Russia is back on the global strategic and economic map. It has transformed itself from a defunct military superpower into a new energy superpower. Energy revenues no longer support a massive military-industrial complex as they did in the Soviet period. Instead, new oil wealth has been turned more into butter than guns. And, after several years of economic growth, Russia has a new “soft power” role that extends far beyond its energy resources. Indeed, the penetrating forces of Russian power in Ukraine, the Caucasus, and Central Asia are no longer the Red Army. They are Russian natural gas and the giant gas monopoly Gazprom. They are also Russian culture, consumer goods, and job opportunities.

A range of new Russian products, a burgeoning popular culture spread by satellite television, a growing film industry, rock music, Russian popular novels, a revival of the crowning achievements of the Russian artistic tradition, and new jobs in the service and other sectors have made Russia an increasingly attractive country for the region around it. Millions of people from the Caucasus, Central Asia, and the rest of Eurasia have flooded into Moscow, St. Petersburg, and other Russian cities in search of work and a better life.

As a result, since 2000, Russia’s greatest contribution to the security and stability of its vulnerable southern tier has not been through its military presence on bases, its troop deployments, or security pacts and arms sales. Rather, it has been through absorbing the surplus labor of regional states, providing markets for their goods, and transferring funds in the form of remittances (rather than foreign aid). Migration to Russia has become the region’s safety valve.

**NATIONAL MAGNETISM**

Russia may not be able to rival the United States in the nature and global extent of its soft power. Harvard Professor Joseph Nye, who coined the term, has defined soft power as emanating from three resources: a state’s “culture (in places where it is attractive to others), its political values (where it lives up to them at home and abroad), and its foreign policies (where they are seen as legitimate and having moral authority).” Nye notes that “the Soviet Union once had a good deal of soft power. . . . Soviet soft power declined even as its hard economic and military resources continued to grow. Because of its brutal policies, the Soviet Union's hard power actually undercut its soft power.” But Russia today is on its way to recovering the degree of soft power the Soviet Union once enjoyed in its immediate sphere of influence. This resurgence is becoming increasingly apparent to careful observers in Eurasia.

As one of the world’s most energy-abundant countries, Russia has since 1999 benefited immensely from the combination of international concern about energy security, instability in the Middle East, and dramatically rising oil prices. It has regained the prominence in global energy markets it enjoyed in the 1970s and 1980s when the Soviet Union, not Saudi Arabia, was the world’s preeminent oil producer. The Russian economy, too, has bounced forward on a wave of high oil prices and increased oil production. Since 1999, Russia’s annual GDP growth has averaged between 6 and 7 percent. The government boasts a healthy budget surplus and record currency reserves. Although Russia’s economy may still be the size of a minor-league Brazil or Mexico, its energy resources seem to give it a shot at the premier league in the future, especially if oil prices remain high.

The striking growth of the economy since 1999 has also begun to change the nature of Russian power and the way it is exercised. Although Russia has retained many of the vestiges of Soviet hard

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power—including nuclear weapons and a massive conventional army—and is now regaining the Soviet Union’s position in energy markets, it is not the superpower of old. New energy revenues have not been used to boost military spending or to revive Russia’s defense industry at the expense of other sectors. On a range of different indices, Russia’s defense spending remains roughly comparable to that of other major military powers like India, Japan, France, and the United Kingdom.

Since 2000, moreover, Russia has gradually begun to eschew the old Soviet approach of emphasizing the maintenance and deployment of its military power to ensure its geopolitical position. Instead, Moscow has moved in the direction of first building up and now starting to use its economic resources to encourage neighboring states to associate more closely with its regional policies. At the same time, Russia’s growing economy, its consumer products, its popular culture, and the persistence of the Russian language as the regional lingua franca for commerce, employment, and education in many of the states of the former Soviet Union have all made Russia a more attractive nation for regional populations than it was in the 1990s.

At this juncture—in spite of the war in Chechnya and repeated confrontations with Georgia in the South Caucasus—no regional state reasonably anticipates a Russian military invasion. Meanwhile, Russia’s Gazprom is the primary provider of natural gas to the Eurasian states and has regained its position in markets like Georgia, where other companies had entered in the late 1990s. The Russian electricity provider Unified Energy Systems (UES) has similarly expanded its markets, especially in the Caucasus and Central Asia, where early energy sector privatizations brought in foreign investors. And private firms like Russia’s Wimm-Bill-Dann Foods have begun to dominate regional markets for dairy products and fruit juices.

If the influx of migrants from surrounding regions continues; if Russian business investment grows in neighboring states; if regional youth continue to watch Russian TV and films and purchase Russian software, CDs and DVDs, and other consumer products; and especially if the heavy hand of Moscow is pulled back and the hand of commerce is extended instead in Russian foreign policy, Russia will achieve the economic and cultural predominance in Eurasia that the United States has in the Americas. However, some skill is required to draw on soft power resources in crafting policy—a fact demonstrated by the current failure of the United States to capitalize on its own undisputed soft power and the global growth of anti-Americanism. And it is by no means assured that Russia’s increasing soft power will be used to positive effect.

**THE NOT-SO-INVISIBLE HAND**

Moscow’s ability to use soft power resources stands in stark contrast with the situation a decade ago. In the 1990s, beset by the upheavals resulting from attempts to liberalize and reform its economy, Russia lost the capacity to continue providing financial subsidies to the other states of the former Soviet Union and thus to maintain its economic attraction. Economic ties were further undermined by Russian decisions—motivated by the necessity of getting its own economy in order—to dismantle the ruble zone and to increase prices of oil and gas exports. This resulted in most regional states incurring huge hard-currency energy debts to Moscow. While it was cash-poor in the 1990s, Russia was still armaments-rich. Having inherited the bulk of the Soviet military arsenal—including bases, personnel, and equipment—it retained a preponderance of hard power outside its territory in other former Soviet republics like Armenia, the Baltic states, Georgia, Moldova, and Tajikistan. This made the newly independent, and weaker, states around it increasingly nervous as the economic benefits of association with Moscow faded. Russia’s cultural standing in the region also fell as the use of the Russian language became a highly politicized issue.

Concerns about the citizenship prospects of millions of ethnic Russians living in the newly independent states on Russia’s borders—especially in the Baltic states of Estonia and Latvia, and in Ukraine and Kazakhstan—fed into a Russian nationalist backlash against the collapse of the Soviet Union. Russian-speakers and co-ethnics became a cause célèbre in political circles in the 1990s. In Moscow, a number of rising politicians boosted their careers as well as honed their rhetorical skills by calling for government action in support of the interests of “Russian-speakers in the near abroad.” In response, neighboring governments rushed to push through new language laws and programs to expand the teaching and use of their indigenous state languages. Russian-speakers were increasingly viewed as a “fifth column” for the reassertion of Moscow’s influence over its neighbors’ domestic and foreign policies.

Coercion involving the deployment of hard power resources to force former Soviet states to
comply with Russian interests served to turn states away from, not toward Russia. Moscow was increasingly perceived as the bully on the block. Over the course of the 1990s, it lost its formerly dominant position in the region as well as the confidence of its neighbors. Only the most desperate countries like Armenia, Tajikistan, and Belarus (beleaguered by civil war, security concerns, and economic decline) clung to close relations with Russia. Countries like the Baltic states, Ukraine, Georgia, and Azerbaijan turned pointedly toward the West.

Russian hard power exertion drew unfavorable attention from Western analysts and policy makers in the 1990s. They saw a revival of Russian imperial ambitions and desires to reconstitute the Soviet Union, albeit on the cheap. This led to a series of policy responses to shore up the independence of the other former Soviet states and to offer them at least a modicum of security from Russian predation. These included the expansion of NATO and extending European Union membership to nations of the former Soviet bloc in Eastern Europe, including the Baltic states. American and other international investors also moved into key commercial ventures in the increasingly attractive energy sector in the Caspian Basin. International investment in Caspian energy development was backed by the US government, which spearheaded the creation of a new east-west corridor for the export of oil and gas to world markets from the Caspian across the Caucasus and Turkey, avoiding Russia as a potential risk and bottleneck. Russia finally reached its nadir in August 1998 with the collapse of the Russian ruble and resulting financial crisis. The 1998 crash diminished Russia’s regional economic standing even further.

**The Turnaround**

The turnaround came in 1999 and 2000 with the start of the post-crisis recovery of the Russian economy. The World Bank and other observers of Russia's economy typically cite a number of factors as key in stimulating economic growth after the crash of 1998. These include price adjustments that provided a stimulus to import substitution and domestic industry, underutilized labor and capital and a decline in real wages, and a series of reforms that led to improvements in efficiency and industrial restructuring. The most significant factor of all, however, was the rise of world crude oil prices from a low of around $10 a barrel in December 1998 to around $33 a barrel in September 2000. This provided a major injection of cash into the domestic economy.

High oil prices were also the major factor in promoting the recovery of Russia's oil industry, which had been adversely affected by the collapse of the Soviet Union and fell into a prolonged period of decline in the 1990s. Beginning in 1993, the industry was gradually carved up and partially privatized. A number of vertically integrated oil companies were established, each combining oil exploration, production, refining, distribution, and retailing, with some companies organized on a regional basis and some retaining a degree of state ownership. The privatization and division of the oil industry made it possible for new economic actors to enter the sector—including the so-called oligarchs. They had no prior experience in the Soviet oil industry but enjoyed access to capital from private banks, which they owned and controlled, and close political connections to government officials.

The sudden infusion of cash from soaring world oil prices into an essentially stagnant industry changed the underlying incentive structure. The oil price rise boosted company revenues even without increases in production, while the 1998 devaluation of the ruble had already significantly lowered ruble-denominated input costs (including labor) for Russian energy producers. After 1999, low input costs and high energy prices proved the winning combination. They gave Russian oil companies the internal capital to improve production efficiency without infusions of new outside investment. And they gave the new oil barons every reason to restructure and improve the management of their assets. The companies brought idle wells back on line, purchased new machinery, and introduced new technology to enhance well recovery.

By the end of 2001, Russian oil production had increased by around 1 million barrels per day to stand at just over 7 million bpd. New infrastructure, including the Baltic Pipeline System and a new oil terminal at Primorsk on the Gulf of Finland, was built to increase export capacity by a projected 12 percent. By 2005, Russia’s oil produc-
tion had bounced back even further to reach 9.6 million bpd—with medium-term potential for still more increases, at least up to 11 million bpd (close to peak Soviet levels of production). Oil exports reached more than 4 million bpd.

High oil prices and Russia’s oil production rebound have proved extremely good news for the Russian federal budget. Natural resources constitute around 80 percent of Russian exports, and oil and gas account for the majority of total exports, making the budget particularly dependent on the energy sector. In fact, 37 percent of budget revenues are provided by taxes on oil and gas. Research by the World Bank and the IMF has shown that each dollar increase in the price of a barrel of oil (Ural crude) raises Russian federal budget revenues by as much as 0.35 percent of GDP.

In short, as a result of the sudden spurt in oil prices and the revival of its energy industry, Russia has seen its economic fortunes vastly improve. And with economic growth, Russia has more to offer its neighbors than a brandished fist. It gradually has become a more attractive country to do business with.

**Political Realities**

This is not, of course, the whole story. Many of the other countries of the former Soviet Union also suffered from financial crises in 1998–1999 owing to the effects of the Russian ruble devaluation on their own currencies. They underwent similar price adjustments and import substitutions, and boosted their own domestic production. And energy-rich countries like Kazakhstan benefited from the same oil price windfall as Russia. As Eurasian economies started to recover and grow, Russia’s neighbors began to look to it as a market for their exports. They sought to purchase new Russian consumer products that were cheaper than imported goods from the West. Dependency on Russia for energy supplies also continued, and debts to Russia grew with higher oil and gas prices.

At the same time, it became clear that aspirations in Ukraine, the Caucasus, and Central Asia for large-scale Western investment and the development of close economic and political connections with the United States, Europe, and other major economic powers would not be fulfilled in the foreseeable future. Beyond limited bilateral assistance and international financial institution loans and grants; membership in institutions like the Organization for Security and Cooperation in Europe and the Council of Europe; and Western investment in large-scale energy projects in the Caspian Basin, such as the construction of the Baku-Tbilisi-Ceyhan oil export pipeline, economic powers apart from Russia had little to offer. The inescapable facts of distance and geography prevailed.

So did political realities. NATO enlargement and the subsequent expansion of the European Union to cover the countries of Eastern Europe seemed to roll back vestigial Russian attempts to reassert influence in Europe. The emergence of new transnational threats to US and Western interests, especially terrorism emanating from Afghanistan and the Middle East, shifted international priorities. It was also evident that, with the notable exception of the three Baltic states, none of the other states of the former Soviet Union was likely to be a viable candidate for membership of either NATO or the EU in the near term. Opportunities among the Eurasian countries for further security, political, and economic interaction, including trade, with the United States and European countries were thus limited.

In addition to the changes in the West’s approach toward Eurasia, Russia’s goals changed when Vladimir Putin came to power. Putin assumed the presidency in 2000 with a pledge to bring stability and order to Russia, and to begin a process of restoring the country to “greatness” by unifying society, stabilizing the economy, and strengthening the state. His priority was on bolstering Russia internally and putting the economy in order, not on strengthening Russia’s external position—at least not in the short term.

The growth of the economy after 2000 made it possible for Putin to pay foreign debts on time and to free Moscow from the huge infusions of foreign financial assistance from the IMF, the United States, and other major bilateral lenders that it had required throughout the 1990s. A balanced federal budget passed into law at the end of 2000 for the first time in post-Soviet history. By the end of 2001, the Russian economy had experienced its best performance since the fall of the Soviet Union. Real incomes grew 6 percent as wages soared by 20 percent and pensions by 23 percent. Official reserves of gold and hard currency also increased. With the ruble relatively stable, investors were more positive about doing business in Russia.

Economic success contributed to extremely high popularity ratings for President Putin in his first years in office. And thanks to the budget surplus, he was able to pay salaries and pensions, and even provide modest increases. This was something his predecessor, Boris Yeltsin, had been unable
to do in the 1990s. As a result, Putin maintained an approval rating of around 70 percent. This in turn enabled him to push through reforms that the previously cash-starved and unpopular Yeltsin had planned but been unable to achieve. In 2001, for example, new legislation was passed on land reform, pensions, and taxes—including the lowering of the personal income tax to a flat rate of 13 percent, among the lowest in the world.

**PUTIN GOES SOFT**

After 2001, Putin began paying more attention to foreign policy. In conjunction with his carefully planned overtures to the United States, he put an end to the freewheeling and chaotic foreign policy of the Yeltsin period. Yeltsin’s dwindling foreign support, combined with his lack of personal prestige within his own inner circle, had led to considerable freelancing by a variety of groups and institutions in their spheres of responsibility or interest. These included the foreign ministry, different branches of the military, the nuclear power agency Minatom, the fuel and energy ministry, the Russian parliament, regional leaders, and the oligarchs. Today, the freelancing has been eliminated: the president and his administration are in charge of the foreign policy agenda. Even the policy functions of the foreign affairs ministry have been largely ceded to the Kremlin.

For many outside of it, the Kremlin remains a black box. The motivations behind individual policy initiatives are still difficult to discern. Nevertheless, from the perspective of its neighbors, Moscow has been somewhat more predictable in its dealings in recent years. And Russia has generally exercised regional power in a different way from how it used to. Investing Russian capital, exporting Russian consumer products and popular culture, and offering access to Russian markets have become increasingly more important in securing Russian interests.

Putin’s annual addresses, other high-level policy statements, and the thrust of Russia’s recent relations with its immediate neighbors would all seem to indicate that Moscow no longer embraces the grandiose imperial ambitions of the Soviet period. But it clearly still has geopolitical aspirations, even if they are more modest. These aspirations are very much focused on the Commonwealth of Independent States (CIS)—Russia’s immediate neighbors and fellow former Soviet republics.

This fact was underscored in July 2004 when Putin addressed a plenary session of Russian ambassadors who had been recalled to Moscow for a special meeting to review foreign policy priorities. Putin stressed that Russia’s priority tasks abroad were “to protect national economic interests, raise the investment attractiveness of Russia, and resist discrimination in foreign markets,” and generally to “serve the cause of the overall development and modernization of the country.” He also reemphasized that the “main priority” remained the CIS. Interestingly, Putin noted that Russia had not yet learned to use “sufficiently well the historical credit of trust and friendship, the close ties that link the peoples of our countries”—in other words Russia’s soft power resources. He stated that “relations between CIS states and Russia should be made as attractive as possible not only for us, but also for them” (emphasis added).

Perhaps most significantly, Putin cautioned against calling for exclusive Russian “leadership over the CIS expanses,” acknowledging that Russia could no longer claim a monopoly over the affairs of the region. While still stressing the importance, as a decade earlier, of protecting “the rights and interests of our co-citizens and our fellow countrymen in CIS and Baltic countries,” Putin also suggested that this might be done by establishing “large information and cultural centers for work with expatriates”—again by soft power rather than hard power means.

Putin’s emphasis on soft power and economic integration suggests something of a departure from Russia’s more traditional heavy-handed and military force-oriented approach to its relations with the CIS. However, hard power is still present and deployable. Saber-rattling tendencies persist, and a real danger remains that “restorationists” in the military and security services, as well as in the Russian parliament, will try to reassert themselves in foreign policy.

The more hard-line circles—the so-called siloviki—in Moscow make their opinions on the means of reconstituting Russia’s authority in Eurasia quite clear in private discussions, as well as in public articles and presentations. They still favor exclusive Russian leadership over the CIS expanses.
that Putin warned against and the use of coercive force to secure Russian interests. Their views are also shaped by the fact that the United States under the Bush administration has been more assertive elsewhere in the world, including in areas of former superpower competition in Asia and the Middle East. The feeling in these circles is very clearly that if Russia now has to leave the rest of the world to the United States, then the United States should leave Eurasia and the CIS to Russia.

Although freelancing has been discouraged, and Putin has repeatedly set forth his foreign agenda, the fact that policy making is now confined to the relatively narrow circles of the Kremlin and presidential administration means that Putin has few elite cadres to rely on to implement a policy based on Russia’s soft power resources. There are many more people sitting on hard power resources on Russia’s borders and in bases in CIS states, sharing views similar to those of the hard-liners in Moscow. They may be tempted to deploy these resources on their own or someone else’s, initiative, and are very difficult to rein in—especially from behind the Kremlin walls many hundreds or even thousands of miles away.

Even so, desires to deploy the hard power of military resources have been tempered to a degree by the debacle of the war in Chechnya. With the high costs of the conflict—including tens of thousands of Russian military and civilian casualties; the total destruction of the city of Grozny, a key refining and training center for Russia’s oil industry; a massive humanitarian disaster; and increasing linkages with international terrorism—Chechnya offers a sobering, negative example of the use of force and Russian hard power. It underscores how quickly and easily the use of military force can become self-debilitating and counterproductive.

**EURASIA’S TWO-WAY STREET**

Other developments in Russia’s neighborhood illustrate the benefits of soft power and turning Russia into an economic magnet. In June 2004, for example, Moscow saw a reversal of negative trends in two key relationships in Central Asia: with Tajikistan and Uzbekistan. In the case of Tajikistan, the government in Dushanbe sought the removal of Russian troops from Soviet-era bases in the republic, and Russian guards from its border with Afghanistan. Although there was still some arm-twisting, the two sides reached a mutually acceptable agreement relatively quickly. Russia secured its troops and military installations—including ownership of a strategic space surveillance center—in return for forgiveness of a portion of Tajikistan’s debts to Russia and new energy investments (which also gave Russia eventual ownership of a hydro-electric power facility). Most important for Tajikistan, it secured an agreement on the entry of its labor migrants into Russia.

With Uzbekistan, Russia signed a new strategic partnership agreement. This marked the end of a decade in which the Tashkent government had drawn further away from Moscow (in part because of poor personal relations between Yeltsin and Uzbekistan’s president, Islam Karimov) and had begun to pursue closer political, economic, and security relations with the United States. The new agreement emphasized not only military issues, including Moscow’s provision of armaments and the training of Uzbek servicemen, but also large-scale projects to bring Gazprom, LUKoil, and other Russian companies into the Uzbek energy sector. LUKoil, for example, undertook to invest $1 billion in a single gas project. Tashkent’s overtures toward Moscow in the weeks preceding the agreement were motivated in part by a souring of its relationship with the United States over Uzbekistan’s failure to pursue economic liberalization and worsening human rights abuses. But the attraction of the Russian energy sector’s huge investment capital potential was evidently a major factor.

The June 2004 agreement with Tajikistan highlighted the increasing significance of migration and labor migrants both for the Russian economy and for Russia’s relations with its neighbors. Indeed, Russia is now a pole of attraction, rather than repulsion as it was in the 1990s, for regional populations. Its economic growth has meant increasing numbers of customers to sell products to and new jobs in the service and other sectors for migrants, as well as for Russians. In recent years, millions of economic migrants, not just from Tajikistan but from elsewhere in Central Asia and the CIS, have poured into Russia in search of work. Regional businessmen and traders have also started bringing their goods to Russia’s markets and stores to take advantage of a burgeoning consumer economy.
This is a two-way street. Growth in CIS states and increasing trade within the CIS benefit Russian manufacturing industries and further stimulate the Russian economy as export demand grows for Russian manufactured goods, fertilizers, and chemicals not produced by neighboring countries. And migrants from the CIS fill growing niches in the lower-paying sectors of the Russian service industry, agriculture, and the construction industry as Russia’s continuing demographic decline produces long-term labor shortages.

In many respects, by virtue of its more limited foreign policy focus on the CIS, Russia is in a better position today to use its soft power resources to positive effect than the Soviet Union was. Part of the attraction of association with the Soviet Union for some of the far-flung members of the Soviet bloc in Cuba, Afghanistan, the Middle East, and Africa was the potential for trade, infrastructure subsidies, technical assistance, and training and education programs in Soviet universities. But the possibility of large arms transfers and the sheer implacability of Soviet military power always tended to eclipse these benefits. The Soviet Union was also overtaxed and overstretched in its abilities to entice effectively. Today in the CIS, Russia can be more focused and draw to its benefit on the cultural, linguistic, and other ties that persist in the region from the Soviet period.

Ultimately, though, the possibility for Russia to change modalities in Eurasia comes directly back to energy. Russia’s new ability to wield soft power resources and expand its economic and political influence comes from its oil power. The increasing windfall from high oil and gas prices since 1999 has spurred Russia’s economic growth, enabled it to push through some important reforms, and afforded it the opportunity to become a “new Russia” at home and abroad, including well beyond the boundaries of the CIS. Oil and gas have made Russia something of an indispensable power on today’s global stage.

THE ENERGY SUPERPOWER

Despite the necessary cautions about the perils of overemphasizing the oil price windfall, energy will remain the base of Russia’s power for the foreseeable future. It will underpin the Russian economy and domestic stability, enhance Russia’s political and economic position in Eurasia, and restore Russia to a degree of its former super-power status—at least as an energy superpower, by making it a player in Asia as well as in Europe, and by increasing its attractiveness to the United States. Its vast energy resources also have the potential to make Russia a different kind of power in the twenty-first century from what it was in the twentieth (although, of course, this is in conjunction with the collapse of the Soviet Union, the end of the nuclear and military confrontation with the United States, and the contraction of Russia’s geopolitical ambitions). Russia today is not the Soviet Union of the past. Russian oil no longer supports a massive military-industrial power and military machine.

This, in itself, could be one of the most significant developments of this decade—especially when one considers the trajectories of Germany and Japan after World War II. Fueled by oil and gas, Russia may yet follow the same path after the end of the cold war. It could become the dominant power in its immediate neighborhood by virtue of its economic growth and new soft power resource potential—not as a result of the old hard power that led it to invade, conquer, and colonize territory in the past. Russian dominance of Eurasia in this manner would be much more palatable, even for the traditional hawks in the United States and the West, who eventually became comfortable with the economic dominance by Germany and Japan of their immediate neighborhoods.

Politically, however, Russia’s soft power potential will not be realized if hard power advocates win out and squander Russia’s developing economic relations with the CIS by resorting to old strong-arm tactics in pushing Moscow’s interests. The tension between soft and hard power advocates remains acute. In addition, foreign policy and domestic policy are intertwined. A harder, more authoritarian line in Russia’s domestic policy could easily spill over into its foreign policy if the siloviki gain the upper hand in Moscow.

This is a time for some optimism about Russia’s economic future and its new role in its region and the world, but it is not a time for complacency. Russia’s partners need to encourage Moscow to take steps to enhance and strengthen the energy sector and to use the revenues it generates appropriately. This is a critical issue not just for Russia, but for a much broader region in Eurasia, as well as for the primary consumers of Russian energy in Europe, Asia, and increasingly the United States.