac, which would have deepened the turbulence in US capital markets.[65]

---

[60] See 'Putin Steps Up Gazprom Defense', *Moscow Times*, 28 April 2006, http://www.themoscowtimes.com/sitemap/free/2006/4/article/putin-steps-up-gazprom-defense/205276.html.
[61] Ironically, Putin made this remark at a signing ceremony for an asset-swap agreement between Gazprom and BASF. See 'Putin Steps Up Gazprom Defense', *Moscow Times*, 28 April 2006.
[62] Sherr, *Hard Diplomacy and Soft Coercion*.
[63] From 2000 to 2008 oil and gas rents rose from around 20 per cent to 30 per cent of the total economy – that is, by 50 per cent. See Sergei Guriev and Alec Tsyvinski, 'Challenges Facing the Russian Economy After the Crisis' in Anders Åslund, Sergei Guriev and Andrew C. Kuchins (eds), *Russia After the Global Economic Crisis* (Washington, D.C.: Peter G. Peterson Institute for International Economics, Center for Strategic and International Studies, New Economic School, 2010), p. 19.
[64] Speech at 12th St Petersburg International Economic Forum, 7 June 2007, http://en.kremlin.ru/events/president/transcripts/345.
[65] Robert Peston, 'Russia "planned Wall Street bear raid"', BBC News, 17 March 2014, http://www.bbc.com/news/business-26609548.

The crisis eventually hit Russia hard, causing the economy to contract more than that of any other G20 country.[66] Russia's initial response under the presidency of Dmitry Medvedev (2008–12) encouraged those who advocated a policy course of reform and deeper international integration.[67] Though constrained by the de facto limits on his power, Medvedev set out a vision of a modernized Russia prospering from a healthy relationship with the international economy. His remarkably candid manifesto, 'Go, Russia!', criticized historical patterns of engagement: 'Centuries of economic backwardness and the habit of relying on the export of raw materials, exchanging these for finished products.' He lamented the fact that 'domestic business does not invent nor create the necessary things and technology that people need. We sell things that we have not produced, raw materials or imported goods.' He even appeared to look forward to a time when Russia would adapt to the global economy through political and social, as well as economic, reforms, achieving prosperity through intellectual, rather than natural, resources and 'creating unique knowledge, exporting new technologies and innovative products'.[68] And as he explained one year later, this would be supported by 'special modernization alliances' with the US and the EU.[69] It was a vision very different from that of Putin's dissertation a decade earlier that the country's 'resource potential will become one of the most important pre-conditions for Russia's sustainable entry into the world economy' and remain the basis of its development into the mid-21st century.[70]

A few steps were taken in the spirit of Medvedev's manifesto. His flagship Skolkovo Innovation Centre was founded as a high-technology institute with international faculty and collaboration. And after years of pressure on international energy companies, Russian policy began to show renewed recognition of their importance in developing the challenging offshore fields necessary to sustain longer-term production. The Law on Strategic Investment was amended to make it less restrictive.[71] But Medvedev's presidency, constrained by Putin's continued dominance, was a brief interlude that masked and delayed a deeper reorientation of Russia's approach to the global economy.[72] Several new factors began to impose strains on Russia's strategy of 'sovereign globalization'. Three were especially significant:

1. **Russia's declining economic performance**. Although the oil price soon bounced back, the 2008 global financial crisis marked a watershed in Russia's economic performance. For the period 2000–08 the average annual growth rate was 6.9 per cent, while from 2009 to 2013 it fell to just 1 per cent, despite the fact that the oil and gas windfall for the latter period was, at US$1.2 trillion, one-third higher.[73] Russian growth had become even more dependent on the oil price as well as on international private capital, but hydrocarbon revenues could no longer provide the same degree of economic stimulus as before. As Putin himself appeared to

[66] The economy contracted by 8 per cent in 2009, and the net negative change in the growth rate over 2008–09 was 13 percentage points. See Guriev and Tsyvinski, 'Challenges Facing the Russian Economy After the Crisis', pp. 17–18.
[67] As Dmitri Trenin put it, modernization was the only alternative to marginalization (see Trenin, *Post-Imperium*, p. 237).
[68] 'Go, Russia!', published on 10 September 2009, available at http://en.kremlin.ru/events/president/news/5413. Medvedev's difficult relationship with Igor Sechin, CEO of Rosneft, epitomized his support for a modernizing rather than statist-*silovik* approach to economic management.
[69] 'Speech at meeting with Russian ambassadors and permanent representatives in international organisations', delivered on 12 July 2010, http://en.kremlin.ru/events/president/transcripts/8325. Some foreign-policy implications of this approach were set out in a report by the Ministry of Foreign Affairs published in May 2010. See the Jamestown Foundation's *Eurasian Daily Monitor*, Volume 7, Issue 97, 19 May 2010.
[70] Vladimir Putin, 'Mineral and Raw Materials Resources and the Development Strategy for the Russian Economy', translated by Thomas Fennell, http://www.theatlantic.com/daily-dish/archive/2008/08/putins-thesis-raw-text/212739/.
[71] For example, the threshold for defining 'foreign control' was raised from 10 per cent to 25 per cent ownership.
[72] As noted earlier, President Medvedev could not, for example, prevent Putin from briefly suspending Russia's WTO accession process.
[73] Alexey Kudrin and Evsey Gurvich, 'A new growth model for the Russian economy', BOFIT Policy Brief 01/2015.

recognize, in an implicit but decisive rejection of the argument of his dissertation, the hydrocarbon-export growth model was exhausted.[74] In other words, the 'supply effect' – Russia's economic gains from international interdependence – had diminished.

2. **The 'revolution in energy affairs'**.[75] The spread of industry-changing technologies – chiefly, shale 'fracking' in the US and the expansion of global liquefied natural gas (LNG) transportation – began to undermine Gazprom's model of supplying gas through bilateral long-term contracts and thus Russia's ability to extend and entrench its influence in Europe. Gazprom's instinctively monopolistic behaviour exacerbated this challenge. The company was slow to acknowledge these profound market changes, while some voices even dismissed shale gas as a CIA plot. More generally, Gazprom's multiple failures – poor performance, inefficiencies and failure to control costs – provoked frustration even in Putin, who had assigned the company a key role in his external energy policy. This prompted a search for alternative instruments of energy policy, notably Rosneft. In short, Gazprom had become a less effective means of exercising influence abroad.[76]

3. **The EU's response**. The EU sought ways to reduce dependence on Gazprom because of growing concerns about the company's dominance and reliability. These concerns were triggered at the very moment of a major achievement of Russia's 'sovereign globalization'. On 1 January 2006, the first day of Russia's first (and only) G8 presidency, whose main theme was 'energy security', Russia cut off gas supplies to Ukraine over a debt dispute with the 'Orange' government. Hitting downstream consumers in several EU member states in midwinter, that move ignited a debate about the risks of growing dependence on Russian energy. It hastened a search for ways to diversify suppliers and routes and was to lead, via the Third Energy Package and pursuit of anti-trust cases, to the legal challenge of Gazprom's restrictive and monopolistic practices. In 2009 the EU launched its Eastern Partnership, offering a closer relationship with Belarus, Moldova, Ukraine and the three countries of the South Caucasus. The partnership's economic dimension was the most attractive one for these post-Soviet states.[77]

Together these developments marked a sharp and adverse shift in the terms of economic and political exchange facing Russia. The returns of its strategy were declining: Russia's influence was meeting effective resistance, and the EU's own influence in Russia's self-declared 'sphere of privileged interests' was growing.[78] The synergies of interdependence and *derzhavnichestvo* ('great-power status'), harnessed so well by sovereign globalization, now gave way to contradictions, of which three stood out:

[74] 'Today, the potential of the "natural resource economy" is running out and, most important, has no strategic prospects.' See Vladimir Putin, 'Russia in Focus: The Challenges We Must Face', pre-election article in *Izvestiya*, 16 January 2012. Putin also commented that the 'capacities of the raw materials-based economy are exhausted' in his address to the Federal Assembly in 2012, http://en.special.kremlin.ru/events/president/news/17118.
[75] This term was coined by Pavel K. Baev, echoing the scientific-technological revolution of the 1980s that undermined Soviet military power. See Pavel K. Baev, 'Russia and Turkey Find a Common Cause in Confronting the Specter of Revolution', *Turkish Policy Quarterly*, Volume 12, No. 4, Winter 2014, p. 47; and 'How Russia's Energy "Weapon" Turned into an Oil Pillow and Gas Rattle', PONARS Eurasia Policy Memo No. 294, September 2013.
[76] It is now ranked only the 43rd-largest oil and gas company in the world, having fallen from fourth-largest in 2014. See http://top250.platts.com/Top250Rankings.
[77] This included bilateral aid and Association Agreements with Deep and Comprehensive Free Trade Agreements. For a recent summary assessment, see 'The Eastern Partnership – A policy that delivers', European Commission Fact Sheet, Brussels, 21 May 2015, http://europa.eu/rapid/press-release_MEMO-15-5019_en.htm.
[78] This only increased Russian alarm, which had been stoked by the 'colour revolutions' in Georgia, Kyrgyzstan and, above all, Ukraine.

- The opportunity cost of Russia's hydrocarbon growth model became clear. Economic reforms had been shelved; the country had failed to modernize; and a dysfunctional corrupt state capitalism had become entrenched. The pursuit of external influence had been bought at the cost of future growth. 'Supply' and 'influence' effects, it turned out, pulled in different directions after all.

- The inherent tension between international markets and great-power monopoly was exposed. Once Russian actions had provoked the EU to formulate a response to growing energy dependence, the union's slow, bureaucratic deliberation proved unexpectedly effective. It drew on market-based legal and regulatory solutions and was aided by technologically-driven market development of the kind that monopolists resist or are slow to comprehend. Long treated by Russia as a weak and easily divided player, the EU demonstrated a strength that surprised Moscow.

- Russia's great-power attitudes to, and treatment of, former Soviet countries – including the political manipulation of trade in order to punish – hindered the development of stable and cordial relations. This coercive influence impelled Russia's neighbours to seek a stronger, countervailing European influence and to welcome the Eastern Partnership and other opportunities for closer association.[79] Moreover, Russia's treatment of its post-Soviet neighbours heightened EU concerns about the longer-term implications of its own energy dependence on Russia.

External influence at the expense of domestic modernization, monopolism at the expense of free and open markets, domination at the expense of partnership – all were manifestations of the underlying tension between great-power assertiveness and international interdependence. Rather than serving as a long-term strategy, Russia's sovereign globalization was revealed as able to work only in specific and temporary circumstances: high oil prices, high consumer dependence on a regional gas market, and the ability to insulate the use of coercive and co-optive methods of influence from one another.

How did Russia respond to these setbacks? The outlines of a new Russian relationship with the international economy emerged with Putin's return to the presidency in 2012, following the most significant public demonstrations so far seen against his regime.[80] He brought back to this office a darker and more pessimistic view of globalization.

First, while continuing to reject autarky, Putin became notably less effusive about the benefits of globalization, which he now began to portray as a source of 'objective pressures' on Russian national identity.[81] Second, no doubt sensitized by the Bolotnaya protests, he now increasingly saw globalization as a threat to domestic cohesion, especially as it subverted the loyalties of business and administrative elites – with their assets, tastes, holidays and families in the West. While Russia

[79] The extent of the welcome varied, of course. But even Belarus, compelled by Russian pressure to seek balances, joined the partnership, despite its long hostility to the EU's 'values agenda'.
[80] Major protests had taken place in 2005 but had been directed against a specific government policy – the monetization of social benefits – rather than the system itself. The 2011–12 protests were an inherently more significant challenge to the regime and were understood as such by it.
[81] See Putin's remarks to the Valdai International Discussion Club on 19 September 2013, http://en.kremlin.ru/events/president/news/19243.

had assiduously cultivated Western elites to exercise influence on the policies of their countries, Putin now feared that the attractions and security offered by the West might call into question the commitment of Russia's elites to his regime. This was to effloresce into the idea of a 'sixth column' working against Russia from within the state – outwardly loyal to the president but quietly sabotaging his work with arguments citing 'limited resources', 'foreign political and economic ties' and 'concern for Russia's image' in order to advance 'the trading system, liberalism, individualism, globalism'.[82] To bolster elite dependence, Putin launched a 'de-offshorization' campaign, which included a decree banning government officials from holding financial assets overseas. This unilateral revision of the elite rules of the game was controversial, unpopular and subject to evasion.[83] In addition, Putin criticized major Russian businesses for conducting most of their transactions under foreign, not Russian, law. He sought to limit offshore arrangements by Russian companies, even as large capital outflows resumed. State officials were later discouraged from taking holidays outside the former Soviet Union.

Third, Putin tightened integration of the post-Soviet space. After years of inconclusive discussion of a 'single economic space', the Russia–Belarus–Kazakhstan Customs Union was signed in 2007 and entered into force in 2010. Preparing his return to the presidency, Putin proposed its transformation into a full 'Eurasian Union' that would become 'one of the poles in the modern world' attracting further members.[84] In practice, this group is best understood as a geopolitical project to use economic integration to deepen Russian influence over the post-Soviet space.[85] While the union is ostensibly 'legal and rule-based' in form,[86] Russia has used its dominant position to push for harmonization of member states' trade and other policies overwhelmingly on Russian terms.[87]

Finally, the decline of Russia's growth model meant that a new basis of regime legitimacy was needed – a point the Bolotnaya demonstrations had driven home too. Putin placed new importance, even urgency, on the protection of Russian traditions against a 'deficit of spiritual values'. This threat, he argued, arose in particular from the West's betrayal of its civilizational heritage and attempts to impose an 'equality of good and evil'.[88] While Russia continued to express the desire to play an active role in the global economy,[89] its rhetoric and policies were shifting into a different key. The ambition and reach of sovereign globalization gave way to defensive retrenchment; protection of regional 'space' took priority over the spread of diffuse influence in Europe; and

[82] See, for example, Alexander Dugin, 'Sixth Column', *Vzglyad*, 29 April 2014. Dugin, who is leader of the Eurasian Movement, believes that elites' integration into the world economy has impelled them to urge restraint on Russia in Ukraine. See his 10 July 2014 interview with the BBC, http://www.bbc.com/news/world-europe-28229785.
[83] Putin acknowledged that this policy would not be welcomed when he introduced it in his 2012 address to the Federal Assembly: 'Hold your applause, you may not like what is coming', see http://en.special.kremlin.ru/events/president/news/17118.
[84] Vladimir Putin, 'A new integration project for Eurasia: The future in the making', *Izvestiya*, 3 October 2011.
[85] Owing to its trade-diverting consequences, the Eurasian Union offers only limited net economic benefits, especially for Russia as the overwhelmingly dominant member. For a Russian view of Eurasian integration as a geopolitical struggle for great-power status and influence, see Timofei V. Bordachev and Andrei S. Skriba, 'Russia's Eurasian Integration Policies', in *The Geopolitics of Eurasian Economic Integration*, a report published by the London School of Economics and Political Science in June 2014.
[86] Rilka Dragneva and Kataryna Wolczuk, *Russia, the Eurasian Customs Union and the EU: Cooperation, Stagnation or Rivalry?*, Chatham House Briefing Paper, August 2012.
[87] Russia continues to push for closer integration, despite the apparent reluctance of other Eurasian Union members. See, for example, 'Russia's Putin calls for regional currency union', Reuters, 20 March 2015.
[88] See Putin's 2013 address to the Federal Assembly, http://en.kremlin.ru/events/president/news/19825; and his 2013 meeting with members of the Valdai International Discussion Club, http://en.kremlin.ru/events/president/news/19243.
[89] Very little in the way of policy development supported such statements. One exception was the further liberalization of the bond market to allow greater access to foreign financing. See 'Debt Investors Turn Page on Russia', *Wall Street Journal*, 19 December 2012.

spiritual and ethical opposition, not common economic interests, increasingly defined Russia's attitude towards the West.

Like two tectonic plates drifting towards each other, the Russian and Western conceptions of economic relations collided over Ukraine, the most significant of the EU's Eastern Partners and the ultimate prize of Russia's Eurasian integration project.[90] In November 2013 intense Russian pressure on Ukraine not to sign the planned EU Association Agreement and Deep and Comprehensive Free Trade Agreement triggered a chain reaction.[91] The Viktor Yanukovych government's surrender to this pressure, and its decision to revive plans for a deeper relationship with the Russian-led Customs Union, sparked protests that led to its overthrow. Russia responded by annexing Crimea, to which the West, in turn, reacted by imposing sanctions and suspending Russia's membership of the G8 in its presidency year. Russia's retaliation to the embargo was, in effect, to impose further sanctions on itself by banning Western food imports.

A new era began in Russia–West relations, inverting patterns that had defined their post-Cold War relationship. The West now sought to punish Russia by restricting its economic ties, rather than integrate it by expanding them. Russia in turn now emphasized self-reliance rather than interdependence. In Putin's words: 'We must above all understand that our development depends primarily on us … rather than hope for favourable circumstances or foreign markets.' He set out an agenda of import substitution that would limit Western imports to 'unique equipment and technology abroad'.[92] Russia escalated its strident 'civilizational' campaign not only against the West but specifically against Europe – a striking departure for a country that, historically, and however great the ideological divide, had always insisted on its European heritage.[93]

Only two years earlier, one of Russia's most astute observers had written that 'expansion has yielded to introspection', the 'West is back as Russia's ally' and the 'EU is Russia's most important modernization resource'.[94] The speed and scale of the decline in Russia–West economic relations – the strongest strand of their relationship during the Putin presidency – can be measured by the fact that such prospects now appear unthinkable.

Conclusions and implications

The 20th century saw the fall and rise of Russia's engagement with the global economy. The 21st century has so far seen its rise and fall. The largest country in the world risks being decoupled from globalization, the dominant trend of our times.

De-globalization does not mean isolation. Russia continues to trade, invest and attract investment; Russian firms are still quoted on foreign stock markets; and foreign citizens continue to work in

[90] Those conceptions were at odds with each other inside Ukraine as well: political forces in that country reflected the Western and Russian governance models – the one 'essentially based on rights and rules, and the other on connections, clientelism and the subordination of law to power'. See James Sherr, *Ukraine and Europe: Final Decision?*, Chatham House Programme Paper 2013/05, p. 10.
[91] For more details about Russian pressure on Ukraine, see James Sherr, 'Ukraine "is in a dangerous situation"', *Kyiv Post*, 23 December 2013.
[92] Putin, annual address to the Federal Assembly, 2014. See http://kremlin.ru/events/president/news/47173.
[93] Some Russian scholars have gone so far as to suggest that the country has now broken decisively with its 300-year-old aspiration to join the West. See, for example, remarks by Viktor Sumsky, director of the ASEAN Centre of the Moscow State University of International Relations (MGIMO), at an open forum on Russia's turn to Asia at Chulalongkorn University, Thailand, on 22 May 2015.
[94] See the 'Conclusion' in Trenin, *Post-Imperium*, pp. 233–42.

Russia. The decoupling is limited to Russia's most important partners. But given the West's dominance as a market and source of capital and technology, this is a striking development – one that has swiftly thrown into reverse the deepening relationships that Russia had actively encouraged and the West actively supported. Russia's engagement with globalization is thus not just a technical subject for trade and finance specialists. It tells us much about the Putin project, Russia's development choices and prospects, and the future of globalization itself.

Russia's approach to globalization after 2000 stemmed from the dual imperatives of political control and economic prosperity, which lay at the heart of the Putin project. Putin himself understood that economic prosperity and state strength demanded a deeper relationship with the global economy. This meant engaging with powerful external actors, interests and jurisdictions, but on terms that would limit unwelcome external influence. The need to accommodate the demands of globalization may have been the most important constraint on *silovik* reflexes to tighten further political control.

Russia's early management of this balance was so successful that Putin began to seek from globalization not just domestic affluence but foreign influence.[95] This was a novel departure, turning Russia's traditional weakness into a source of strength and completing the emergence of an ambitious 'sovereign globalization' strategy. Like 'sovereign democracy', the new strategy sought to manipulate spontaneous processes for state-directed ends. But sovereign globalization proved inherently harder to practise. While sovereign democracy insulated the domestic polity from international influences, sovereign globalization could not, by definition, do without these influences. It sought rather to make them useful and safe, harnessing the principles of interdependence – positive-sum, based on exchange and reciprocity – to the practice of power politics – zero-sum, rooted in power and subordination.[96] An initially successful approach was built on the shifting sands of specific, temporary and favourable circumstances. A combination of domestic inefficiency, market developments, Russian overreach and international reaction caused the synergies of this strategy to give way to contradictions and the balance of opportunity and risk to turn sharply against the Putin regime.

This perspective resolves several paradoxes. It explains why Russia rapidly increased its exposure to international markets even as it restricted reforms that would support domestic ones. It explains why Russia–West economic relations deepened even as their political relations deteriorated. And it explains why sovereign globalization initially succeeded and later failed as a consequence of the changing terms of engagement – first a meshing, then a clashing – between Russian intentions and the conditions in which they were pursued.

This approach also offers a fresh interpretation – a political economy – of the present crisis in Russia–West relations as a logical outcome of the unravelling of Russia's sovereign globalization. As with sovereign democracy, when manipulation failed, then harsher methods were used. This

[95] This did not feature in Putin's 1997 dissertation, which is otherwise a fairly reliable predictor of key aspects of Russia's economic policy. The dissertation states that the 'Russian mineral and raw materials complex plays an important role in all vital state functions', including 'the foundation of the defensive might of the country'. This is an aspect of the 'supply effect', discussed above, rather than an 'influence effect' on other countries' policies (see Putin, 'Mineral and Raw Materials Resources').

[96] For a discussion of these contrasting 'normative systems demarcating different traditions of statecraft and governance, law and business', see Sherr, *Ukraine and Europe: Final Decision?*, p. 10.

explains the singular fact that the crisis was triggered not by hard security issues such as NATO enlargement or ballistic missile defence, which had long stoked Russian resentments, but by a technical trade document at the heart of the EU's draft Association Agreement with Ukraine. When the EU's economic attractiveness threatened Russia's geopolitical aspirations, Moscow ceased to draw a sharp distinction between the 'good West', represented by the EU and trade, and the 'bad West', epitomized by NATO and security.

What next for Russia? The goals of sovereign globalization were to integrate Russia into the global economy and governance in order to make it richer and therefore stronger, to limit unwelcome globalizing influences on Russian interests and to use those same influences as instruments of its own foreign policy. The prospects that now face Russia are the opposite in each respect:

- **Russia's economic growth prospects look bleak**. In the short term, this is a consequence of lower oil prices and Western sanctions. In the longer term, and more seriously, prioritizing the pursuit of sovereign globalization over domestic reforms has shaped a political economy that hinders modernization and diversification.[97] The result could be a lost decade of development and renewed potential for popular disillusion and protest.[98] Ironically, Russia is now more dependent than ever on global economic conditions. Had it pursued an orthodox globalization policy – one that sought primarily to maximize the 'supply effect' of economic welfare gains – it would be better placed to manage its economic future.

- **Russia's influence in its own region is under strain**. In Ukraine, always the prize for Putin, public opinion has turned decisively in favour of alignment with the EU. Concerned by these developments, other post-Soviet states are showing a renewed interest in a stronger, balancing Western vector to their foreign policy. The Eurasian Union will probably survive the economic strains and political anxieties that the present crisis has stoked, but it is unlikely to become the strong integrating project that Russia intends it to be.[99]

- **Russia's influence on the West has suffered severe damage**. Even among its sympathizers in Europe, Russia's reliability as an energy supplier has been cast into doubt – a concern that never arose during the Cold War. Further consequences could follow if the Russian ban on food imports is referred to the WTO or if Western sanctions escalate.

These failures mark the latest in a succession of Russian attempts to overcome the economic backwardness of a great power in an interdependent age. It has been a journey, so to speak, from Crimea to Crimea. It began when the Crimean War exposed Russia's weakness in 1856, impelling the country to introduce domestic reform and pursue integration into the international economy. The collapse of sovereign globalization following the annexation of Crimea in March 2014 leaves Russia in search of a new solution to its calculus of power and prosperity. Autarky is not an

[97] Even if the political will to implement major economic reforms returns, it will prove very difficult to implement given the resistant vested interests that have grown under sovereign globalization. This is especially the case in the crucial energy sector, which Putin has shaped in part to serve his globalization strategy.
[98] The Higher School of Economics in Moscow sets out this risk in a report discussed in 'Russia might lose ten years of development', *Vedomosti*, 6 April 2015.
[99] For the limits of Russian influence, see James Nixey, *The Long Goodbye: Waning Russian Influence in the South Caucasus and Central Asia*, Chatham House Briefing Paper, June 2012.

economic option but the West is no longer a political option. What choices does Russia now face in forging a modernization strategy and a foreign economic policy to support it?

One approach would be for Russia to focus on domestic prosperity and give up great-power assertiveness – or, to put it more palatably, to define 'greatness' in terms of the satisfaction of its citizens' needs. This way lies a vision of modernizing alliances supporting economic diversification and innovation. But Russia's current trajectory makes this less probable over time. The more likely choice, already evident, is to seek closer ties with non-Western economies, especially in Asia – that is, with relatively less, rather than more, developed countries. Such partners will be tough and pragmatic, more modern and less post-modern than the EU. As a veteran senior Russian policy official has noted: 'Everyone understands that Chinese investments in Russia will not be high. China will only invest in projects of interest to it and will not provide freely usable capital for Russian business. Only the West can provide this.'[100] Moreover, the relationship between Russia and China must contend with the latter's ambitions to extend economic influence into the post-Soviet space: the resources available for China's 'New Silk Road' will dwarf those allocated to the EU's Eastern Partnership programme.

Finally, what does Russia's experience tell us about globalization itself?[101] One major cause of Russia's strategic failure has been the EU's transformation from an entity vulnerable to division and influence into one with the legal tools to overcome this and itself pose a threat – as the Putin regime saw it – to Russian control of geopolitical 'space' through its economic attractiveness. Underestimated by most, the bureaucratic and legal processes to develop and implement the Eastern Partnership, the Third Package and similar measures have ground forward steadily – an exercise not so much of soft power as of 'slow strength'. An erosion of EU resolve might still undermine this, as Russia evidently hopes. Moscow's retaliatory ban on food imports may have been a daring throw of the 'influence' dice, extending to the West discriminatory trade practices it has long used with former Soviet states to impose costs and so exert pressure for a more accommodating policy.[102] But in this contest of rival versions of globalization, it is the orthodox Western one that is currently prevailing over the sovereign Russian one.

Russia's sovereign globalization presented a highly distinctive challenge to the international economic system. Could it be repeated elsewhere? While a full discussion is beyond the scope of this paper, we can specify the key condition that must be fulfilled for this to happen: disproportionate possession of a valued resource on which others are dependent, by a state that seeks to use this dependence to achieve non-economic goals. With the decline of Russia's own attempt to do so, it is now harder to envisage this condition being satisfied in a systematic way – although some have suggested that China's role in the global economy may offer such potential.[103] The fate of sovereign

[100] Remarks at the annual conference at the Higher School of Economics in Moscow on 9 April 2015.
[101] Until recently it was a commonplace that Russia 'ran rings' around the EU on energy policy. See Dieter Helm, 'The Russian dimension and Europe's external energy policy', 3 September 2007, http://www.dieterhelm.co.uk/sites/default/files/Russian_dimension.pdf.
[102] Russian agricultural interests have welcomed, and benefited from, these counter-sanctions. But domestic sectoral interests have played relatively little role in the formulation of Russian foreign economic policy, especially compared with the role of their counterparts in most Western countries.
[103] Some observers see China's reported blocking of rare-earth metal exports to Japan in 2010 as evidence of its readiness to manipulate the dependence of others on its supplies as an instrument of influence. Even in this case, though, market responses have reduced the political utility of China's disproportionate share of such metals – see 'Rare earths and China's self-correcting folly', *Financial Times*, 8 January 2015. Others suggest that China could use its US debt holdings to exert leverage; but such an approach would entail significant financial risks for China. Economic sanctions are a special case of a country, or group of countries, seeking political goals through the deprival of markets or

globalization, then, encourages pessimism about Russia but encourages optimism about globalization.

No single master key can unlock a reality as complex as Russia.[104] But the rise and fall of Russia's sovereign globalization illuminate key dynamics of the Putin project and its international consequences. A recent landmark study of Russia's relationship with international investors notes that 'most conflicts in Russia are actually about power rather than creating value and profits'.[105] As a general truth about Russia's political economy, this might serve as an epitaph for the audacious failure of sovereign globalization.

withholding of supplies. The most systematic attempt to exert political pressure involving a valued resource – OPEC's use of the 'oil weapon' – gave way in due course to the cartel-like pursuit of better commercial terms rather than specific political goals.

[104] For example, some might argue in favour of the role of rent-seeking by domestic interests. Clearly, some individuals and groups have benefited handsomely, especially in the natural resources sector. But what stands out is how far Russia under Putin has departed from a 'normal politics' of globalization. Domestic interests have largely followed, not determined, policy; rather, it has been the pursuit of power, at least as much as of prosperity, that has shaped policy.

[105] James Henderson and Alastair Ferguson, *International Partnership in Russia* (Basingstoke: Palgrave Macmillan, 2014), p. 230.

About the author

Nigel Gould-Davies is a lecturer and programme co-ordinator in international relations at Mahidol University International College in Thailand. He taught at Oxford University before serving in the Foreign & Commonwealth Office, and later worked in the international energy industry. He writes and consults on international relations, post-Soviet affairs and energy issues.

Acknowledgments

I would like to thank Guy Gould-Davies, Fiona Hill, Iikka Korhonen, Andrew Monaghan, James Nixey, Jo-Anne Pugh and two anonymous reviewers for their comments on an earlier draft.

Independent thinking since 1920

ISBN 978 1 78413 104 3

This publication is printed on recycled paper.

The Royal Institute of International Affairs
Chatham House
10 St James's Square, London SW1Y 4LE
T +44 (0)20 7957 5700 F +44 (0)20 7957 5710
contact@chathamhouse.org www.chathamhouse.org
Charity Registration Number: 208223