Centre for Air Power Studies (CAPS)
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De-Dollarisation, De-Offshorisation and Diversification

The 3Ds of Russia's Economic Revival Programmes

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The contemporary international milieu has put to test Russia's economic endurance. Uncompromising sanctions by the West are putting pressure on Moscow to disengage itself from Ukraine. Russia is seen grappling with its economy as the coercive measures have plunged the value of its currency and set oil prices leading southwards. In such a scenario, it is important to evaluate the efficiency of Russia's current economic policies and its ability to tolerate further impact of sanctions. More importantly, would Russia's resurgence be affected as a consequence of the ongoing economic conflict? To what extent will alternative economic policies assuage Kremlin's current economic status? Will Russia succeed in somehow gaining from the sanctions and get the country out of the energy riddle?

As an attempt to isolate and punish Russia, the US and OPEC member nations have pursued a shrewd strategy by refusing to consider oil production cut.[1] As a result, the fall of oil prices, has triggered fear and shock in Russia which has predominantly depended on oil markets for its hard currency revenue. This has left its economy at the mercy of a market that has seen prices drop 60 percent since June to under $46 a barrel.[2] This has however been a blessing in disguise for the US as the booming shale production has turned the United States from the world's biggest oil importer into one of the top producers, pumping out over 9 million barrels per day.[3] Accordingly, many fear that Russia may have engineered its own downfall by relying more on energy markets as its primary financial resources.

However, it is important to explore other factors before pronouncing a premature judgement on Russia's fate. To begin with, Russia has diversified its global portfolio of political options and has advanced in the international system. Russia now has the potential to retaliate as it has smartly resorted to energy supplies as leverage to counter the Western policy of containment. Moscow recently cut energy supply completely in few European countries which include Bulgaria, Greece, Macedonia, Romania, and Croatia. Many more are expected to follow. Gazprom move to cut gas exports to Europe by 60% has plunged the continent into an energy crisis. Russia also stated its plans to shift all its natural gas flows through a proposed link under the Black Sea through Turkey, fully replacing shipments via Ukraine. Hence, Europe will have to develop new infrastructure that will transport gas to the rest of the continent.[4]

However, Putin's move to put pressure on EU to reconsider its position on the sanctions imposed on Russia may hurt its reputation as a reliable gas supplier as the move during peak winters will only make Europe more vulnerable. Moreover, such measures by Russia will have negative impact as 1) It will compel Europe to reconsider its dependence on fuel exports on Russian energy markets in the coming future 2) US may replace Russia as the main energy source to the European zone through shale revolution.

Nevertheless, the following are the three economic measures initiated by Russian President Putin to stabilise the value of its currency and revive Russian economy despite depleting oil prices. They are:

a) De-Dollarisation b) De- Offshorisation and c) Diversification

De- dollarization- Russia recently unsealed nearly $88 billion reserve fund and converted some of its foreign-currency holdings into rubles. This means that it is buying rubles and selling foreign currency holdings and in particular selling US Treasury Bills denominated in dollars. Buying rubles on a large scale means increasing the demand and hence, the price of rubles. In addition, timely intervention by Russian government through the current economic reforms propelled the ruble to recover some lost ground which bounced back to 60 rubles per dollar.[5]

Moreover, de- dollarization, if it succeeds will have a major impact on US currency value in Russia. This will in turn devalue the US dollar position which will dethrone the 'petrodollar' (means for settling international trading in oil). Alongside Russia, countries like China are intended to weaken the petrodollar by promoting the use of their own currencies for trading oil and for other commercial transactions which will come in the form of bi-lateral currency agreements. For example, the $400 billion Russia/China natural gas deal is actually a zero dollar agreement. Payment for the gas will be settled in rubles and yuan, thus avoiding transactions in US currency.[6]

However, although de- dollarization may cause the dollar to depreciate, it is doubtful whether it would make much of an impact as the US dollar is the international reserve currency and there is always demand for it elsewhere.

De-offshorisation- means taxing the profit of foreign companies and the incomes of foreigners. In other words, it means controlling foreign companies that prevents them from having an advantage over domestic enterprises. This will be achieved by introducing taxes that are levied heavily on the foreign company and are easy on domestic enterprises. This measure will help Russia as it prevents entrepreneurs from off shoring their profits thereby causing each penny to be accountable to tax and thus preventing the most common form of tax evasion. It will also increase state revenue and at the same time the government does not become despotic in levying more tax from its own population. This also means that the gas profits won't be drained away to other countries; instead part of them will be spent within Russia as demand for Russian goods would increase locally.

As for *diversification*, to avoid a perilous impact on Russia's already struggling economy, Moscow has now sought to diversify its energy markets other than the European zone. As a result, more recently Russia and China signed a 30-year agreement worth $400 billion for the purchase and sale of natural gas between China National Petroleum Corporation
and Russian gas giant Gazprom. This alliance between Beijing and Moscow has however sent warning signals to the West which now needs to be more watchful.[7]

Russia is also tapping into those defence market which are either looking for diversification of its defence purchases or for a stable defence market. Knowing Pakistan's urge to upgrade its defence equipments and need for reliable defence market; geographic diversification of defence export destination has led Moscow to begin defence cooperation with Pakistan to fund its defence industrial complex. More importantly, Russia has imposed an embargo on food imports from countries that participated in sanctions against it. Therefore, import substitution from domestic producers and other countries will lessen the impact on Russian consumers. Russia is also thinking of diversification of its economic resources although it is still not clear whether the Russian state has the institutional capacity at the cost of disengaging its ties with Europe and the US. [8]

It is true that the Western sanctions have adversely affected Russian economy, but Putin has remained strong in pursuing an autonomous foreign policy especially on the Ukraine issue. The above mentioned economic measures should not be seen as an absolute solution to the crisis but even if it achieves the desired aim; it will still take a couple of years to overcome the current crisis. Above all, the people of Russia have demonstrated courage and unprecedented resilience in times of crisis that has rocked the nation. Their display of confidence in their leader and his policies will be a key aspect in resonating Russia's image as a sovereign and assertive player in the new global security architecture.

(Disclaimer: The views and opinions expressed in this article are those of the author and do not necessarily reflect the position of the Centre for Air Power Studies [CAPS])

End Notes

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[5] Arun Mohanty, "Russia at Crossroads", Mainstream, vol. LIII, no. 1, December 27 2014. Pg. 1.

[6] Interview- Marin Katusa: Startling Rise of 'The Colder War' With Anthony Wile, *The Daily Bell,* November 02, 2014 http://www.thedailybell.com/exclusive-interviews/35783/Anthony-Wile-Marin-Katusa-Startling-Rise-of-The-Colder-War/ Accessed on 16 January 2015

[7] Ibid

[8] Peter Rutland, "The Impact of Sanctions on Russia", *Russian Analytical Digest*, No.157, December 17, 2014. Pg. 5. www.css.ethz.ch/rad Accessed on January 12 2015
