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POLITICS

# Putin Plans Re-Election on ‘Great Power’ Platform

Expect More Sabre Rattling and Brinkmanship

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2017 will be dominated by preparations for Russia’s presidential elections scheduled for March 2018. President Vladimir Putin is almost certain to win another term in office, but he will not leave anything to chance. A faltering economy will be his greatest challenge, and as such he will try to divert voters’ attention towards the grand theatre of geopolitics as he continues his “mission to restore Russia’s status as a global power”. The coming year will thus likely bring heightened international tensions which may foreshadow domestic transitions that will determine the operating environment for international businesses in years to come.

## **Top Priority: Presidential Elections**

For 2017, Putin’s number one priority will be ensuring that he remains in power. Although there is no potential opponent that could match Putin’s popularity in the March 2018 election, he will want to see a resounding victory confirming his position as an undisputed leader, laying the groundwork for his next six years in office. This follows a pattern already established with the recent legislative elections, when despite an assured victory for United Russia, the Kremlin took a number of measures to avoid any potential volatility.

Putin’s personal popularity remains underpinned by his continuous TV presence and his image as a leader who is heavily involved in all domestic and international matters and who personally makes the whole system function. His current term in office has seen much state messaging shift towards covering his perceived geopolitical victories and the restoration of Russia’s sta-

tus as a global power. Beyond being regarded as an omnipresent president, Putin is cast as a respected world leader who helps resolve geopolitical issues created by ‘the West’, i.e. the United States (US).

This messaging helps divert attention away from Russia’s difficult economic situation. In Putin’s first two terms in office, his personal rating was mostly driven by the country’s increasing economic prosperity. However, this has changed since the global economic crisis, the fall in oil prices and European Union (EU) and US sanctions, and Russia has failed to recover to its previous GDP growth rates. In light of this development, Putin has shifted his rhetoric from delivering on economic growth to restoring Russia’s global power status.

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Putin’s recent promises seem to have resonated well with the population, as his current ratings suggest. However, it has also meant a more confrontational Russia in international relations, predominantly in its relations with ‘the West,’ which has been cast in the role of Russia’s main opponent in this new narrative. Given the domestic popularity of the new image of Russia as a great power rising from the ashes, Putin will likely seek to place this at the forefront of voters’ minds in the run up to the elections. While confrontational rhetoric does not necessarily mean a military conflict, sabre rattling and brinkmanship may occur more frequently through 2017.

### **Challenging Economic Context**

While it is unlikely that a strong opponent to Putin would emerge before the vote, he will not leave anything to chance and will try to avoid any potential challenges. The carefully planned handling of the anti-Kremlin opposition, which has been divided and marginalized ahead of the Duma elections, is

telling. Public protests of vocal groups, such as the so-called creative class in 2011-12, or the more recent 2016 truck drivers' strike over road charges, would be particularly unwelcome in the pre-election period. However, Russia's economic outlook for the coming years suggests that such events are likely to occur.

2016 has seen a moderate rebound of oil prices, thus stabilizing the rouble exchange rate, Russian economic output, and inflation in process, though the forecast for 2017 remains precarious. The anaemic GDP growth of around 1.1-1.4 percent is unlikely to help restore a sense of economic prosperity. Over the past two years, many workers in monotowns across Russia have had their working hours (and therefore salaries) cut, negatively affecting local economies where economic dissatisfaction has been simmering.

In 2017, Putin's priority will be to dampen discontent to avoid it spilling over into public protests. The primary vehicle to achieve this would be the state budget. However, the budget has been strained by low oil revenues over the past two and a half years and spending has been cut almost to the bone. The two rainy-day funds – the Reserve Fund and the National Wealth Fund – have shrunk significantly and the government will have to seek additional revenue to maintain even current levels of spending.

The government's desire to try to redress grievances of the economically weaker sections of society with increased social spending in 2017 would necessitate additional increases in budget revenues or borrowing. The state has several options to increase its revenues: draw down the remaining reserves in the sovereign wealth funds, raise taxes, or transfer dividends from state owned enterprises (SOEs) or privatization. It is likely that the 2017 budget will use a combination of these options. The Kremlin may be tempted to impose more quasi taxes on households and small and medium enterprises (SMEs) as they have high collectability. However, some of these measures (for example any attempts to crackdown on the informal "garage" economy that employs 30mn people, as per Putin's own estimate) might prove explosive

in the election year. The government may eventually resort to taxing large businesses instead, potentially the energy sector.

Increased borrowing could come from either the domestic or international financial system, but both options present some difficulties. Borrowing on the domestic market could crowd out lending to the economy, and international markets will likely remain difficult to access as long as international sanctions on Russia are in place in their current form.

Continued economic difficulties and the potential need for external financing may lead to improving relations with the EU and the US. However, moderating his confrontational tone appears at odds with Putin's nationalist project and brings only potential benefits. It is more likely that the stand-off will be used to shift the blame for a difficult economic situation on external factors and cast the government as the protector of the nation from negative external influence, or even anti-Russian conspiracies.

In any case, any anti-Putin feelings will likely be muted, unless there is a catalyst for mass protest. This could include an acute budget crisis, tax increases or similar economic policy issues that hit the population directly. Should such protests in the pre-election year occur, Putin will likely search for a scapegoat among the ranks of the administration. Prime Minister Dimitri Medvedev, the government and the Duma keep sliding in the ranks, regardless of a recent general elections victory for the United Russia party. Putin could easily shift responsibility for the economy, possibly disposing of the most unpopular ministers in highly televised ways.

### **New Elites**

Meanwhile, Putin will also be preparing for his next six years in office. Shifting economic conditions and a nationalist project have exposed the weaknesses of the existing elites, in regards to their ability to deliver desired results to the establishment, but also their proverbial corruption and flashy lifestyles. Those deemed as incapable will likely be replaced. This process has been under-

way for over a year, beginning with the dismissal of one of Putin's closest allies, Vladimir Yakunin, the head of Russian Railways, a service notorious for its inefficiency, and continuing with Putin's chief of staff, Sergei Ivanov, in August 2016.

Moreover, a generational change of ruling elites is well overdue in what will be Putin's eighteenth year in power. The recent Duma elections will likely be taken as a gauge of who is delivering the desired results and who is likely to be dismissed. The changes are most likely to occur in the government's administrative ranks and in regional governments, while the key economic and foreign policy makers will probably remain in their positions.

Who will step up to replace these elites is perhaps even more interesting than who will be dismissed. A new type of elite, typically but not exclusively with a background in security services, is moving up the ladder. These individuals tend to be personally trusted by Putin, share his world view and aim to restore Russia's status as a global power. In contrast with the flashy early 2000's power generation, they are best described as low-key, effective operatives.

The new elite will bring its own distinct characteristics and stamp on the system. Given their background in government services, they tend to be statist in their view of the economy and likely to bring increasing emphasis on regulation. At the same time, they share suspicion of external influences and will view foreign investment with an increasing dose of caution. Finally, the background in security structures combined with an increased focus on Russia's power status will almost inevitably make the new elite more confrontational vis-à-vis 'the West' than the outgoing, profit-driven class.

### **Regional Polices Will Make for a Tense Environment**

It is likely that Russia's aims in its immediate region will not shift significantly; the priority remains a consolidation of Russia's own sphere of influence. As a result, relations with the EU will likely be tense, but manageable, with the like-

ly return to some degree of pragmatism. However, a return to the cooperative relations preceding the Ukrainian crisis is unlikely and relations will remain confrontational in the medium-term, if not for longer.

Ukraine will likely remain the focal point of international contention, even though it may be at times eclipsed by other developing crises or one-off events. Russia's aims in Ukraine will likely remain unchanged: to stop Ukraine from any westward (EU and NATO) integration in the short term and to return it to Russia's own geopolitical orbit in the medium term. For this purpose, the Kremlin has pushed for two possible scenarios. First, federalization of Ukraine, where eastern regions would likely block westward integration of the country; or second, a frozen conflict in the Donbass region, relying on the EU and NATO member's unwillingness to accept a country with an unresolved military conflict on its territory.

As federalization appears politically unfeasible in Ukraine (the parliament is majority pro-Western and would not vote for such a change to the constitution), Russia will likely work towards a frozen conflict in the Donbass. This means stabilizing separatist rule in the territories they control and ensuring provision of basic services for the population, as well as the gradual restoration of at least some level of economic activity. For these purposes, separatist advances to take over areas of strategic or economic significance – such as power plants, water reservoirs and industrial areas – along their boundaries appear inevitable. As a result, cyclical flare ups of violence during times of convenient weather conditions should be expected. Similarly, given that eastern Ukraine's landscape is defined by a lack of natural boundaries, this conflict is unlikely to ever be completely frozen and occasional skirmishes or exchanges of power will likely be characteristic in the near future. The tension may be specifically high in the run up to the presidential elections in the winter of 2017-18 as geopolitical tensions appear to boost Putin's popularity ratings.

However, the Kremlin will take care not to jeopardize its aim of gradually wearing down the resolve of the European Union to maintain economic sanctions imposed over the 2014 war in the Donbass in place. For this purpose, given that the decision to extend the measures requires unanimity, Russia will likely try to lobby individual members of the EU to speak out against the renewal of sanctions at times when their sunset clause falls (January 2017, and likely again July 2017). Eventually, this will probably lead to the easing of sanctions, though not their complete removal. The sanctions most likely to be eased are those affecting the financial and energy sector, but those on defence equipment and dual use technology will likely remain in place.

Elsewhere, Russia may occasionally be preoccupied with re-flares of violence in Nagorno-Karabakh as has been the pattern over the past two years. Increasingly, Moscow will have to pay attention to the developing domestic context of the countries that have joined its Eurasian Economic Union, particularly Armenia and Kazakhstan, where economic grievances are driving anti-government protests. Russia will likely lend a helping hand to political leaders that will ensure a continued alliance with Russia, but this may prove to be destabilizing (as it did in case of Russia's support for the ousted Ukrainian president Viktor Yanukovich in 2014). Such a situation could arise in Kazakhstan, in the unlikely case that President Nursultan Nazarbayev chooses a successor who is not to the Kremlin's liking.

Finally, it is unlikely that Russia would fulfil the much discussed scenario of attacking the Baltic States on the North-Eastern flank of NATO. Such a move would be inconsistent with the current Russian military doctrine focusing on plausible deniability and hybrid warfare. However, it is likely that the Kremlin will continue to foster its military capability in the two NATO facing military base areas – Kaliningrad in the North and Crimea in the South. This may be a source of contention with NATO and its European members in the run up to presidential elections, when military posturing by Russia will likely reach its peak.

### **Globally, a Mixed Picture**

On global level, Russia's priority remains to push for a shift away from US dominance towards a multi-polar global structure of relations. In such a structure, the big powers would all have their own economically and politically integrated blocs and exchange security guarantees with each other. This suggests that while Russia may try to build good relations with other powers, such as China, there is a certain self-limiting quality to these efforts. In any case, 2017 will likely be dominated by Russia's relations with the new US administration.

The context of likely confrontational behavior by Russia in 2017, though not necessarily any military adventurism, suggests this pattern will continue and deepen. In fact, it may be convenient for the Kremlin to play up tensions with the White House in the run up to presidential elections to emphasize Putin's role as leader on the global stage and the opponent of US world dominance. However, for domestic purposes, the Russian media, which is largely Kremlin-controlled, can play up the tension without any actual deterioration of relations. Although unintended transmission of the message to international audiences or accidents cannot be ruled out, this exaggeration of rhetoric at the presidential level would not necessarily hamper pragmatic operational relations on lower levels, such as the coordination of military activities in Syria.

In the Middle East more broadly, Russia will likely seek to continue restoring its lost Soviet-era influence. Tactics will likely be those typically used: foster individual and political forces that appear to be best aligned with Russian interests. This generic tendency appears in many forms, be it Russia's direct military support of the Assad regime, the renewed friendship with Turkey, or outreach to Iran the moment that international sanctions were lifted. It is in the Middle East where Russia believes it has a place at the decision-making table with the US again – a perception which Putin will continue to foster.

Putin will likely seek to announce some major strategic achievement in the region in the run up to elections, which may complicate relations with the US. For example, Russia may push for a new security arrangement in the region that could rival NATO. Russia took such a step in 2008 after the war in Georgia via the creation of the Caucasus Stability and Cooperation Platform, which excluded NATO but included Turkey and Russia as regional peace-makers. Overall, Russia will continue to actively seek new partnerships; how deep those relationships become remains to be seen.

In regards to other powers, Russia will likely continue to focus on China in 2017, although some emphasis will be placed on developing relations with India, too. Three years ago, when relations with the West started to sour over the Ukrainian crisis, Russia envisaged an expansion in the trade and investment relationship with China as a way to redress the economic losses from the geopolitical fall out. However, the results fell well short of expectations. In 2015, mutual trade in monetary terms dropped significantly on the back of declining oil prices and the ruble exchange rate. Chinese investment in Russia collapsed completely in 2014-15 and has only been slowly recovering. Chinese banks have so far failed to replace large global banks as a source of long-term financing for the Russian financial sector. While some successes have been achieved more recently, large infrastructure projects have been hampered by a mismatch in interests on both sides, and Russian suspicion of Chinese investment as a source of political leverage. It is likely that some progress on joint projects – for example, far-eastern railway projects – will be achieved (or at the very least announced) in 2017, these achievements will likely be marked by the self-limiting characteristics of Sino-Russian relations: lack of mutual trust, drive to build their respective power positions in global politics and a mismatch in interests. In the long term, the growing Chinese influence in Central Asia may also start to be a point of contention between Moscow and Beijing.

## Doing Business with Russia in 2017

In the year 2017, geopolitics will dominate the domestic public debate, as Putin's reputation depends ever more on global power positioning rather than on Russia's faltering economy. The global stage provides an exhilarating theater for the masses to be distracted from tenuous economic realities at home. Nonetheless, it makes confrontation on the international stage almost inevitable, albeit likely just fustian in nature.

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This year will likely showcase processes and influences that will later dominate Putin's next term in office: increasing focus on the restoration of Russia's global power status and the generational change that will bring officials with a more statist view of economy into the fold. The two processes will likely translate into an increased suspicion of foreign businesses and efforts to wean off imports. This will lead to greater pressure to build local production facilities in a wide variety of sectors considered to be strategic, from pharmaceuticals to telecommunications. Pressure to completely replace some imports with domestic production will likely increase. More regulation, licensing requirements and constraints on technology transfers will also be likely. The use of economic tools in foreign policy, such as sanctions, import bans or restrictions on health and safety grounds, will likely continue. Foreign businesses may thus face increased compliance and insurance costs. Finally, foreign businesses will remain potential victims in the geopolitical cross-hairs for the foreseeable future and may need to seek new personal contacts as elites change.

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