

## POLITICAL AND ECONOMIC RESULTS OF MARCH 2014

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*In March 2014 Russia announced the accession of Crimea based on the results of the referendum held on 16 March 2014. In response the U.S. and EU introduced visa sanctions and a ban on the possession of assets in their jurisdictions for Russian officials (and in the U.S. this also extended to certain businessmen close to Vladimir Putin). The G8 forum ceased to exist and, effectively, Russia, on the one hand, and the U.S., Canada, Europe and Australia, on the other, returned to the situation before 1991 when they considered each other as major opponents. For Russia this may result in a considerable decrease in investment, the withdrawal of capital and an economic decline, even despite the fact that, in the short term, these countries will be unable to replace the Russian hydrocarbon exports and this will cause substantial economic damage. The Russian Parliament introduced a bill to confer citizenship on all descendants of residents of the Russian Empire who are “native speakers of the Russian language” and to cancel mayoral elections in the largest cities, however, consideration of these laws has not been accelerated and they will most probably be amended.*

The main news in March 2014, not only in Russia, but also globally, was the accession of Crimea to Russia. Back in February this had seemed unrealistic and the announcement of a referendum on the status of Crimea as a part of Ukraine, planned for May 2014, to coincide with the Presidential election in Ukraine, had at least looked like a means to influence the Kiev government, and at most as to provide the possibility for the emergence of another non-recognised republic such as South Ossetia, Abkhazia, Northern Cyprus, Karabakh, etc. However, the situation changed dramatically in the first days of March. On 1 March the Federation Council gave to Vladimir Putin its permission to use armed forces “in the territory of Ukraine”. On 8 March the Supreme Council of Crimea changed the wording of the referendum (it had originally sounded quite vague, talking about the status of Crimea in Ukraine on the basis of an agreement) to two alternative questions — “Do you support the accession of Crimea to the Russian Federation with all the rights of a subject of the Russian Federation?” and “Do you support the re-enactment of the Constitution of the Republic of Crimea of 1992 and the status of Crimea as a part of Ukraine?”, and the date of the referendum was moved to 16 March. Ukrainian government officials were prevented from entering Crimea and Ukrainian military units in Crimea were blocked by masked gunmen, who few doubted were members of the Russian armed forces. According to official data from the Crimean government, the referendum turnout was 82%, with 95.5% of all voters supporting the option to join Russia. Those who were against joining Russia, mainly, Crimean Tatars (about 12–15% of the Crimean population) boycotted the referendum. Although the official data give rise to a certain extent of

doubt — for example, observers and journalists were not allowed into some sites, it is evident that, in general, most of the Crimean population did participate in the referendum and did vote for joining Russia. Following this, some of the Ukrainian armed forces in the Crimean military garrisons agreed to join Russia, while the remaining ones peacefully evacuated to the territory of continental Ukraine. The new government announced the nationalisation of the property in Crimea of Ukrainian state companies, and the Russian government declared a denouncement of the agreements on the Black Sea Fleet in Crimea, which had given Ukraine a considerable discount on Russian gas.

The timing of the special operation in Crimea was quite well-chosen — in particular because the Ukrainian government was faced with the dilemma of either beginning military operations in Crimea, with the prospect of a protracted war on Ukrainian territory, or of accepting de facto the loss of Crimea, allowing it to concentrate on the conduct of the Presidential elections in May and on the protection of its eastern and southern regions from a repeat of the Crimean scenario. Predictably, they chose the second option. They managed to negotiate with large businesses in the eastern and southern regions, the representatives of which (former members of Viktor Yanukovich’s the team) were appointed as governors of the relevant regions, and the local legislatures which agreed not to take any separatist action, while the few leaders “from the street” who tried to storm government institutions were arrested, after which the protests began to calm down.

However, at the end of March, it was still not clear if it would be possible to avoid war, although the likelihood of this had decreased. The official rhetoric of the

Russian government still does not recognise the new Ukrainian government and the elections planned for May, arguing instead for “the legitimate President Yanukovich”, who had actually been declared, by consensus in Ukraine as a state traitor and expelled from the once-ruling “Party of the Regions” and lost the support of his ally, the Communist Party of Ukraine. In Ukraine, there is not a single major party which would consider Yanukovich as the head of the state and does not recognise the legitimacy of the Presidential elections scheduled for May. However, Russia has agreed to send an observation mission from the Organisation for Security and Co-operation in Europe to Ukraine and, from time to time, for its secondary level officials to make contact with Ukrainian officials to resolve certain practical issues. Russian officials deny the existence of plans to invade Ukraine; however, just a few days before the referendum on Crimea joining Russia, Putin also denied having plans for this. Russian TV channels are reporting surprising information on events happening in Ukraine, including hundreds of thousands of refugees, which no-one has ever actually seen, etc. while the image they are creating appears to be aimed at justifying a possible military operation.

The events in Ukraine have not greatly affected the Russian internal political situation. Mass rallies have been held supporting the accession of Crimea and, in contrast, against war with Ukraine. Roskomnadzor (the Federal Supervision Agency for Information Technologies and Communication) banned a few opposition websites, including the blog of a prominent opposition activist Alexei Navalny in ‘Live Journal’ (however, its numerous mirrors have persisted). The Speaker of the State Duma Sergei Naryshkin denied the possibility of early parliamentary elections (opinions had been expressed that, with the increasing popularity of the current regime, such elections could make sense for it). However, it is worth specifically mentioning two important bills introduced to the State Duma.

Firstly, there is a draft law, proposed by a group of deputies of the United Russia party, on the elimination of mayoral elections for the largest cities. According to this draft law, mayoral elections in those cities which have district separation (the 56 largest cities, including most of the capitals of subjects of the Russian Federation) would be cancelled; furthermore, the direct elections of city Dumas that have to elect a mayor from amongst themselves, would also be cancelled — these Dumas would be delegated by the district Dumas, in equal proportion, regardless of the number of electors in the district. No similar system exists in any developed country and, it actually mimics some of the feudal systems that used to exist hundreds of years ago, a kind of ‘États-Généraux of pre-revolutionary France.

Moreover, this system, if put into place, would directly violate Putin’s pre-election promises made in February 2012 on the introduction of the direct election of city mayors throughout the country (currently such elections (from amongst the deputies) are possible through a municipal power — both direct and indirect.) However, the fact that this draft law was not proposed by the President or the RF Government, leaves the opportunity for it to be altered. If it is adopted, the following different scenarios are possible: the one expected by United Russia, in which people will express hardly any interest in the elections of numerous unknown deputies to the district Dumas, which then become the key elements of this system, and the other, where, due to the considerable reduction in the number of people in each election district, the opposition can actually walk each district “from door to door” without any material costs.

Secondly, there are the amendments made by the Russian Government to the Law on Citizenship of the Russian Federation. It is clear that the Crimean story required at least a change of the rules for obtaining citizenship by residents of Crimea and, perhaps, even by Ukrainian citizens. However, the draft law turned out to be a shock — according to this draft, any descendant of a citizen of the Russian Empire who is a native speaker of the Russian language can obtain citizenship of Russia. Whether a person qualifies or not will be determined by special commissions of executive bodies, so, there is not even a need for a formal examination. Such an applicant should surrender citizenship of the other country and express his or her willingness to move to Russia for permanent residence. It actually means that tens of millions of residents of Central Asia and the South Caucasus will easily obtain the right to become Russian citizens — quite clearly they will have little reluctance in surrendering their citizenship of poor countries. Moreover, there is a provision for an applicant for citizenship legally to stay in Russian territory for two years, which explodes the existing system of protection of the national labour market — labour quotas, residence permits, etc. Currently, a visitor must leave the country within three months if they have not obtained appropriate legal permits. The draft law did not originally arouse any considerable opposition (initially, because people did not understand the range of citizenship covered, and assumed that it was only about Russians in Crimea, which would be logical), however, its consideration, originally scheduled for 21 March was postponed for an, as yet, indefinite period. Apparently, the government understand either the rawness of the draft law, or is afraid of the public reaction when it is realised which “imperial descendants” are included.

As for the external political situation, this has changed dramatically. We are actually talking about the biggest change in international relations since 1991. Neither the events around Kosovo, nor the wars in Iraq and Afghanistan, or that between Russia and Georgia in August 2008, aroused such a resonance. The strictest sanctions against Russia have been introduced by the U.S. — they declared a prohibition on the entry to the country and a freezing of the assets of two dozen Russian government officials (including the Heads of the Lower and Upper Houses of Parliament, Sergey Naryshkin and Valentina Matvienko, the Vice President Dmitry Rogozin, the Head of the Presidential Administration, Sergei Ivanov, its Deputy, Aleksey Gromov, associates of the RF President, Vladislav Surkov, Andrei Fursenko and Sergei Glaziev, a number of other deputies and senators and the CEO of the State Company, JSC Russian Railways, Vladimir Yakunin, businessmen Yury Kovalchuk (“Russia” bank), Gennady Timchenko (co-owner of oil trader Gunvor, the gas company Novatek and various construction companies) and the Rotenberg brothers (the largest contractors for JSC Gazprom), who are considered to be friends of Vladimir Putin. The European Union, together with Switzerland, Norway, Canada and Australia all introduced similar sanctions, excluding, however, the most sensitive sanctions against individuals — i.e. the above five businessmen, who have considerable assets in EU countries. A resolution on the liquidation of the G8 forum and a return to the G7 format that had existed twenty years ago was passed unanimously. Moreover, the U.S. declared a prohibition on the export to Russia of dual-use products. In response, Russia declared ‘*persona non grata*’ a number of American and European politicians, introduced restrictions on the import of European pork and Australian beef and terminated the Russian businesses of the Ukrainian politicians and businessmen Petro Poroshenko and Igor Kolomoisky (the accounts of the confectionary factory of the former were frozen and factory operations suspended, while a temporary administrator was appointed over the Russian branch of the latter’s bank). Gennady Timchenko declared that he had sold his stake in oil trader Gunvor one day before the introduction of the US sanctions. At this point, a balance has been established. Obviously, in the case of an intrusion into continental Ukraine, the sanctions will be extended, primarily, to businesses suspected of close relations with the Russian government. Voting in the UN General Assembly at the end of March on a resolution not to recognise the validity of the Crimean referendum gave the following indicative results: 100 countries voted “in favour” (with the exception of Israel which did not participate in the vote,

this included almost all the developed countries, plus Indonesia, Malaysia, Chile, Colombia, Azerbaijan and Moldova), 11 voted “against” — besides Russia, these were Belarus, Armenia, Syria, Sudan, North Korea, Bolivia, Nicaragua, Venezuela, Zimbabwe and Cuba, while 58 countries abstained, many did not vote (among the countries abstaining were China, India, Argentina, Brazil, South Africa, Iraq, Kazakhstan and Uzbekistan; non-voting countries included: Iran, Kyrgyzstan and Tajikistan). Certainly, this can hardly be called a diplomatic success — it is rather an “honourable” defeat, given the non-zero score.

It is quite difficult to explain rationally what is happening, when both politicians and people in Russia, Ukraine and the West are overwhelmed with emotion. However, we can try. The essence of the claim against Russia is this: Russia violated its own diplomatic obligations under the Budapest agreement, pursuant to which Russia, the United Kingdom and the U.S. guaranteed Ukraine and Belarus their sovereignty and security in exchange for their commitment to eliminate all nuclear weapons from their territories. Moreover, the arguments used by Russia (in particular the reference to the ‘Russian-speaking population’) mean that, tomorrow, Russia could attack not only continental Ukraine, but also Belarus, Kazakhstan or Moldova. Furthermore, an informal rule that has existed for decades has been broken. The understanding was that, in the case of the secession of a particular territory from a country, it is not acceded to another, but becomes independent. If one looks closely, this rule was observed in the cases of Northern Cyprus, Karabakh, South Ossetia, Abkhazia, South Sudan, Kosovo, etc. The Russian position is that, firstly, its obligations have changed with time and have lost their force in the case of Ukraine because the sovereignty of Ukraine had been somehow violated prior to the Crimean issue; secondly, that the Russian speaking population has a right to self-determination, especially taking into account that there are currently issues of self-determination being discussed in Europe as well — in Scotland, in Catalonia and in Flanders. In fact, all this is leading to a collapse of the international security system and a return to a “might makes right” scenario. At the moment the West is not ready to fight for Ukraine, Moldova or Kazakhstan — hence, the Russian army, with its military potential could capture them, although it would be much harder to retain them with no support from the population. However, Russia has a serious economic dependence on Western countries — primarily in respect of capital markets, but also in respect of its turnover of goods — European countries account for over 50% of Russian exports, which, in turn, are represented mainly by hydrocarbons and are the mainstay

of the Russian budget. Replacing these exports would be hard for Europe in the short term, but in the mid-term it would be quite possible to reduce their extent considerably (by removing the sanctions imposed on Iran, removing the prohibition on the export of crude oil from the U.S., accelerating the construction of regasification terminals — already in progress in the U.S. and Europe, substitution with coal, etc.). For Russia, there is no adequate replacement for the exports to Europe in monetary terms — China is ready to buy energy resources only at prices far below the current market levels (for example, for almost 10 years Russia and China have failed to agree upon a gas price formula and to start the construction a gas pipeline). Capital outflow from Russia was huge even before the Crimean crisis — \$35bn in January-February versus \$63bn for the whole year of 2013; in fact, projections indicate that the first quarter volume, alone, may reach the annual level of 2013); the more the rift between Russia and the developed countries grows, the more the capital outflow will increase and the more the population will feel the effects of it. Thus, it is hard not to agree with the Chairman of the Committee of Civil Initiatives and former Minister of Finance, Alexei Kudrin, that the price for a foreign policy which ignores the developed countries would be enormous. As for Crimea itself, it is unlikely that the expenditure on it

will be particularly high — especially, if for its part, the Russian government withdraws from a range of highly questionable mega projects, such as the construction of a high speed rail line between Moscow and Kazan, worth over Rb 1 trillion.

Regarding Russian internal events, there is one more worth mentioning. The Command of the Caucasian militants has officially confirmed the death of Doku Kumarov. A well-known racketeer in the early 1990s, he turned to Islam and became famous amongst the leaders of the underground resistance when he announced that he had joined the international terrorist ‘caliphate’ to promote their causes rather than “Independence for Ichkeria”, as he had previously been doing. Umarov, apparently, died of wounds received in action. Aliaskhab Kebekov (Abu-Mukhammad), who had been second-in-command in the underground resistance in Dagestan, was declared its new leader, the so called “qadi” (Islamic judge) and the holder of the underground’s financial reserves, which represent hundreds of millions, if not billions, of rubles, received initially from the Russian budget but later through racketeering government officials. This event reflects the fact that the main terrorist threat has moved from Chechnya and Ingushetia to Dagestan and, judging by the recent terrorist attacks in Volgograd, remains quite serious. ●