

## LOOKING AT THE FUTURE OF RUSSIA AFTER VLADMIR PUTIN REELECTED AS PRESIDENT

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### INTRODUCTION

The Russian Presidential Election was held on March 18, 2018. As previously expected, incumbent Russian President Vladimir Putin won the election with a 76.69% share of the vote, and he will serve another six years through 2024. With this landslide victory in the election that was widely interpreted as a vote of confidence, the Putin administration achieved the goals of gaining high public trust and showing the country's solidarity both domestically and internationally, largely as planned. Meanwhile, the administration has faced a lot of challenges, including sluggish economic growth, little progress in structural reforms, and Western sanctions against Russia. In this report, we will discuss the future of Russia by looking at Russia's economic and foreign policies, including those toward Japan, as well as the question of who will replace Putin, which should come increasingly to the fore toward the end of his term.

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### ELECTION RESULTS AND ASSESSMENT

At the Russian legislative election held in September 2016, there was only a turnout of 47.9%. As such, the Putin administration's target of achieving a high turnout and a large share of the vote in the most recent presidential election was thought to be difficult. If the election results were too different from the opinion polls and exit polls, it could trigger a protest among voters and the legitimacy of President Putin's "victory" would be damaged. After the previous presidential election, there were large-scale protests against Putin. This time, President Putin ran his campaign in a way that would give him an overwhelming victory, while seeking a result that would be satisfactory to most voters and most of the international community. One of the measures taken was changing the election date to the fourth anniversary of Russia's annexation of Crimea. In Russia, the approval rate for President Putin, which had been about 60%, surged to over 80% after the annexation of Crimea. On the election date, various events were held across Russia to boost patriotic sentiment in a display of public praise for Putin's achievements, including the annexation of Crimea, as the strong President of a strong Russia. Voters were lured to the events and encouraged to vote for Putin, which led to particularly high voter turnout in the Republic of Crimea and Sevastopol City, each with over 70% (vs. 42% and 45%, respectively, at the legislative election in September 2016). Putin's share of the vote also topped 90% in these areas. In addition, public officials were mobilized nationwide for the voting. Public officials here refer to not only those working for the federal and local governments, but also those whose salaries are paid by the federal government budget, such as members of the security forces, police officers, doctors/nurses, teachers, employees of state-owned companies/banks, and those engaged in housing management services, as well as their families. Other measures to boost voter turnout included selling foods at a bargain price at temporary stalls set up in the polling station.

The presidential election was conducted peacefully overall, although there were some irregularities including ballot rigging and certain candidates being refused the right to run for president. Voter turnout was higher than that of the previous presidential election, and Mr. Putin's share of the vote was the highest on record (Figures 1-2). With the majority of the electorate voting for Putin, the administration apparently achieved its target.

**Fig. 1 Results of 2018 Russian Presidential Election (Top 4)**

Name of Candidate	Party	Vote share (%)
Vladimir Putin	None	76.69
Pavel Grudinin	Communist Party of Russia	11.77
Vladimir Zhirinovskiy	Liberal Democratic Party of Russia	5.65
Ksenia Sobchak	Civic Initiative	1.68

Source: Created by MGSSI based on Central Election Commission of the Russian Federation data

**Fig. 2 Turnout and Vote Share of Winning Candidates in Russian Presidential Elections**

Year	Winner	(1) Vote share (%)	(2) Turnout (%)	(1) x (2)
1996	Boris Yeltsin	53.82	69.40	37.35
2000	Vladimir Putin	52.90	68.70	36.34
2004	Vladimir Putin	71.31	64.38	45.91
2008	Dmitry Medvedev	70.28	69.81	49.06
2012	Vladimir Putin	63.60	65.34	41.56
2018	Vladimir Putin	76.69	67.54	51.80

Source: Created by MGSSI based on Central Election Commission of the Russian Federation data and media reports

## EYES ON INVESTMENTS IN MEDICAL AND HEALTHCARE FIELDS, SUPPORT FROM JAPAN-RUSSIA ECONOMIC COOPERATION

Attention will now turn to the nature of the policies that will be implemented over the next six years. In his Presidential Address to the Federal Assembly given on March 1, 2018, President Putin revealed his de facto manifesto for the next term, including the following economic goals: (1) Increase the proportion of government spending in healthcare to 4% of GDP; (2) Accelerate urban development and infrastructure building; (3) Invest 11 trillion rubles in regional road construction over the next six years. Urban development and road construction in rural areas are not only aimed at replacement of aging infrastructure but also at boosting the economy through public spending. Japanese companies will be able to export technologies for building infrastructure and relieving traffic congestion, as some players have taken part in road construction projects in Vladivostok's urban development in the past.

In addition to infrastructure development, Putin's agenda focuses on medical and healthcare. The goal of increasing life expectancy is at the top of the list and has been set out in the Russia-Japan Eight-Point Cooperation Plan. Investments in drug development and manufacturing as well as hospital construction projects in Russia's Far East are already underway. The targets in the medical and healthcare fields will be included in the Executive Order to be signed by the president on May 7, as major national development goals. The Executive Order is not legally binding, but President Putin can thereby demonstrate that he is well aware of the problem and committed to improving the situation.

According to the Russian Federal State Statistics Service, Russia's average life expectancy was 72.9 years (as of February 2018) and it is expected to rise to 75.12 years by 2024 and 77.22 years by 2030. In line with the Presidential Address to the Federal Assembly in March, President Putin decided the outline of the Executive Order, which includes some numerical targets, including the goal of increasing average life expectancy to 78 years by 2024, and 80 years by 2030. Based on the information provided by the Japan-Russian Trade and Investment Promotion Organization, the three leading causes of death in Japan are cancer (28.9%), cardiovascular diseases (14.9%), and pneumonia (8.8%), while in Russia, these are cardiovascular diseases (37.7%), cerebrovascular diseases (22.6%), and cancer (12.9%). The high mortality from cardiovascular and cerebrovascular diseases in Russia is apparently attributable to high consumption of alcohol and other dietary

habits. The said organization pointed out that such diseases are “preventable”, and Japan possibly will be able to make a significant contribution on this front.

While we need to wait for the announcement of the Executive Order to understand what policy measures President Putin will actually take to fulfill his campaign pledges, it seems that a wide range of areas in medical and healthcare, such as prevention of diseases, diagnosis, treatment, and rehabilitation, will be covered. In his Presidential Address to the Federal Assembly in March, President Putin stated that he would set up a clinic in towns with populations of 100-2,000, and deploy a mobile health clinic in villages with populations of less than 100. Construction of clinics and enhancement of rural and remote medicine will provide business opportunities for Japanese companies.

In addition, exports of Japanese medical services and medical equipment to Russia are expected to increase on the strength of economic cooperation initiatives between Japan and Russia. Prime Minister Shinzo Abe apparently plans to participate in the St. Petersburg International Economic Forum to be held on May 24-26, and the Eastern Economic Forum to be held in Vladivostok on September 11-13, both of which President Putin also looks set to attend. The dialogue between the two leaders will likely facilitate bilateral economic cooperation.

Meanwhile, some observers said that President Putin is now able to sit down and negotiate with his Japanese counterpart over the Northern Territories. However, it seems unreasonable to associate the presidential election, which Putin looked set to win, with the territorial issues. Japan is eager to approach resolution of such issues, through such measures as conducting joint economic activities on the disputed islands and making it easier for former residents to visit the islands. Russia has agreed to hold talks, but it has also moved ahead with military buildup on the islands claimed by Japan and in the neighboring areas, by deploying the newest surface-to-ship missiles in the Kunashiri and Etorofu islands. As such, there are many hurdles to overcome before meaningful progress can be made in the negotiations.

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## **US UNLIKELY TO LIFT SANCTIONS AGAINST RUSSIA, WHICH HINDERS ECONOMIC GROWTH OF RUSSIA**

In the Executive Order to be issued on May 7, President Putin decided to include the following goals: (1) achieving economic growth faster than the world’s average; (2) improving living standards and income; (3) supplying housing to 5 million families per year; and (4) establishing a mechanism for identifying and developing talent. As described above, the Executive Order is not a promise that must be fully realised. Rather, the president conveyed the message that he is well aware of the problem and committed to improving the situation. That said, achieving (1) and (2) looks challenging.

The IMF projects Russia’s real GDP growth rate will be 1.5-1.8% in 2018-22. As crude oil prices are not expected to rise significantly, it is not easy for Russia to achieve economic growth faster than the world average. To boost sluggish economic growth, Western countries’ sanctions against Russia need to be eased or lifted, as such sanctions have placed a burden on Russia’s economy. The Putin administration also needs to push ahead with structural reforms, including downsizing of the state-owned sector. However, being able to carry out both of these is unlikely.

Meanwhile, the conflict in Eastern Ukraine, which triggered the sanctions against Russia, has caused a deadlock, although Russia and the US have discussed possible UN peacekeeping operations in the region. Russia apparently thinks that it is strategically important to keep Ukraine, which is seeking a closer relationship with Western countries, under its influence, and to prevent Ukraine from joining the NATO and/or the EU, even if the US and certain European countries impose sanctions on Russia. Russia allegedly interfered in US and French presidential campaigns by hacking computers and spreading disinformation. What is more, it is suspected of attempting to kill a former Russian double agent and his daughter in Salisbury, England, leading to the expulsion

of diplomats on both sides. Many view that the current relationship between Russia and Western countries is the worst in the post-cold war era (as US State Department officials have said).

In the past, Russia's military intervention in neighboring countries, such as Georgia (Russian-Georgian War) in 2008 and Ukraine (annexation of Crimea) in 2014, were mainly aimed at eliminating a threat to its national security. Recently, there is a widespread belief consistent with the view that "Russia has used old and new forms of aggression to undermine our open societies and the foundations of international peace and stability", as President Trump's former national security adviser Lt. Gen. H.R. McMaster said. One such example is the alleged interference in election campaigns in other countries, despite elections being the foundation of democracy. If the attempted murder in Salisbury was actually carried out by Russia, as the US, the UK and others suspected, it will have been the first case since the end of World War II in which a chemical weapon was used in Europe by Russia, in violation of the international treaty. As such, there is a growing sense of crisis in the US and Europe that Russia is targeting the whole of Europe.

In the annual Presidential Address to the Federal Assembly, President Putin demonstrated his determination to focus on national security and not to fall behind the US in the development of weapons, by showing a video of new missiles and other weapons, and advocating a military buildup. Given that such a stance is widely supported by the Russian people, the relationship between Russia and the West is unlikely to improve soon. We should continue to pay utmost attention to the possibility that the deterioration in diplomatic relations could significantly affect business activities.

Judging from what I have learned from high-ranking government officials and lawmakers in the US in the past month, one of the purposes of enacting the 2017 Countering America's Adversaries Through Sanctions Act, targeting Russia, North Korea, and Iran was to issue a warning to Russia from a diplomatic perspective, and the Act has been implemented cautiously, with efforts to minimize the impact on business activities, and by giving due consideration to its allies. Meanwhile, there has been no sign of the US easing sanctions on Russia. Indeed, the US imposed additional sanctions on Russia, by designating Russian government officials and businessmen close to President Putin as Specially Designated Nationals and Blocked Persons. It is also planning to impose new sanctions on Russia over its support for Syria. As such, it is unlikely that the US will start to consider easing/lifting the sanctions any time soon. Although relations between the two countries is said to be the worst in the post-cold war era, as previously stated, the US and Russia have continued to cooperate in the areas of scientific research, protection of the environment and ecosystem in the Arctic, as well as in space exploration (e.g., using a Russian spacecraft to carry US astronauts, joint operation of the International Space Station). If such cooperation in the Arctic and space development projects are reduced or terminated in the future, it would warrant caution, as that could be interpreted to mean that relations have worsened to the extent that cooperation in such mutually beneficial areas is impossible.

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## **CLOUDED VISIBILITY FOR STRUCTURAL REFORMS**

In Russia, the need for structural reforms was advocated in 2009, when oil prices fell in the wake of the global financial crisis. Then Russian President Dmitry Medvedev tried to push ahead his "modernization" strategy, but his campaign lost momentum as oil prices recovered. Similarly, as the current macroeconomic conditions are stable owing to the recovery in oil prices, a return to positive, albeit slow, economic growth, and a historically low inflation rate of below 4%, the Putin administration does not seem to be highly motivated to carry out painful structural reforms by challenging vested-interests held by state-owned companies, which are led by Putin's inner circle, and/or by raising the pension age, which could provoke negative public reaction. In addition, the Russian leadership appears to believe that the country's economy can do without structural reforms, even if it deteriorates slightly, given foreign reserves that are equivalent to about 30% of its GDP.

Public opinion, which prefers stability to reforms, is also an important factor. Russian people have overcome difficulties in such periods as the 1990s, following the collapse of the Soviet Union, the economic crisis triggered by the global financial crisis in 2009, and the one caused by falling crude oil prices in 2015-16 and US sanctions

against Russia. In particular, the turbulent period in the 1990s was remembered by the Russian people as a terrible experience, in which hyper-inflation was caused partly by reforms amid a shift to the market economy after the collapse of the Soviet Union. As the economy is currently stable compared to the dark 1990s, although the growth rate is low, few people call for structural reforms, which could end up in economic turmoil.

As such, it is highly likely that Russia will keep the status quo, and Dmitry Medvedev is expected to stay in his position as prime minister. Meanwhile, the former finance minister, Alexei Kudrin, who published a newspaper article emphasizing the need for structural reforms, immediately after the presidential election, also appears to be seeking the post. It is said that President Putin tends to decide national security policies by himself, but asks for advice from ministers/advisors on economic policies. As such, the prime minister and other ministers holding positions related to the economy seem to have some influence over the president's decisions on this front. Mr. Kudrin continues to be a proponent of raising the pension age, while advocating the reduction of national defense expenditures and increasing spending for education. In Russia, social security costs, including pension fund finance, account for nearly 30% of total government expenditure, and is the main cause of the fiscal deficit incurred every year. As the budget gap is filled by issuing government bonds and using reserve funds, the need for pension reforms has been recognized, but the implementation of the reforms has been postponed. Given the likely public backlash, the Putin administration is unlikely to carry out pension reforms. However, there is a slight possibility of Mr. Kudrin becoming a minister and undertaking reforms.

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## SUCCESSOR PROBLEM

Russia's constitution limits the presidency to two consecutive terms. As Putin starts his second term through 2024, he needs to deal with the problem of his successor. Possible scenarios are: (1) He will revise the constitution and stay in the post from 2024 onward; (2) He will step down as president but maintain power by establishing a new position; and (3) He will nominate his successor. In his interview with the American television channel NBC on March 10, President Putin did not clearly rule out the possibility of changing the constitution, and said "if voters give me the opportunity to work for another term, I will work, of course, with full force". In another interview with media on the next day of the presidential election, he avoided giving a straight answer, but stated that he had no plans to change the country's constitution for the time being. US experts on Russia believe that it is not easy to change the current regime, in which President Putin is the top decision maker for all important matters, and that Russia may amend the constitution, just as China decided to remove the two-term limit for President. The successor problem will likely come to the forefront from the next legislative elections in 2021. An important issue is whether the ruling party United Russia will be able to win more than two-thirds of the seats that are needed for revision of the constitution. Our eyes are also on generational changes in key government positions, including Director of the Russian Federal Security Service Nikolai Patrushev, as well as executive officers of state-owned companies, as they are mostly President Putin's longtime friends. Any of the scenarios noted above would require support from the public to be realized. The biggest challenge for President Putin for the coming six years will be how to solve the successor problem while maintaining public support, amid likely sluggish economic growth and a hard-line stance against the US and Europe.

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## CONCLUSION

The Putin administration is unlikely to undertake structural reforms, and the economy will probably continue to grow at a slow pace. Russian society after the annexation of Crimea is characterized by (1) patriotism with a desire to restore Russia's great power status, and (2) anti-Americanism and the rivalry with the US, which is trying to thwart Russia's great power ambitions. If the economy remains sluggish and Russian people become frustrated, President Putin might take advantage of such patriotism and anti-American sentiment. More specifically, he might try to increase Russia's presence through such measures as military intervention in other countries, increased illegal activities, and behind-the-scenes activities to influence national election results in Western countries. He might also fuel confrontation with the US and European countries to spark nationalist

sentiment and make Russian people turn away from economic issues. Even if Western countries impose sanctions against Russia, President Putin could demonstrate his strong leadership by not succumbing to external pressure, and maintain public support while forcing them to be patient. Of note, the Trump administration, which fails to develop a clear strategy on Russia, and the EU member states, which differ in opinion as to whether they should focus on the threat posed by Russia or economic benefits, have provided opportunities for Russia to take advantage of the situation. As such, there are lingering concerns over Russia's risk-taking moves in diplomacy. If Russia make such moves, Western countries will probably impose more severe sanctions as a tit-for-tat response. From a business perspective, the long-term investment climate is unlikely to improve, and is more likely to deteriorate. Russia is an attractive market in terms of its market size and growth potential, and it is rich in natural resources. However, companies doing business in Russia should continue to watch for risks such as strengthened sanctions by the US and Europe, subsequent rapid changes in exchange rates, and a rise in investment costs.

Note: The original Japanese report was written in April 2018.