

Medvedev's Keynote Speech: A Blueprint for Change

By [The Moscow Times](#)

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President Dmitry Medvedev has just finished giving his keynote address to the assembled Russian elite and their would-be partners at the Kremlin's annual investment jamboree in St. Petersburg.

I won't go into the details of the speech; he has said almost all of this before. It is what has become his standard reform fare: remove government from the economy, stamp out corruption, and the points that he made earlier this year during his speech in Magnitogorsk.

It is a blueprint for changing Russia. What encourages me so much is that he has focused on all the right points. As bne has pointed out in recent articles and blogs, Russia is at one of those crossroads that emerging markets seem to be always reaching.

This one among the most significant. Russia is already prosperous. Kirill Dmitriyev, the new head of the Kremlin's \$10bn direct investment fund (RDIF), pointed out to me this week that Russia is now the sixth biggest economy in the world (and second biggest in Europe) and that

the number of people earning \$10,000 per year has tripled in the last six years. The economy has moved incredibly fast.

The problem is that the previous model of growth based on state spending of oil revenues and using up Soviet-era capacity is almost exhausted. As Alexei Moiseyev pointed out in a recent note, "All oil spending will produce now is not growth, but more inflation and more inflation."

In the early stages of reform, not only is the role of government in the economy necessary, it is essential, because the government is the only economic agent with resources, and state spending is the only way of getting the wheels of commerce moving. However, once the economy is moving, there comes a point where the state has to step back and switch to nurturing private business. If it doesn't — many countries have failed to make this change — then the result is stagnation.

What was so encouraging about Medvedev's speech is that he made these points more-or-less explicitly. He mentioned "stagnation" as the danger the country faces. He spoke at length about the need to make the anti-corruption drive work. He reinforced his commitment to removing state officials from big companies and reducing the state's role in the economy. And so on. There will be details galore in tomorrow's papers. In short, Medvedev "gets it"; I really don't have any criticism for the plan he laid out.

But there is the rub: The plan is good, but the president doesn't have the power to put it in place. Indeed, Medvedev and Prime Minister Vladimir Putin to a great extent personify the two stages of emerging-market development. Whereas Medvedev is all about nurturing, Putin is clearly the "Big Push" guy, the one that did the pushing and started Russia's rapid rise.

And Putin's time is over. He needs to step back and give Medvedev his head. There is still a role for the state in the economy, but if Russia is to fulfill its potential, then the state must withdraw, and Medvedev just laid out a pretty detailed plan on how this can be done.

Things are not entirely black. The Moscow Times recently listed Medvedev's promises from last year ([story](#)), and I was encouraged to see that about half of them have already been fulfilled — at least the legislative parts — and another quarter is in hand. Medvedev is not the lame duck he is made out to be, but clearly Putin is the one who is in charge, and Medvedev's power is very limited.

An optimist on Russia — like me — can hope that while reform is clearly on hold ahead of the twin Duma and presidential elections in December and March, once political stability returns — following the re-election of the Medvedev/Putin duo — there will be a significant acceleration of reforms. I predict that the two big themes for 2012 will be investment and pension reform, both of which could be transformational for the economy.

That was another positive aspect to Medvedev's speech: In the 1990s, these speeches were all about attracting investment, because the Russian government — and indeed all emerging countries — needed cash, aka investment. However, while investment is still high on the agenda, the purpose of this investment is not cash, but know-how. The goal now is all about system change, not making money. Making money is a by-product of system change.

This is a way more sophisticated understanding of the problems that Russia faces and is in itself an important aspect of modernization.

I say again that the Duma, not the presidential elections, will be key. Putin is an obstacle not because of his ideas or his control but because of his very existence.

The way power works in Russia is that once someone gets it, everyone around him begins to invest heavily in patronage, connections, pay offs and inter-dependencies — what Russians call their krysha, or "roof." Putin needs to do nothing, and this network will build up around him. That is the price you pay for a "managed democracy," half-way between an autocracy and an open market.

Putin has done so much and been there so long that this network is like cancer that has spread throughout the body politic and the economy, and even if Putin chooses to step back, it will continue to function and stymie all those things Medvedev has just talked out.

Image what would happen if Putin resigned in December. It would be a revolution, and in the process of remaking the system, Medvedev could make all those changes he just mentioned. My fear is that the ever-cautious Putin will go for the other option: engineering his constitutional majority in the vote, which will only reinforce the existing web of vested interests and make it, at best, extremely hard for Medvedev to make these changes. The upshot will be that Russia will continue to move forward as it has done over the last decade. But the danger of stagnation increases, and the first symptoms are already there: capital flight, and the desire of young people and members of the elite to leave the country.

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