

## **EXCLUSIVE TO CPF David Clark – Russia and the West: New Beginnings?**

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Only a few months have passed since Russia's war with Georgia, yet the world already seems like a very different place. Many reactions to Moscow's swift and emphatic victory last August pointed towards two far-reaching conclusions: that Russia was back as a power capable of setting the international agenda according to its own preferences and that relations with the West were destined to return to a state of tension not seen since the end of the Cold War. Both assumptions are now open to question.

Two major events are responsible for this change. The first is a rapid deterioration in Russia's economic fortunes since last summer. Much of this is undoubtedly to do with financial volatility and falling oil price caused by the global economic crisis; a double-whammy that has hit Russia both as an emerging market and a major energy exporter. Yet it is also important to understand that a lot of its economic difficulties pre-date the banking crisis of September 2008 and stem directly from policy choices made by the Russian government itself. Concerns about property rights provoked by the Vladimir Putin's attacks on the steel company, Mechel, wiped 38% off its share value and 5% off the Russian stock exchange in a single day last July. The invasion of Georgia itself triggered capital flight totalling \$19bn within a month and precipitated a further collapse in the stock market, which lost 70% of its value by the end of the year.

With inflation running at an annual rate of 13%, unemployment set to reach 12% and the economy overall projected to contract by around 5%, Russia's revival has stalled and may not resume quickly. Given that energy exports account for around two-thirds of Russia's export earnings and around half of its federal budget, a major concern has to be the price of oil (and, by extension, the price of gas). This peaked at \$147 a barrel in the middle of last year before sliding to \$34 six months later. There has been a modest recovery since, but it remains well below the \$78 Russia budgeted for this year. Russia's financial reserves are being quickly depleted and any budgetary retrenchment that hit social payments could increase popular opposition and widen the street protests that have already started happening in many major Russian cities.

If the economic situation has led to renewed doubt about Russia's real underlying strength, both among foreign observers and within the Russian political elite itself, the election of Barack Obama in America has added a second unexpected element to the equation. Whereas most analysts believed that President Obama would pursue continuity in policy towards Russia, he has instead offered a new opening in relations following Vice-President Joe Biden's public offer to "press the reset button". The White House is now keen to engage Russia in discussions about nuclear arms control and seek cooperation on issues like Iran and Afghanistan. Russia is happy to oblige because nuclear policy is one area where Russia and the US still talk as equals and the Kremlin, for all its swagger, craves recognition as a Great Power.

The jury is out on whether this is likely to work. The mood around Obama's bilateral meeting with President Medvedev at the G20 summit in London was certainly very positive and the two have agreed to meet again in Moscow in July. But a great deal of scepticism has been expressed about Russia's

willingness to reciprocate on points of substance and there is much nervousness in Eastern Europe that countries described by Medvedev as part of Russia's "sphere of privileged interests" will once again become bargaining chips in a game of Great Power diplomacy.

In reality, Obama's approach is less surprising than it first seems. He has, after all, made similar gestures towards Iran, Syria, Venezuela and even Cuba. Extending the offer of improved relations probably has less to do with any specific conception of how to deal with Russia than with the desire of a new president to give countries the opportunity to make a fresh start in relations with the US unencumbered by past resentments. This is a perfectly sensible idea provided Obama has a clear sense of what his bottom line is and doesn't miscommunicate his intentions to Moscow. All we have heard so far is his desire to put relations on a better footing. We do not yet know how far Obama is prepared to go in pursuit of that aim or what he ultimately expects from Russia in return.

He would be wise to clarify this soon because Russian leaders have a very strong sense of what a 'grand bargain' should look like. Russia would become a reliable partner for the West, providing secure energy supplies, facilitating the resupply of NATO troops in Afghanistan and helping the EU and US in areas where there is no conflict with Russian interests. In return, the West would refrain from criticising Russia's retreat from democratic commitments (or interfering in its domestic affairs, as the Kremlin sees it) and allow Russia a free hand within its "sphere of privileged interests". There would be no further expansion of the EU or NATO to the east, and the West's relations with countries like Ukraine and Georgia would be subject to a de facto Russian veto.

The risk in Obama's approach is that Russian leaders may miscalculate that a bargain of this kind is on the table, implying as it does an abandonment of the post-Cold War vision of a "Europe whole and free". No American President is going to agree to that and Obama needs to make that absolutely clear if he is to avoid sowing the seeds of future tension. At best it would lead to frustration and disillusionment. At worst it would encourage further Russian adventurism of the kind we saw in Georgia.

Nevertheless, an opportunity exists in the midst of economic crisis to find a new way forward in relations between Russia and the West. Russia's problems are structural and not just cyclical, a fact that will become increasingly apparent over the next few years. The oil price will probably rise when global trade picks up, but Russia's dysfunctional, state-dominated energy sector will not, on current trends, be able to sustain output due to chronic inefficiency and underinvestment. Demographic decline may see Russia's population shrink by as much as a third by the middle of the century, putting a cap on economic growth and creating new security risks in the sparsely populated territories of the east. Corruption and the absence of basic political freedoms will continue to stifle creativity and retard Russia's development as a society.

The Putin model of authoritarian government, crony capitalism and assertive nationalism is ultimately unsustainable because it cannot address these problems and more often exacerbates them. In the long run, Russia will need access to western investment, ideas and engagement if it is to prosper as it wants. The issue for the West is how to frame a grand bargain that will allow that to happen on terms that are acceptable to all concerned. The starting point has to be a strong transatlantic understanding on policy towards Russia. President Obama and his counterparts in Europe need to frame a common approach in their dealings with Moscow and avoid the divisions that have allowed Putin to play a game of divide and rule so successfully against the EU.

The message from Washington and Brussels needs to be the same. Russia can meet all of its legitimate needs and aspirations within the international system, but only on the same terms as everyone else. In

particular, it has to respect the rules and principles that define the post-Cold War European order, such as human rights, the rule of international law, the peaceful settlement of disputes, sovereign equality and the right of self-determination of all European nations. There can be no going back to the power politics and spheres of influence of Europe's past. Prestige and influence are rewards that go to those willing to make a constructive contribution to progress in Europe and the wider world, not a privilege to be asserted by the powerful.

We need to establish clear choice paths that will encourage Russian policy makers to understand the link between actions and consequences. Does Russia want to be treated as a respected partner in building European security? Then it needs to resolve disputes with other countries peacefully and abide by its commitments as a member of the OSCE. Does it want access to western investment and technology to develop its economy? Then it needs to guarantee property rights and stop expropriating investments. Does it want to be seen as a reliable energy supplier with full access to the European single market? Then it needs to end monopolistic energy policies and stick to its obligations under the Energy Charter Treaty. Does it want to be regarded as part of the community of civilised nations? Then it needs to restore democratic politics and stop abusing the rights of its people.

We should want better relations with Russia, but not at any price. The best hope for Europe and America to achieve the change they want is to remain faithful to their values. The future of relations between Russia and the West will ultimately be defined by the example we set.

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