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The review provides a detailed analysis of main trends in Russia's economy in 2011. The paper contains 6 big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and credit spheres; financial sphere; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts.

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## **Socio-political Context in Russia in 2011**

### **1.1. Economics and Politics in 2011: the Global Crisis and the Quest for a New Growth Model**

#### 1.1.1. The Results and Lessons of the Year 2011

Russia's socio-economic development in 2011 was determined primarily by two factors: the forthcoming elections on the one hand, and the global economic crisis on the other. Although they considerably differed both by the force and the vectors of their impacts, it was nevertheless these two factors that had predetermined the behavior of all the subjects involved in the economic and political life.

So far, the global crisis has had no negative influence on the Russian economy (see *Table 1*). We may point to three main mechanisms through which the world economy is influencing contemporary Russia: demand for exported commodities; access to investment resources (direct investments and credits); and demand for Russian securities on the stock market. Of course, the slow rate of growth of the world economy was bringing down the demand for Russian exports. However, the prices for the basic exported commodities remained high, although the rate of their growth was lower than in some of the pre-crisis years. Russia's stock market is very vulnerable to the effects of external shocks, which was confirmed by the events of August–September 2011, but so far it has not been playing a prominent role in ensuring this country's economic growth. The volume of external borrowings attracted by the corporate sector continued to be on the rise, thus surpassing its pre-crisis level. At the same time, the understanding of the lengthy character of the global crisis, with its unpredictable geo-political and geo-economic outcomes, has had some impact on the formation of Russia's economic policy in the medium term.

The standard mechanisms whereby elections influence one or other society's economic life are the increasing uncertainty of future economic policy and the equally increasing populism of any authorities striving to be reelected. Both mechanisms have turned out to be effective for Russia in 2011, in spite of the fact that the probability of power remaining in the hands of the ruling party and its leaders seemed to be exceptionally high to everybody – in other words, they did not need any large-scale financial investments in order to ensure public support. However, this fact did not prevent the country's leadership to declare their intention to make some big investments, in the next few years, mostly in the public welfare sphere and the power structures.

Over the past year, Russia demonstrated a sufficient stability of her economic development. Economic growth remained moderate and, on the whole, quite natural for a country with a medium level of economic development – higher than in Germany but lower than in China. In formal terms, the macroeconomic parameters remained favorable – the budget by that year’s results was executed with a surplus of nearly 1% of GDP, while the inflation rate dropped to its historic low for the entire 20-year period of Russia’s post-communist existence. In the sphere of monetary policy, the RF Central Bank managed to switch over to a floating currency exchange rate and inflation targeting. This has been the most important institutional achievement of the past decade.

*Table 1*

**Russia’s Macroeconomic Indices Compared to Those  
of Some Other Countries (2010–2011)**

2010					
Country	GDP growth rate, %	Unemployment, %	Inflation Dec./Dec., %	Budget deficit (-), % of GDP	Government debt, % of GDP
<b>Russia</b>	<b>4.3</b>	<b>7.5</b>	<b>8.8</b>	<b>-3.2</b>	<b>9.2</b>
USA	3.0	9.6	1.7	-10.3	94.4
EU, including	1.8		2.5	-6.4	79.8
France	1.4	9.8	1.7	-7.1	82.3
Germany	3.6	7.1	1.9	-3.3	84.0
UK	1.4	7.9	3.4	-10.2	67.7
CIS, including	4.6		8.9	-2.6	14.5
Kazakhstan	7.3	5.8	8.0	1.5	10.7
Belarus	7.6	0.7	9.9	-1.8	26.5
Ukraine	4.2	8.1	9.1	-5.7	40.1
China	10.3	4.1	4.7	-2.3	33.8
Brazil	7.5	6.7	5.9	-2.9	66.8
India	10.1	9.3	9.5	-8.4	64.1
2011					
<b>Russia</b>	<b>4.2</b>	<b>6.7</b>	<b>6.1</b>	<b>0.8</b>	<b>11.7</b>
USA	1.5	9.1	2.5	-9.6	100.0
EU, including	1.7		2.8	-4.5	82.3
France	1.7	9.5	2.1	-5.9	86.8
Germany	2.7	6.0	2.2	-1.7	82.6
UK	1.1	7.8	4.5	-8.5	72.9
CIS, including	4.6		10.2	-0.6	14.9
Kazakhstan	6.5	5.7	9.5	1.8	12.9
Belarus	5.3	0.7	108.7	-0.7	46.3
Ukraine	4.7	7.8	10.7	-2.8	39.3
China	9.5	4.0	5.1	-1.6	26.9
Brazil	3.8	6.7	6.3	-2.5	65.0
India	7.8	9.7	8.9	-7.7	62.4

At the same time, Russia’s macroeconomic stability remains extremely vulnerable. It rests on high budget revenue generated by high oil prices, which at present are staying at its historic high and in terms of constant prices are comparable with the level of the late 1970s – early 1980s. The policy of increasing budget spending obligations, which implies that these ‘situational’ incomes become guaranteed, is very dangerous – as demonstrated by the experience of the USSR in the 1980s. Meanwhile, the non-oil deficit of the federal budget in 2011 amounted to approximately 10% of GDP, while the budget deficit amounts to approximately 4.5% of GDP with the price of oil is on its average level of the past decade (conditionally guaranteed level).

The year 2011 saw a surge in capital outflow, which exceeded \$ 85bn. That outflow was produced by a combination of different factors – an unfavorable investment climate, demand

for foreign assets on the part of some big Russian investors, increasing competition for capital with the developing markets in Asia и Latin America, the global crisis pushing up demand for placements in a reserve currency (notwithstanding the economic difficulties faced by its issuer country), and the political risks of the pre-election period. However, that systemic problem needs to be studied in-depth, so that a number of acceptable solutions could be found. Its complexity results specifically from its multi-aspect nature involving a variety of closely linked processes, so that in reality it can be broken down into several problems, each of which requires its own individual set of corrective measures.

An economic crisis is always a starting point for modernization. Since the accumulated reserves allowed the Russian authorities to avoid bankruptcies and enforced structural modernization, they began to elaborate an agenda for ‘modernization from above. In 2011, the discussion of the general principles of promoting modernization once again came to the fore (i.e., the discussion of a new economic growth model) and some targeted innovation development projects were initiated. The latter have taken shape as specifically oriented territorial enclaves (Skolkovo, Tomsk) or as some separate sectors for scientific and technological development (information and communication systems, outer space exploration, nanotechnologies, etc.). Two commissions on modernization and technological development were functioning simultaneously – one under the RF President, and the other under the Chairman of the RF Government.

However, modernization cannot be carried on through directives alone – even if these are approved at the topmost level. Modernization (at least in its present form) requires competition – both between economic agents and institutions. In this respect, two important decisions taken in 2011 in the sphere of foreign trade may become relevant modernization factors – namely Russia’s accession to the WTO and the breakthrough achieved in post-Soviet integration (the establishment of the Customs Union and the conclusion of the agreement on the creation of the Common Economic Space between Russia, Belarus and Kazakhstan). The accession to the WTO will intensify competition for Russian producers, while the creation of the Customs Union and the Common Economic Space will supplement competition between commodities with competition between institutions.

A characteristic feature of the year 2011 has been rapid politicization of the population, which could be clearly observed in Russia and elsewhere across the globe. There were anti-government riots in the Arab world, the *Occupy Wall Street* movement in the developed countries, and the growth of political activism in Russia in late 2011 and early 2012. Evidently, the causes and mechanisms of politicization are region-specific in each case, but their coincidental timing cannot be overlooked. So far we can only tentatively assume that the intensity of political activity in the world will be increasing alongside the development of the global economic crisis (which does not necessarily mean its intensification).

One of the dangers that in this connection may threaten Russia’s economic policy will be an increasing ‘budgetary populism’ in addition to political populism. However, if the latter presents no danger from the point of view of ensuring this country’s long-term stability, the former, while pursuing the noble goals of protecting the welfare of the people and some selective social groups (the military, budget funding recipients, pensioners, etc.), may in the end produce a severe economic and political crisis. At the same time, while the outer world is plagued by the crisis but this country has in store some substantial resources accumulated thanks to its government’s recent conservative policy, the risks fraught in ‘budgetary populism’ may become greater in response to a sudden upsurge of social and political issues.

### 1.1.2. The Global Economic Crisis: Its General and Specific Features

The global economic crisis that began in 2008 is systemic and structural in its nature. In terms of its basic parameters it is comparable with the crises of the 1930s and 1970s. We can point to a number of fundamental features of such a crisis which, in their turn, may predetermine the factors and preconditions that will help to end it.

*First*, a structural crisis is determined by the presence of some serious misbalances in the organization of economic life. These are produced by fundamental technological shifts – namely, the emergence of some fundamentally new technologies (termed *a new technological way* by a number of economists). That is why the exit from the crisis is associated with a transformation of the production bases of the leading countries through implementing new technologies. The creation of a new technological base will be playing the same core role in the future development as the one that way played in the mid-20<sup>th</sup> century by large-scale machine industry, and after the 1970s – by microelectronics and computer systems.

A crisis implies a technological renewal which transforms demand for many industrial and consumer commodities, and especially investment and fuel and energy products. Naturally, this transformation is reflected in the prices for a majority of market commodities, and this implies an achievement of some new balances of prices and leads to a change in the political configurations.

*Second*, the world accumulates a variety of serious geo-economic and geo-political misbalances. The economic and political potential of each individual country develops slowly, but then comes the moment when a qualitative leap takes place, and so it becomes necessary to switch over to some new system of balances. In contemporary conditions one of the most evident examples of such misbalance has become a change in the distribution of roles between developed and developing (or rapidly developing) countries. How to find a trajectory of a better balanced growth (in terms of savings against investment, exports against domestic consumption, revenue against expenditure) – this is the key issue faced by many developed and developing countries in Europe, America and Asia.

Thus, and *third*, a structural crisis becomes a global one. It spreads to all the leading countries; and in contemporary conditions, globally coordinated efforts will be needed in order to finally overcome it. In other words, *decoupling* (development along different trajectories) – something that so much spoken about back in 2008 – has been effectively taken off the crisis agenda. By now there have remained practically no relevant countries that have not experienced at least some of the crisis-linked process, with a varying degree of intensity. Thus it becomes even more important to ensure the participation of all those countries in working out global anti-crisis measures.

A global character of the crisis by no means rules out the possibility of its movement across the world. Depending on its specific phase, crisis phenomena may be concentrated in some specific regions or countries. Thus, the crisis originated in the USA and then spread on to Europe and a part of Asia; now it is centered mainly in Europe.

*Fourth*, a structural crisis is conducive to the formation of some new currency configurations – a new world currency emerges (or a number of new world currencies). In the 20<sup>th</sup> century this occurred as a fundamental change in the role of gold, the prominence of the US dollar, and after the 1970s – as the increasingly bi-currency character of international business settlements. In the present situation there has emerged the issue of the future prospects of the US dollar, the euro and the yuan. And there has also emerged the issue of whether or not regional reserve currencies should play a more prominent role in the future.

*Fifth*, a structural crisis gives rise to a serious intellectual challenge. It becomes necessary to work out a new agenda of economic and political (and also generally social) analysis. The crisis transforms into a powerful stimulus to rethinking the existing economic and political doctrines both on a global scale and in terms of a given country.

This is specifically true with regard to economic doctrines. Economists must suggest some new approaches to analyzing the economic processes, and first of all to regulating socio-economic life. After the Great Depression the world was transformed into a Keynesian and socialist (*etatiste*) one. After the experience of stagflation those ideas gave way to deregulation and liberal democracy. The new economic model must not only provide answers to the most urgent current questions, but to express these answers in a more distinct and understandable form.

This intellectual challenge become especially important in the early phases of a structural crisis when it is being countered with by means of applying those ideas and recommendations that had proved to be effective over the preceding decades of smooth economic development (with occasional bubbles being the only trouble). It takes some years to finally bring home the realization that to apply the traditional anti-crisis policy in a new setting is quite unreasonable and even harmful.

*Sixth*, a structural crisis lasts for approximately a decade – a period termed ‘*a turbulent decade*’. It means that the crisis period can be broken up into separate stages, each marked by the domination of some specific problems originating in a given sector or region. But at the same time this means that no single feature can serve as a criterion for judging whether the crisis is further deepening, or if its end is near. This is also true with regard to recession (a crisis does not begin with a recession, and by no means is limited to it), as well as to the fluctuations of the stock market, and to any other parameters.

*Seventh*, the struggle against a crisis is associated with applying some drastic but sometimes inadequate anti-crisis measures. On the one hand, this has to do with the acuteness of the structural problems, the overcoming of which requires certain (sometimes great) economic and social sacrifices. On the other, the aforesaid ‘intellectual unpreparedness’ for a structural crisis – that is, attempts to solve new problems by applying old remedies – produces some additional problems, thus often resulting in a further aggravation of the crisis – its economic and sometimes even political aspects. Thus emerges the issue of an *exit strategy* (the strategy for discontinuing the anti-crisis functioning mode), and so additional time is required not only for overcoming the crisis but also for eliminating the consequences of the anti-crisis measures.

All these factors taken together can explain the fundamental difference between a systemic crisis and a cyclical one. A cyclical crisis recedes with time; it does not imply the necessity to alter a current policy but ends by itself when the economic bubble emerging during a boom period disappears. A systemic crisis, on the contrary, requires a significant transformation of the old economic policy on the basis of a new philosophy of economic life. In other words, structural problems predominate over cyclical ones.

However, the current global crisis has a number of specific features that must be taken into account when elaborating an anti-crisis policy and a viable model of socio-economic development. Many of its specific features have been produced by the technological achievements of the modern era – the development of information and communications technologies that

have made the world flat<sup>1</sup> and so make it possible for businesses to rapidly shift their activities from one region or sector to another, carry on instant transactions, and to start and terminate entrepreneurial projects. The increased dynamism gives rise to some new phenomena and the resulting new economic and political conflicts.

Since the current structural crisis is evolving in the era of globalization (or, more precisely, during a qualitatively new phase of globalization), its significant features are global structural imbalances. First of all, these are imbalances between developed and developing countries, in particular between the USA as a focus of spending and consumption, and China as a focus of money saving and production. The term *Chimerica* (*China + America*) suggested in 2008 by N. Ferguson<sup>2</sup> has become a symbol of the issue of global imbalances. As a result, the process of modern globalization produced a regime that is opposite to the model typical of the turn of the 20<sup>th</sup> century: if a century ago capital was moving from the center (the developed countries) towards the periphery (the then emerging markets), now it is the developing markets that have become the savings centers, and the USA and other developed countries are predominantly the consumers of commodities manufactured in the developing countries.

The category of structural imbalances also includes the growing controversies *between short-term and long-term interests of companies* that manifest themselves in a conflict between capitalization and production growth. In recent decades the attention of shareholders and managers alike was focused in the main on a company's capitalization, which was viewed as the principal indicator of its commercial success. The possibility to easily get rid of stocks (much easier, in fact, than in the times prior to the information revolution) is yet another argument in favor of rapid capitalization growth – a goal that may be quite contrary to the goal of ensuring a company's long-term stability. Consequently, that criterion becomes the main one when estimating management efficiency and elaborating a corporate bonus policy.

Meanwhile, the goal of maximum capitalization comes into conflict with the real foundation of socio-economic progress – growth of labor productivity. It is, of course, linked to capitalization growth, but only in the final analysis. However, shareholders must receive annual reports, and attractive annual reports and current capitalization growth are produced by factors other than those that ensure productivity growth. Nice reports require mergers and takeovers, because asset growth is conducive to capitalization growth. Naturally, it is not advisable to shut down outdated enterprises, because this will result in a lower capitalization level in a current period. As a result, many big industrial corporations continue to keep old inefficient production entities going.

A systemic crisis always implies the emergence of a *new regulation model*, including a basically altered economic role of the State. The Great Depression of the 1930s led to a dramatic expansion of state interference in the economy; the crisis of the 1970s produced deregulation. At the onset of the current crisis, the theme of an inevitable departure from economic liberalism and a return of Big Government actively interfering in society's economic life once again gained popularity. However, there also occurred a rapid realization of the fact that that crisis could be equally explained both by 'market failures' (excessive deregulation) and by 'government failures' – its ineptitude in ensuring stability of economic growth. Gradually, it was becoming clear that government regulation was indeed necessary, but primarily in the sphere of financial markets. In fact, it was the financial sector that had first introduced those institu-

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<sup>1</sup> Friedman T. *The World Is Flat. The Global World in the Twenty-First Century*. L.: Penguin Books, 2006.

<sup>2</sup> Ferguson N. *The Ascent of Money: A Financial History of the World*. L.: Allen Lane, 2008.

tional innovations that initially produced an unprecedentedly high rate of economic growth that later gave way to an unprecedented crisis. It is a financial crisis (encompassing both the private and public sectors) that generated the current economic problems, and the government's task is to make it a priority to overcome that crisis.

Another specific feature of the new regulation model is that it must necessarily be created as a supranational – if not a global one. There is no sense in carrying on regulation on a national level alone in the presence of modern information and communications technologies. However, it is very difficult to create supranational regulatory institutions. There exist as yet no mechanisms for ensuring their functioning, including universal decision-making mechanisms.

When developing a modern regulation model, one must give consideration to the qualitatively new global economic process that sometimes is called *financialization*<sup>1</sup>. There exist several types of markets (and exchanges) in the world: the monetary market (the stock market), the currency market, the commodities market. Until recently, they functioned quite independently of one another, were developing under different laws, and were operated by different agents (specializing in a given type of markets). Now we are witnessing the processes of their coming together: the markets have begun to influence one another, and capital is flowing between them. As a result, the logic of pricing the relevant products is undergoing a certain transformation. On the one hand, this seriously hinders the analysis and forecasting of further development of the situations on these markets and throughout the entire world economy. On the other hand, economic agents have obtained some new instruments for their functioning, including for hedging risks. From the point of view of the specific issues of the Russian economy's development, especially interesting is the transformation of oil from a typical product traded on a commodities exchange, whose price is determined by the demand/supply ratio, into a financial market instrument, whose price is influenced by speculators in oil futures, and through that mechanism – also by currency speculators. This significantly increases the degree of uncertainty with regard to the price of oil as one of the most important factors applied in forecasting the prospects of the Russian economy.

The current global crisis is evolving against the backdrop of a *demographic crisis* that has spread to a greater part of the developed world and also to some developing countries. That crisis, in its turn, has given rise to two sets of problems, which must be solved in order to launch a trajectory of stable development. On the one hand, there is the issue of the mechanisms of economic growth, because until now such growth has always implied an increase in population. On the other hand, developed countries, having succeeded in ensuring a high level of social welfare, are now faced with increasingly grave budgetary problems. The social welfare load per worker was constantly increasing throughout the entire 20<sup>th</sup> century, and in the situation of a demographic crisis this pressure become fraught with very high danger for financial stability – and consequently, for growth. In 2011, European countries became acutely aware of this circumstance; for them, the exit from the macroeconomic crisis will mean a significant restructuring of their budgetary obligations. Russia will be faced with similar problems – not only in the event of a substantial decline in oil prices, but even if these prices remain at a stable level.

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<sup>1</sup> This term was used by UNCTAD in its Trade and Commodity Report (2009), which contains a chapter entitled The Financialization of Commodity Markets. Also see Gaidar Ye. Golovokruzhenie ot uspekhov. [Dizzy from Success.] // Ekonomicheskaja politika [The Economic Policy]. 2008. No 3.

This situation has pushed to the fore the task of restructuring all the branches of the social welfare sphere – first of all the educational, public health care, and pension systems. Here we mean specifically structural reforms and the elaboration of new models for the functioning of these sectors, and not only the necessity to save budget resources. It should be emphasized that a financial crisis is a reflection and manifestation of a structural crisis. It can be overcome through in-depth reforming of the relevant sectors and bringing them in conformity with the new technological base and new social structure of postindustrial society.

It will be even more difficult to find solutions to the most pressing social problems because a prominent feature of the current crisis is that the leading developed countries have reached critical levels of sovereign debt. In part this is the result of the irresponsible financial policies of the previous decade, and in part – the consequence of the anti-crisis struggle that involved some measures designed to create budget incentives. The undermined trust in the financial situations and policies of the leading countries, a drop in the credit rating of the USA that has hit its 50-year low, the decline or threat of decline in the credit ratings of the world leaders and their global banks have all been pointing to a profound crisis of confidence in the existing economic and financial institutions. The key to exiting from the global crisis in the foreseeable future will be reestablished confidence.

And finally, the current crisis has *some political consequences*, although so far these have not yet acquired a more or less radical character. The events of 2010 – 2011 have made it possible to define some of these repercussions.

First, there has occurred a general shift to the right in the political mood of a number of important countries: center-right parties have won parliamentary elections in Germany, the UK, Poland, Spain and Portugal. The Republicans have significantly strengthened their representation in the US Congress.

Second, Europe has embarked on an experiment of sorts designed to find an optimal anti-crisis political anti-crisis model – somewhere between a technocratic government that lacks a voters mandate (Italy, Greece) and a party government winning an election (the new center-right governments in Spain and Portugal).

Third, there is the deepening conflict within the US political elite that has already triggered a downgrade of the USA's sovereign rating, previously deemed to be impregnable. The choice of an economic model (between raising taxes and cutting budget expenditure) in that country has turned to be a purely political problem whose acuteness is further enhanced by the approaching presidential election of 2012. In such a situation, it is only natural that no simultaneous movement in two directions in order to reduce budget deficit becomes possible.

Fourth, numerous large-scale protest actions have taken place – mainly in developed countries. So far, however, such mass protests have had no significant impact on the formation of the governments' economic and political courses. In any event, in spite of their openly leftist (and sometimes extreme left) slogans, it was the right parties that won last year's elections.

### 1.1.3. Russia's Economic Policy: the End of the Old Model

So far the crisis has had only a limited influence on the situation in Russia. Naturally, the rate of economic growth became slower, thus making it impossible to set the goal of doubling this country's GDP over the next decade. However, the doubling of Russia's GDP is by no means a task of critical importance. It is much more important to ensure the realization of progressive structural shifts that can serve as a foundation for the modernization of the Russian economy and policies, including the goal of making this country less dependent on the

fluctuations of the world economic situation. That is why the global crisis has revived discussions on the possible ways of Russia's modernization. In late 2010 – early 2011 Vladimir Putin set for the experts' community the task of elaborating the possible scenarios and this country's development strategy until 2020.

Strictly speaking, there exist two sets of causes that have put to the fore the need to elaborate a new strategy. First, there are the consequences of the global crisis which, as noted earlier, has made it necessary to rethink the current socio-economic policy. 'You never want to see a serious crisis go to waste,' said White House Chief of Staff Rahm Emanuel, and these words very accurately describe the goals that the governments of developed countries are now faced with.

Secondly, there also exist some specifically Russian causes for the renewal of the economic course. Last decade's economic policy model was shaped by the powerful intellectual, political, and even psychological impacts of the post-Communist transformation of 1991–1999 in general, and the 1998 financial crisis in particular.

### ***The Economic Policy of 1999–2009: The Demand Economy***

The principal features of the economic policy model applied over the pre-crisis decade are as follows:

- to ensure political and social stability as a *sine qua non* condition;
- to gradually increase the role of the State as the source of that stability. This role has become manifest in at least three forms: state property growth; growth of budget revenues and expenditures (in absolute terms and as a share of GDP); compensation for the insufficient trust in financial institutions through developing state financial structures (which was typical of the countries involved in catching-up industrialization);
- to maintain a well-balanced budget against the backdrop of increasing budget revenues and expenditures. However, this situation is unstable in face of a large-scale budget expansion. Any interruption (or even a significant slowdown) in revenue growth will result in a budget deficit;
- to implement a policy aimed at moderating the process of the currency exchange rate's strengthening alongside a high inflation rate and high interest rates. This was viewed as a source of incentives for domestic producers;
- to grant broad access of state, quasi-private and private companies to the international capital market. The high credit value inside the country was counterbalanced by the possibility to borrow on the world market;
- to make the government a major source of demand in the national economy. First of all, this helped to maintain demand on the part of the medium-income and poor strata of the population that depended on the state budget: pensioners, unemployed, government employees and the military, as well as the employees of state corporations attached to them. A prominent role was played by the funding allocated to the power structures – both for the upkeep of the military and arms purchases. It was further enhanced by the evolution of the global crisis in 2008–2010;
- to limit government investments in infrastructure. Being aware of the high corruption level in that sector, the government was very prudent in its policy with regard to it – in contrast to social expenditures;

- to support some big and inefficiently functioning enterprises – as a preventive factor against social destabilization. This explains the political and administrative restrictions imposed on dismissal of workers engaged in inefficient production;
- to limit the administrative reform to constant redefining of the range of functions of various state bodies alongside a refusal to implement any fundamental alterations in the state administration system;
- to raise taxes in order to ensure macroeconomic and social stability.

This type of economic policy inevitably has a number of natural consequences. An economy based on government demand is, in principle, more inclined towards preserving and supporting monopolies – as well as inflation. Monopolies ensured stability of the economic and political situation – although at a heavy price: the quality of goods and services was low, while the rate of inflation increased. The predominance of government demand was mitigating the need of economic agents in a lower inflation rate because government investments had priority over private ones, and it is for the private investor that a low inflation rate is more important as a precondition for lowering interest rates. The government's decisions were becoming increasingly individualized (or targeted) – it granted privileges as incentives for certain types of investors and producers in order to compensate them for the increasing taxes, high interest rates and administrative barriers. In effect, that policy can be described as a *demand economy*.

***The Macroeconomic and Structural Limitations of the Model Existing in 1999–2009 (the Demand Economy) Necessitating the Elaboration of a New Growth Model***

*Budgetary issues.* Increasing budget expenditures coupled with a halt in the growth of oil prices resulted in budget deficit. The Russian economy suddenly became very vulnerable to external shocks due to the unpredictable behavior of oil prices.

At the same time, the Stabilization Fund's dual role (that is, the role of the government's reserves generated by the super incomes from oil exports) in dealing with the strategic tasks of Russia's economic development explicitly manifested itself. On the one hand, the reserves helped to avoid budget populism and money supply sterilization, simultaneously serving as a safety cushion in a crisis situation. On the other hand, the presence of substantial reserves in face of a crisis became a powerful factor of modernization slowdown, because social tension was released at the expense of a delay in the restructuring of bankrupt enterprises. A similar situation was observed in the banking sector.

*A monetary policy,* based on suppressing the process of strengthening the ruble's exchange rate in nominal terms at the expense of an accelerated inflation rate, was also no longer effective in providing solutions to the existing problems. The ruble's exchange rate was strengthening, and in real terms it had long ago surpassed its 1997 level, amounting by the time of the onset of the crisis to 65% of its rate in nominal terms (25% in 1999). In such conditions the exchange rate of the national currency could not seriously protect domestic producers from foreign competition<sup>1</sup>. At the same time, a persistently high inflation rate produced two-digit interest rates on credits, thus making it impossible for domesticity businesses to obtain much-

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<sup>1</sup> As calculated by A. VedeV, approximately 75% of Russia's domestic demand produces inflation and growing imports, and only about 25% of it promotes domestic production. (VedeV A. et al. *Na puti k deshevym den'gam*. [On the Way to Cheap Money.] / Bank of Moscow's Strategic Research Center. 2010. June).

needed resources and creating obstacles to the development of the housing mortgage sphere. Previously, that situation had been in part relieved by availability of cheap foreign credits. Now, in crisis conditions, some serious problems arose. Further growth of the Russian economy will require the emergence of a domestic credit system which, in its turn, requires a low inflation rate.

*The pitfall of insufficient competitiveness* is contemporary Russia's most dangerous structural challenge. If ten years ago this country had average-quality institutions and a qualified and cheap labor force, now the situation has undergone a fundamental change. High labor cost coupled with weak institutions and low labor productivity limit opportunities for increasing industrial exports and satisfying the growing domestic demand by domestic output. In the past decade labor cost was growing at a stable rate, while institutions were stagnating or even somewhat deteriorating<sup>1</sup>. Naturally, both these indices become important only when set against similar indices in the countries with comparable levels of economic development that are competing with Russia for attracted capital and production capacities. In terms of per capita GDP Russia has been rated first among the most dynamically developing markets; in terms of business climate (*doing business*) its position, on the contrary, became worse – now it has joined the 'backward' group together with Brazil, India and Indonesia whose per capita GDP is far below Russia's. So this country is becoming relatively less attractive in terms of investments – for foreign and domestic capital alike. Among other things, this is evidently one of the reasons for the recently started capital outflow from Russia.

In other words, Russia has found itself in a structural 'trap' created by the combination of (relatively) expensive labor and (relatively) bad institutions. Quite understandably, the competitive sectors in such a situation will be services and raw materials production (exploitation of natural resources) which, in fact, are currently dominating Russia's national economy.

There exist two ways out of that trap: either the quality of institutions must be improved to match that of labor, or labor quality will deteriorate to match that of institutions. Russian economists, for evident reasons, prefer to discuss the issues of improving the quality of institutions. However, the scenario of labor deterioration cannot be entirely dismissed, either. It is precisely in this direction that today's Russia is being pushed by the current migration trends.

*The demographic crisis* represents one more systemic problem that has lately acquired some new outlines.

One facet of this crisis is the natural population decline that can be only somewhat slowed down by the government's measures designed to stimulate natality. Besides, Russia's able-bodied population has recently started to show a downward trend. There exists an opinion that the demographic problem can be solved by means of external migration. However, in reality modern migration may only provide a solution to the issue of quantity, while only aggravating the qualitative problem. Migration is flowing into Russia from countries with lower levels of development and is represented by a population with a much lower demand for political and human potential development institutions (first of all in the spheres of education, health care and science). Thus, the issue of improving the quality of Russia's institutions and human capital becomes hopeless.

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<sup>1</sup> The issue of institutions' quality was considered, in particular, in: Freinkman L., Dashkeev V. *Rossia v 2007 godu: riski zamedlenia ekonomicheskogo rosta na fone sokhraniaiushcheisia institutsional'noi stargnatsii*. [Russia in 2007: the Risks of Economic Growth Slowdown Against the Backdrop of Persisting Institutional Stagnation] // Voprosy ekonomiki [Issues of Economics]. 2008. No 4.

Its other facet is the rapid spread among the creative class of an *exit strategy* based on the desire to start a new life in another country. This is a rather new phenomenon requiring some serious consideration. It is probably for the first time in Russian history that this desire to emigrate is associated with a markedly improved well-being level rather than with its worsening. Globalization coupled with rapidly improving domestic living standards have produced a rapidly growing well-educated and mobile class consisting of individuals who feel competitive on the world labor and capital market. There is a demand for them in the most developed countries of the world, and they may easily move from country to country. As a result, Russia has to compete for her own creative class – as if it has already become international property.

This situation has given rise to some fundamentally new conditions in terms of institutional environment improvement. Members of the creative class, in fact, no longer need better institutions in their country of origin because they can get all the necessary services (a political system, education and public health care) whenever they want. But without a demand for modern institutions there will be no supply. So this has become the most cumbersome structural obstacle in the way of Russia's modernization.

*The entrepreneurial climate* is yet another serious limitation of the existing economic growth model. If one accepts the hypothesis that the entrepreneurial climate is more favorable in countries with higher levels of economic development, Russia will represent a noticeable exception: here, the quality of the relevant institutions is much lower than in countries with a comparable per capita GDP level. Out of about 200 countries of the world, Russia is at 50<sup>th</sup> position by its development level, while in terms of institutional quality it is among the second hundred. According to the latest ratings and opinion polls among entrepreneurs, the problem of gaining access to infrastructure has recently become more acute.

Rapidly rising oil prices coupled with a growing economic activity of the State during a certain phase were neutralizing the entrepreneurial climate's negative influence on economic growth. Meanwhile, Russia has found itself at the very bottom of the international competitiveness scale by a number of individual indicators. These are, first of all, the customs regulation; the procedures for starting and closing down a business; the construction business; and investor protection. Besides, serious limitations are imposed by the existing status of basic (law enforcement) and financial institutions.

Russia's *spatial development* serves as another structural limitation to increasing its competitive capacity. Because of the uneven territorial development and insufficient responsibility of regional and municipal authorities for the situations in their own territories the federal budget bears an excessive budgetary load, while the regions are not interested in seeking new resources. The mechanism for appointing heads of regions has become an additional factor for them to lobby for redistribution of federal funding in their favor. In absence of proper incentives for territorial consolidation of human and financial resources, as well as any mechanisms for such consolidation, the financial pressure exerted by the regions on the federal government will be constantly renewed and thus give rise to an inevitably unreasonable allocation of budget expenditures.

#### 1.1.4. The New Growth Model: The Supply Economy

The exhaustion of the potential of the growth mechanisms applied in 1999–2008 in combination with the challenges posed by the global crisis have put forth the question as to the need to generate a new economic growth model. The new growth policy must be able to put forth some mechanisms that will enable Russia to become successfully competitive in the struggle

for human and financial resources (human and investment capital) that is currently going on a global scale. Below we are going to look at the key components of the new growth model.

**Budgetary policy.** The major directions of the budgetary policy are: to reduce the budgetary load relative to GDP; and to lower the budget's dependence on the fluctuations of the world market situation.

The achievement of these goals will be helped by the reestablishment of the rigid budget rule: budget estimations must be based on a fixed oil price level that does not depend on any political negotiations but instead is geared to, say, a decade's average price. In other words, budget rent-generated revenue must be guaranteed with a high degree of probability. If it becomes necessary for expenditures to exceed the amount of revenues calculated on the basis of that assumption (structural revenues), the government must raise taxes or borrow money – and these must be ruble-denominated loans. Their aggregate sum must not exceed 25% of GDP. If oil prices go above the estimated decade's average, the surplus revenues must be transferred into a reserve fund and by no means be spent on current consumption even if there occurs a parallel government debt growth.

Budgetary policy needs to resort to a structural maneuver towards increasing the investment and innovation-oriented (on human capital development) budget expenditures, while simultaneously cutting social welfare expenditures (through expanding the regions' powers) and providing funding to the power structures.

At the same time it is necessary to optimize budget expenditure. The adoption, in recent years, of the laws on autonomous and budget-funded institutions that have significantly transformed their status and separated their obligations from budget obligations can be regarded as only the first step in the direction of budgetary network rationalization. It is important to define more precisely the role of the Stabilization (or Reserve) Fund in order to prevent the use of its resources for the support of inefficient enterprises.

Any further alterations in the tax system must be brought to a minimum, with the exception of those that deal with the expansion of the revenue base of regional and municipal budgets. However, here we mean expansion of the tax powers of the sub-federal bodies of authority rather than the redistribution of the existing tax revenues.

**Monetary policy.** It is necessary to lower the inflation rate to a level approximately equal to or slightly exceeding the index typical of developed countries – that is, about 5%. This implies a continuation of the policy of modified inflation targeting and a refusal to artificially keep the ruble's exchange rate within an established currency corridor – when the monetary authorities level down its fluctuations. The operations on the monetary market will play a more prominent role in the formation of monetary policy, and crediting of the economy will be further developed by means of listing high-quality securities of domestic issuers.

A separate issue that deserves elaborate consideration is the prospect of making the ruble a regional reserve currency. The ruble has some advantages as a regional currency (these are, first of all, the impressive size of the Russian economy and the gravitation towards it of the neighboring countries), as well as some serious limitations (a resource-based economy implies an increased volatility of the national currency exchange rate). It would be feasible to prepare a special program (a system of measures) aimed at strengthening the ruble's international position.

In this connection there arises one important task – to create in Russia an international financial center. The center's goal will be to ensure appropriate institutional conditions for developing a national financial system and increasing the ruble's competitive capacity as a re-

gional reserve currency (this will also involve increasing the demand for the ruble as an instrument for carrying out financial transactions).

The monetary policy measures are closely associated with the issues pertaining to the organization of *financial markets*. Here the main directions can be described as follows: toughening the requirements to banks' capital; the introduction of *International Financial Reporting Standards* (IFRSs); the development of a special program designed to promote competition in the banking sector (instead of demonopolization); macroprudential supervision of banks and system-forming non-banking institutions; development and implementation of special programs aimed at training the population in dealing with financial issues.

***Development of the entrepreneurial climate and promotion of the activity of private entrepreneurs.*** With regard to that sphere, it is important to focus efforts on the least favorable components of the entrepreneurial climate – i.e., areas where an improved situation can yield the most rapid results.

Among the principal measures to be implemented here, we can point out the following ones:

- lowering the risks associated with doing business: a revision of the RF Criminal Code in order to abolish a number of its articles envisaging punishment for some economic and tax crimes (de-criminalization of the corresponding deeds), as well as a more precise definition and separation of the functions and powers of the law enforcement agencies supervising economic activities;
- improvement of legal protection of competition, expansion of companies' rights to defend their interests;
- lowering the level of state interference and improving regulation efficiency (measures designed to alter the motivations and increase the control of the state apparatus);
- creating incentives for improving the conditions for doing business at the level of regional and local authorities;
- improving the efficiency of legal regulation of entrepreneurial activity, including the creation of a National Investment Council;
- a more precise definition of the functions of and limitations to the direct and indirect presence of the State in the economy as an economic agent (privatization);
- promoting the elaboration of various forms of public protection of business interests, the activity of business associations and the independent mass media;
- development of a strategy ('a road map') designed to lower those barriers that impose the most serious limitations on economic growth (market access barriers, access to networks, border crossing regimes, and liberalization of the construction market).

***Liberalization and greater efficiency of the labor market*** becomes an especially important task in the situation of a decline in the economically active population.

It is necessary to revise the Labor Code in order to liberalize the procedures for the hiring and dismissal of workers and to abolish the practice of informal (political) regulation of employment within the framework of separate enterprises and in the regions.

Another direction involves a policy designed to stimulate labor mobility (domestic migration), concentration of labor in areas of economic growth, as well as a redistribution of the labor resources that have become redundant in the budget-funded sector. These measures will imply legalization and development of the residential leasing market, and also granting to

Russian citizens an easier access to public welfare funds everywhere in Russia's territory (medical insurance, etc.).

And finally, it is necessary to implement a number of measures designed to increase the attractiveness of immigration to Russia. They should include a switchover from the restriction-based principles of migration regulation to differentiating ones; an orientation towards 'sedentary' migration; a policy aimed at attracting a highly qualified workforce (including the promotion of immigration and mobility in the fields of education and academic studies). The migration of qualified workforce is the most difficult to promote, but it would be much more important to practically achieve that goal than to simply discuss the issues of illegal migration of unskilled labor.

*Human capital* is a key factor in the development of a sound post-industrial society. Investments in human capital have been the most relevant factor in those countries that over the last 50 years have achieved successful modernization leaps. This refers mainly to the development of sectors like education, public health care and the pension system.

According to the traditional (industrial) understanding, these sectors are branches of the social sphere. Although the social welfare aspect has retained its importance in contemporary developed economies, these branches now represent a network also of fiscal, investment and political components. In contrast to the practice that was widespread in the late 19<sup>th</sup> and most of the 20<sup>th</sup> century, education, medical services and pension provision are now available to the entire population (taxpayers and consumers of the corresponding benefits alike), and the demographic crisis has only further aggravated the already tense situation. As a result, the deductions to the development of these spheres can undermine the financial stability of any developed country. Besides, these deductions are, as a rule, long-term ones, and so they largely shape up a nation's investment resources. And finally, an efficient functioning of these sectors actually determines the political and social stability of societies with a predominance of the urban population.

Human capital development implies providing solutions to both financial and structural problems. As far as financial targets are concerned, it is advisable to compare Russia's relevant expenditure indices with those of countries with comparable or higher levels of economic development – in particular, the OECD countries. Russia spends on education and public health care approximately 1.5–2 p.p. and 3–4 p.p. of GDP (respectively) less than the OECD.

However, problems hindering the development of the human capital sphere are not limited to insufficient financing. The other, more important, aspects are structural transformation and adequate response to the challenges of postindustrial society. Below we are determining the five characteristic features (or principles of functioning) that must be taken into account when undertaking their structural modernization. These reflect the distinctive features of modern technologies – their dynamism (a rapid renewal cycle) and the increasing customization of technological solutions.

First, the services are provided on a continual basis. Education and health care are turning into a lifelong process – people train and get medical care as long as they live. The very idea of work is being transformed, thus also making more vague the idea of retirement.

Secondly, the services are becoming increasingly customized. More and more often people will be making a choice of their own educational 'trajectories' and health care mechanisms out of the available variety of educational and medical services. The retirement age is also increasingly becoming a matter of personal decision when people determine individually when they can and want to discontinue their professional activity. With regard to the pension

system this will imply a very significant diversification of the forms of support provided to senior citizens.

Thirdly, the services are acquiring a global character. Educational establishments and hospitals are now competing not only with the neighboring or even national ones, but also with those situated elsewhere in the world. Of course, such a broad choice is by no means affordable to everybody, but as people become wealthier and the real cost of the relevant services and transport cheaper, more and more individuals will be participating in that global-scale competition.

Fourthly, the role of private spending on human capital development is becoming more prominent. The first three characteristic features imply expanding opportunities for individuals to buy the services that they need – consequently, the share of private demand is also going to expand at an accelerated rate, getting increasingly ahead of budget-funded demand. Private payments and co-payments become not only a natural but an inevitable outcome of the technological modernization of the social sphere.

Fifthly, the role of new technologies is also on the rise, thus radically changing the character of the services being provided. As the information and communications technologies and transport are getting increasingly more sophisticated, the traditional forms of medical care and education are becoming a thing of the past. This can also be said of organizational innovations.

All the aforesaid features can provide a foundation not only for human capital modernization, but also for the economic and political modernization of the entire country, including its technological base.

***Openness of the economy and promotion of competition.*** The year 2011 saw two major steps towards creating the preconditions for modernizing the Russian economy: the establishment of the Customs Union and the Common Economic Space on the one hand, and a breakthrough on Russia's WTO accession on the other. The importance of these decisions is that they will increase the level of competition for Russian enterprises, which has so far been insufficient. Until recently it was believed that these two goals (post-Soviet integration and Russia's accession to the WTO) cannot really be achieved simultaneously. However, by early 2012 all the contradictions previously existing in that sphere had been successfully removed. One can really expect from the movement in these two directions something more than simply a more intense competition.

Post-Soviet integration may have two important consequences. First, it not only pushes further the market's boundaries but also sets a precedent of reintegration that can be followed by other countries. Secondly, it helps to strengthen the ruble's international positions and becomes *de facto* a significant step towards making it a regional reserve currency. Thirdly, in addition to competition between commodities it creates preconditions for a competition between institutions and jurisdictions. Although the partner countries' institutions are probably not the most attractive ones, the very fact of competition will be conducive to progressive institutional shifts.

Russia's accession to the WTO will help to diversify her exports. Of course, the State and businesses alike must undertake some coordinated efforts in that direction. Nevertheless, Russian companies have been given some additional chances to participate in international production chains.

Besides, the Russian Federation's accession to the WTO will become the first step on the way towards Russia's broader integration in the world economy and its institutions. The next

important steps will be accession to the OECD and the start of active efforts towards creating a free trade zone with the European Union. Given that the EU's share in Russia's external trade is approaching the level of 60%, the strategic goal of the RF is to establish a EU-Russia relationship similar to the one that exists between the European Union and Norway.

All these events must be taken advantage of by Russia in order to seek some new niches in the international division of labor through diversifying her raw materials exports, promoting exports unrelated to raw materials, and boosting the international cooperation of Russian companies. The strategic goal in promoting exports unrelated to raw materials (or hi-tech exports) will be to occupy a niche in South-South trade (the exchange of technology and hi-tech products between countries with medium and low revenue levels). It should be emphasized that all the successful modernization breakthroughs of the last 50 years have been based on orientation towards exports.

***Spatial development.*** Spatial policy must rely on two principles: promotion of population inflow into economic growth points (or regions) as a compensation for the demographic crisis (an overall decline in population); and promotion of competition between regions and municipalities for the attraction of population and businesses.

The federal center, when determining the goals of its own development and planning the ways for their achievement, must also guarantee autonomy to each level of authority; provide all the regions with equal conditions for modern growth; ensure transparency, simplicity and predictability of the 'rules of the game' applied in the relations within the federation, including interbudgetary relations. These goals can be achieved through expanding the revenue base of regions and municipalities, while at the same time increasing the level of their responsibility and accountability to the population for the execution of their powers in the sphere of social policy. This will require the introduction of some serious alterations in the tax system, including those implying its decentralization.

An important priority for the federal authorities in the sphere of spatial policy must become the task of providing transport links to territories possessing their own economic potential, as well as that of supporting the naturally evolving centers of development. It will be necessary to create incentives for improving the conditions for doing business at the level of regional and local authorities by making federal support performance-based in terms of economic development results (and primarily the rate of investment attraction).

One of the main issues is to ensure that the heads of municipal formations with adequate financial bases, as well as heads of regional bodies of authority, are elected to their posts. In 2011, both the RF President and the Chairman of the RF Government suggested that direct gubernatorial elections should be reintroduced. However, it is very important to consistently implement that principle on the municipal level.

#### 1.1.5. Political Processes and the Economy

The past year was marked by the growing political activity of different social strata. The December elections to the RF State Duma escalated political tensions across the whole of Russia, because a considerable part of society was not prepared to recognize the election results as legitimate.

Over the last decade, Russia has been consistently constructing a 'one-and-a-half-party democracy' that has become well-known from the experience of Italy and Japan in the 1950s-80s and Mexico for a greater part of the 20<sup>th</sup> century. This type of democracy is characterized by a decades-long single-party rule, while there also exist other political forces that partici-

pate in elections but are incapable of exerting any significant influence on the decision-making process. The main drawback of that model is a high level of corruption, which is inevitably associated with a long-term rule of one and the same political force. On the brighter side, the government usually achieves political stability and successful economic growth. The model has been quite appropriate for Russia – given her current level of economic development historical features.

On the darker side, one-and-a-half-party democracy is poorly compatible with contemporary technological challenges, and especially with the information saturation of contemporary society. It is these factors that push a country towards liberalization, and these ideas can easily gain support of the more ‘informed’ (and younger) part of the population. Thus, a rise in political activity is not necessarily associated with a worsening economic situation. On the contrary, improved well-being promotes growth of political activity and readiness to present the authorities with some ‘awkward’ questions. It was Alexis de Tocqueville who noted that revolutions happen in countries characterized by dynamic economic and social development, and not in stagnating societies. The experience of the 20<sup>th</sup> century, including our domestic experiences, can only serve as a confirmation of that statement.

It would be a mistake to view the current intensification of political processes as a manifestation of a revolutionary situation. Russia experienced a full-scale revolution in 1987–1999, and any repetition of those events nowadays is absolutely improbable. However, it seems quite reasonable to analyze the current political developments in Russia through the prism of the historic experiences of revolutions.

The great revolutions of the past always produced an impact on the development of the corresponding countries that lasted for several decades. This was manifested in periodical (once every 15 to 20 years) dramatic turns in the political situation which occurred as if for no reason at all. Such events never resulted in the total dismantling of the existing system and did not introduce any fundamental changes in economic and political relations. Nevertheless, they brought to power some new socio-economic strata and new generations of politicians. These strata and politicians by no means always denounced their predecessors and, as a rule, had belonged to the previously existing elite. But they answered the needs of the new generation, and thus continued the course towards the post-revolutionary consolidation of society<sup>1</sup>.

An increasing political uncertainty may have a negative effect on the rate of economic development, and especially on capital movement. However, the economic situation can be threatened not so much by political uncertainty (to which businesses can adapt rather easily) as by political, macroeconomic and social instability. The most important present-day task for the Russian authorities is to avoid destabilization in the forthcoming period.

From the point of view of economics, there exist two sources of destabilization: external and internal.

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<sup>1</sup> A classical example of this type of development is, of course, nineteenth-century Post-Revolutionary France, which underwent considerable political changes in 1830, 1848 and 1870. The Restoration of the Bourbons in 1814 returned to power the landed aristocracy, which was replaced at the helm, in 1830, by a financial oligarchy (under a new monarch who was a relative of the previous king), only to be succeeded, in 1848, by the urban bourgeoisie (under an emperor who was a nephew of the previous emperor). The period of turmoil came to an end with the establishment of the Third Republic in 1870, which ensured that all key interest groups were sufficiently well represented at senior levels of government. It may be said, without going into details, that the same trend can be seen in the aftermath of other great revolutions of the past.

The *external* source is, most likely, associated with the prospects of the world recession (or at least recession experiences by Russia's main trading partners). This will be followed by a marked decline in the prices for energy resources, which are the main source of revenues from exports and thus the foundation of Russia's budget stability. Such a change will produce an internal shock that will have to be countered with some decisive and consistent measures in the spheres of budgetary and monetary policies. The afore-said drop in energy prices will not be a disaster if we duly prepare for it. The introduction of the *budgetary rule* and the discontinuation of the policy aimed at sustaining a stable ruble exchange rate (see above) will represent important steps towards mitigating the effects of the possible shocks. However, that will be not enough: the government must also have at hand a well-elaborated plan for actions to be taken in an event of a dramatic deterioration of the global economic situation.

*Internal* risks are primarily associated with the danger of switching over to the policy of budget populism. An abundance of budget revenues and a formally very beneficial macroeconomic situation (especially by comparison with the European countries) coupled with a threat of growing socio-political discontent may entail a weakening of the budgetary policy – in other words, may result in a rise of expenditure covered by situational revenues from exports and borrowings. Politically, this would be the easiest way – but it is fraught with some serious future problems.

Another form of response to the political events of late 2011 would be to develop a comprehensive modernization strategy. The core problem plaguing the three-century history of Russia's catch-up modernization has been its non-comprehensive (or, so to say, 'patchwork') character. The authorities have always tried to emphasize some separate aspects of modernization (military, technological, economic, scientific, educational, or more rarely – political), but there has never been a single comprehensive program. That is why the results of Russia's previous attempts at such modernization were inconsistent and unstable.

Now, when modernization has become a slogan of the day, it is becoming absolutely necessary to push it in every direction, and in particular to combine modernization of technologies with modernization of institutions (economic as well as political ones).

