

Russia's "Sovereign Globalization"

INSULATION, INFLUENCE, AND DECLINE

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Economic problems are once again at the center of debates about Russia's future. For the first time under the Putin presidency, the country faces a protracted decline in living standards. This will have important implications for domestic cohesion, and perhaps for the capacity to sustain a strongly assertive foreign policy. One important cause of these problems is Russia's distinctive, ambitious, but failed strategy of globalization. The legacies of this failure can help us to understand the difficult choices that Russia now faces.

When Vladimir Putin became president, he demonstrated a strikingly positive attitude toward engagement with the global economy. He was explicit and consistent in his view that a strong Russia had to be prosperous, and that prosperity could not be achieved without deeper international economic integration. Unlike other aspects of the Soviet experience, he showed no nostalgia for autarky and isolation.

But there was an inherent tension between enthusiasm for globalization and the *silovik* project of re-establishing political control through a strong authoritarian state. Building a "vertical of power" meant limiting unwelcome external influences, weakening independent institutions, and harnessing legal powers for political ends. By contrast, integration into the global economy meant easing control of commercial and financial flows across borders, increasing Russia's dependence on external actors, and binding Russian entities to contracts and jurisdictions beyond Russia's control. These two priorities pulled in different directions. To manage this tension, Russia developed a strategy, which we may call "sovereign globalization." Just as sovereign democracy sought to manage domestic political processes to strengthen regime legitimacy and control, so sovereign globalization sought to manage international market processes to strengthen Russia's economy and extend Russian influence abroad.

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The rise and fall of sovereign globalization has shaped the evolution of the Putin project. We can trace three phases: insulation, influence, and decline. Their passing marks the failure of Russia's ambitious attempt to harness economic integration to great-power politics. This failure leaves Russia with a series of less attractive foreign-policy strategies among which it has yet to make a clear choice.

Insulation

During his first term, President Putin expressed strong commitment to restoring Russia's economic strength through international integration. As he [stated](#) in his 2003 annual address to parliament:

“Russia owes its economic growth above all to the favorable world economic situation over recent years... 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.”

Numerous Russian policy measures supported this. They included: encouraging foreign direct investment, completing the liberalization of ruble convertibility, lifting restrictions on foreign ownership of Gazprom shares, and reviving Russia's World Trade Organization (WTO) bid.

With significant domestic reforms stalling in 2003, foreign economic relations became the main driver of growth. Every strand of these thickened significantly. From 2000-08, inward investment rose 28-fold and outward investment six-fold. In 2002, Russia joined the G8, and chaired it in 2006. The same year, Russia recorded its first net capital inflow of the post-Soviet era.

At the same time, flows of goods, services, and capital were carefully managed to ensure they did not bring Western influences that might undermine the rebuilding of a strong and autonomous Russian state. In particular, restrictions were tightened on foreign asset ownership in a wide range of strategic industries. The Yukos affair signaled, among other things, the Kremlin's determination to head off potential foreign control of Russia's largest private company, while Russia also regained majority control of major Western-led energy projects. The only exception to this pattern of deepening international exposure was Russia's foreign indebtedness. But here, too, Russian policy served the goal of protecting the country from unwelcome foreign influence. Putin made early sovereign debt repayment a priority in order to end what he saw as a humiliating dependence on international lenders and to eliminate the potential for exerting leverage on Russia.

These methods appeared highly effective in insulating domestic political control from the beneficial effects of external economic engagement. From 2000-12 Russia enjoyed inflows of over \$1 trillion, helping to drive GDP growth rates of 7 percent per annum.² At the same time, the state became stronger, more authoritarian, and more assertive, while Western business partners became more exposed to Russia but less influential in it.

Influence

This success emboldened Russia to develop a second, more ambitious, strand to sovereign globalization. Russia now aimed not merely to limit external influence but to exert its own influence on others through stronger economic ties. Russia had done this episodically within the post-Soviet region in the 1990s, but from the early Putin era, Moscow began to use economic means for foreign policy ends far more systematically. It did so in two ways.

First, Russia used its position as a major market for, and energy supplier to, the post-Soviet states to link imports of produce, and exports of oil and gas, to unrelated political issues. Actions and policies unwelcome to Moscow were thereby punished through costly disruption of the target state's trade.

Second, Russia sought to use its growing role as a dominant gas supplier to Europe to exert a more gradual form of political influence that we may call "energy Finlandization." Russia sought to deepen its presence across the European energy value chain and so cultivate perceptions of individual, elite, and national interests as naturally aligned with a Russian point of view. Unlike Russia's use of economic means within the post-Soviet region, this more subtle and longer-term approach favored co-option more than coercion, inducements more than threats, and persuasion more than punishment—although a more coercive intent could surface when these softer methods were challenged. Russia repeatedly divided EU states, hindered an effective common European policy, and began to entrench elements of a dominant presence: bilateral over multilateral relations, long-term contracts, and downstream asset purchases. As a result, the Russia-EU economic relationship flourished even as political relations deteriorated. Russia even aspired to turn Moscow into a major financial center and the ruble into a reserve currency.

Over Putin's first two presidential terms, this strategy appeared to work effectively. Sovereign globalization could, it seemed, manage the tensions and harness the synergies of international openness and domestic control. This strategy also marked a historic departure for Russia, whose enduring weakness had always been its relative economic

² Total oil and gas windfall revenues alone for 2000-08 were \$900 billion. See: Alexei Kudrin and Evsey Gurvich, "[A new growth model for the Russian economy](#)," *BOFIT Policy Brief* 1/2015, p. 5.

backwardness as a great power. For the first time, it now sought to use economic relations with wealthier states as a source of strength.

Decline

Moscow's apparent success, however, was dependent on a set of favorable but temporary circumstances. After 2008, three adverse shifts in Russia's relationship with the global economy undermined its strategy. First, the raw material export-led growth model began to fail, with growth rates falling even while commodity prices remained high. As a consequence, prosperity could no longer be achieved primarily from external sources. Second, the "[revolution in energy affairs](#)"—shale gas and the expansion of global liquefied natural gas trade—threatened Gazprom's model of securing a dominant presence in Europe through long-term bilateral supply contracts. Third, EU concerns over the implications of energy dependence on Russia sparked a more cohesive and assertive policy. This was prompted above all by the downstream effects on European consumers of Russia's gas supply cuts to Ukraine. Russia was unable to insulate its coercion of post-Soviet states from its cultivation of the West. In response, the EU hastened its efforts to diversify suppliers and routes and to challenge Gazprom's restrictive and monopolistic practices.

As a consequence, Putin now began to see globalization as a source of threats as well as opportunities. Its effects on domestic cohesion came under scrutiny, especially on the loyalties of business and administrative elites with their assets, tastes, and sometimes families, in the West. Influential Russian commentators [coined](#) the term "sixth column" to describe those who, outwardly loyal to the regime, urged moderation in Russia's policy toward the West because of their own vested interests in this relationship. A "de-offshorization" campaign was mounted in response, with measures that included a decree banning government officials from holding overseas financial assets.

Patterns of international engagement, too, became more defensive. Russia's ambition to extend energy influence across Europe gave way to a narrower focus on tighter integration within the post-Soviet region in order to consolidate Russia's position—in part, as a response to what Russia saw as expansion of the EU's own influence through its Eastern Partnership. Russian pressure on Ukraine to turn toward the Eurasian Economic Union instead of signing an EU Association Agreement became the proximate cause of the present crisis in Russian-Western relations.

This crisis led to the unravelling of Russia's economic relationship with the West as the two sides imposed sanctions on one another. This marked the first time in the post-Soviet era that the West sought to restrict rather than encourage Russia's integration into the global economy, and the first time that Russia raised rather than lowered barriers to its own participation in it. It marks, too, the failure of sovereign globalization, Russia's

ambitious attempt to reconcile competing imperatives of international integration and domestic control, globalization and *Realpolitik*, power and plenty.

Implications

What choices now face Russia? Four options are available, each offering a different way of addressing the central tension between economic prosperity through international openness and political control through a *silovik* state.

1. Status quo ante. This approach seeks not to resolve the contradictions of current policy but to ease the conditions that aggravate them in order to make the present course more tolerable. It seeks to remove Western sanctions (for example, by making Russia indispensable to a resolution of the Syrian conflict) and by attempting to shore up oil prices through closer cooperation with OPEC.

This is a policy of “muddling” rather than “muddling through.” Even if Russia succeeds in achieving the measures dictated by this approach (such as lifting Western sanctions), this will not resolve Russia’s underlying economic problems. The country’s growth model was failing even before the collapse in oil price and imposition of sanctions. This path is not a long-term solution to the challenges facing Russia’s political economy.

2. Self-sufficiency. This approach prioritizes domestic control and great-power assertiveness over prosperity through globalization. Economically, it involves import substitution, “patriotic” retrenchment, and even anathematization of some Western products, for example by their public destruction. Politically, it means raising pressure on, and issuing threats against, domestic opposition.

It is unclear how sustainable this course might be. The Russian economy remains highly dependent on international factors, especially the oil price. Russian economists continue to warn against the inefficiencies of import substitution. Further economic decline could trigger mass discontent and resentment at elite corruption.³

3. Non-Western integration. This approach seeks to compensate for decline in relations with the West and the effects of sanctions by building new political alliances and economic partnerships—in particular in Asia and especially with China. With fewer political differences or military tensions with these states than with the West, Russia seeks international support, or at least “understanding,” for its policies as well as trade and investment.

³ For a recent argument warning of this and other problems, see Alexander J. Motyl, “[Lights Out for the Putin Regime](#),” *Foreign Affairs*, January 27, 2016.

The economic potential of Russia's "Asian pivot" is unclear. While most Asian states will seek to avoid choosing between Russia and the West, few are likely to support Russia if circumstances force them to make such a choice. Nor are economic relations with non-Western states likely to be an effective substitute for the large flows of Western trade and investment on which Russia has depended. China has already demonstrated a tough pragmatism with Russia, for example on gas pricing. Its "One Belt, One Road" policy will deepen its involvement in Central Asia and could generate economic rivalry and political friction with Russia.

4. International integration. This is the opposite of the "self-sufficiency" option discussed above. It prioritizes collective economic welfare over the domestic *silovik* agenda. In this scenario, foreign economic policy is guided only by prospective welfare gains from international integration—perhaps accompanied by significant structural reforms to make Russia a more attractive partner and allow it to benefit more fully from international trade and investment. Crucially, Russia's economic relations would no longer be used as an instrument of external political influence. Since this describes the policy of most other states, Russia in this scenario becomes a "normal" country rather than one with a special identity or mission.

This policy would require a fundamental departure from Russia's current strategy and outlook, in effect, an abandonment of the principles and practices of sovereign globalization. It is unclear, to say the least, how politically feasible this would be under the current regime.

Since 2014, Russian policy has combined elements of all these approaches except the last. Russia's extension of import sanctions on Turkey has shown continued willingness to use economic relations for political ends; it is actively supporting import substitution; and it is courting investment and trade with a host of Asian states.

Russia is still searching for a coherent response to the failure of sovereign globalization without renouncing the principles on which it is based. The new policy that emerges will shape the prospects of both Russia's domestic development and its relations with the West.

For a more detailed argument, see Nigel Gould-Davies, "[Russia's Sovereign Globalization Rise, Fall and Future](#)," Chatham House Research Paper, January 2016.

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