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## From the author

This booklet is based on the last two chapters of the book, which was released in January 2012. This is the 2nd edition of the paper “Will democracy settle down in Russia”. Two circumstances caused the preparation of this booklet.

The first is the feeling that an independent, separate discussion of these issues set out in two chapters, alternatives and prospects of Russian after market reforms of the 90’s, the transformation of the crisis and restoring growth in “zero” years with some clear movement within political stability — even without all theoretical and empirical studies set out in the 2nd edition — can be helpful.

Second, after I became a part of collective of professionals working on behalf of the government over the “Strategy 2020” under the expert sites HSE and ANHGS, I find very important to publicly state my own position, so that later no one could say that, after turning into this collective, I changed it in favor of the official line. To be perfectly clear, I believe quite radical institutional changes are absolutely necessary for the real modernization, including a full-fledged political democratization, in whatever terms they may be implemented. And at the same time, under the circumstances, would have preferred a gradual development, with no state of emergency.

When I wrote Part I of this brochure, I did not expect any significant events likely to change something in Russia unexpectedly. Though, then after rereading the brochure, I realized that it is riddled with the expectation of change and sorrow over their low probability.

Then came December 4, 2011. I note: exactly 20 years after the start of market reforms. It would seem as ordinary Duma elections. And in fact, a sharp turn: how one American newspaper wrote, the Russian again showed a taste for democracy. And once again I had to think over the possible developments after this turn. The point, as I understand it, can be expressed simply. Post-communist Russia needed two major institutional shifts: in the economy — from plan to market, in politics — from totalitarianism to democracy. The first part of the work was done under the leadership of Yegor Gaidar, but with delays in democracy. It seemed that democracy is not our destiny and our country, having the highest potential for development, won’t build a market democracy. But no! The elections in December 2011 showed that there are opportunities. Which ones, how to use them — these are issues that deserve to be discussed.

# Part I

## Not expecting major changes

### 1. Modernization

#### The main ways of Russia' development

Over the past 20 years, Russia has a lot of crucial directions, which would be enough for 200 years and a dozen countries. Only since perestroika three directions of exceptional importance was used.

I remind them:

- 1) *democratization or the empire*: the choice is made, M.S. Gorbachev, the Soviet Union eventually collapsed. Gorbachev did not want the collapse of the empire, but the democratization plus the growth of the economic crisis predetermined the outcome;
- 2) *central planning or the market economy*: the choice is made, B.N. Yeltsin, and as a result of liberal reforms we have a market economy. Not so effective as we would like, but it works. However, to have market reforms in the early 90's we had to some extent to let down democratization;
- 3) *the bureaucracy or oligarchy*: the choice is made, V.V. Putin. The conflict emerged in 1997 and slowly developed until 2003. As a result the bureaucracy won, the state has put the control over the business and almost over all previously independent social forces. Established during these two directions driven, which means that a defective democracy now stands on the brink of transition into an authoritarian regime;
- 4) *inertia or modernization*. Development under inertia also involves modernizing rhetoric, or any actions that could be called modernization "from above" (authoritarian);
- 5) *authoritarianism or democracy*: will Russia stay within its traditional autocracy, or it, having carried out a cultural shift, will move into the category of all democratic countries.

In points 4 and 5, the final selection has not yet been made.

So we have two main directions — the modernization and democracy. Let's start with the first.

We should agree on what we mean under modernization and what is our choice. Literally modernization means the update. But it occurs con-

tinuously. Therefore, I propose to consider the modernization to be the work to overcome the accumulated backlog with assimilation of the best examples and the period during which such work is performed.

### **Technological and institutional modernization**

When, in 1999 the Center for Strategic Research (CSR) started to work, headed by G.O. Gref — a think tank of the new president Vladimir Putin, it was tasked to develop a program to continue the strategic direction of Boris Yeltsin in the transformation of Russia's post-Soviet era. As conceived by the reformers, following the implementation of major market reforms and macroeconomic stabilization, meaning cessation of inflation and recession, the stage of modernization had to begin. This term the authors of “Gref program” have agreed to use instead of the word “reform”, which by then caused negative emotions in the society. It was also noted that instead of radical changes of the early 90's a consistent, systematic work should be done on the creation and the cultivation of an integrated system of institutions necessary for an efficient market economy and democratic society. Thus, initially it meant the *institutional modernization*, a more relaxed, which is realized in an evolutionary way, but which affects almost all aspects of society, including the political system.

It differed from *technological modernization*, which assumes renewal of technologies, products, equipment, methods of organization and management, and economic restructuring in the industry, regional and other cuts. It leads directly to increased productivity through intensification of the flow of innovation. This refers to innovation “for self” (introduced) and “for the market” (sold). Innovative economy, intergrading the country into a group of leaders of world development, is characterized by a high share of innovation “for the market” (10–15% of GDP).

The level of performance that reflects the highest technological advancements, now known as the *technological frontier*. It is promoted by a group of leading countries. In other countries innovation “for self” is dominated which, if successful, lead to the fact that due to the borrowing and their own innovations a country becomes closer to the technological frontier.

Experience has shown that technological modernization and institutional modernization are interrelated. Usually, if the institutional framework is well established in terms of support for market economy, property rights, competition, protection of contracts, the technological modern-

ization develops smoothly, rapidly integrates all the best, an intense flow of its own innovations is formed. There is an economic growth. If it turns out that technological development is impeded by the old institutions, the economy signals and institutions change.

It was so in Britain during the industrial revolution, in Germany and Japan after World War II, when the economies were liberalized. The same pattern was seen in China after 1978, in India — since 1991. Marxists talked about correspondence of the productive forces (technology) and industrial relations (institutions).

But if there is no match, more advanced technologies exist, but poorly implemented, then the institutions are outdated, hinder development, then the technological modernization doesn't develop. Or some constraints are formed, whereby it becomes distorted, deformed. Thus, the Soviet system was incompatible with the efficient use of resources, high quality products, innovations. It is impossible to carry out technological upgrading, endlessly postponing the necessary institutional changes.

### Three policy options

What, however, is the choice on the fourth direction? It is logical to divide it into three parts.

First, we must choose whether it will be a deliberate policy of modernization or development will spontaneously, *under inertia*.

Secondly, *modernization from above* suggests that in order to minimize risks, especially political, the ruling elite restricts the actions undertaken by those who may hold the control. It usually limits primarily institutional changes. Attention is focused on technological modernization, initiated by the state and in large part at public expense. At the same time reducing risk is paid by decreasing results. It is possible that modernization from above will be little different from the development under inertia. *Modernization from below* (democratic) is more risky. It involves the activation of the business, the involvement of the wider population in entrepreneurial activity, self-limitation of power of the ruling elite to improve initiative and energy of the development, making them a more important factor of economic growth. Democratization — a necessary component of this policy.

Third, if you choose an upgrade from the bottom, you should still choose the pace of change — faster or slower. This option is designed to optimize the balance of risks and benefits. To limit the field of analysis, we agree that there is a choice of two options — *a breakthrough* or a *gradual development*.



Thus, further analysis suggests three policy options: upgrade from the top, a breakthrough, a gradual development.

### **Success estimation — the criterion for modernization**

To make any conclusions about the success of modernization, we agree that the level and pace of modernization will be judged by the growth of productivity over time and in comparison with other countries. In other words, if this country is experiencing economic growth and development of new technologies, but the rate of productivity growth over the same period is lower than in other countries, modernization does not occur. The success of the upgrade can be considered only in reducing the lag.

## **2. Starting area**

We can say that over the past 20 years the democratization in Russia has led to the disintegration of the empire and contributed to a very painful market reforms. The market economy — an undoubted positive result of the last period, but its efficiency is low, primarily due to incomplete institutional reforms. Transformational crisis (1990–1999) made it difficult to implement. The victory of bureaucracy over the oligarchy (the choice of the third direction) stopped or significantly slowed them. Political risks to the ruling elite often turned out to be more significant than the changes in institutions — in this case, the positive results did not occur soon and seemed doubtful. This prompted the curtailment of democratic institutions and increased pressure on business.

### **Results of 20 years**

To evaluate the outcome of zero years in Russia, we use the results of calculations of V.A. Bessonov based on The Conference Board Database comparing two versions of estimates of labor productivity in Russia and the USA — the indices GK (Geary-Khamis) and EKS (Eltete, Kevesha and Schultz). The latter index is usually more favorable to Russia, but when comparing the rate of change of the index, their values do not matter. Table 1 presents data on labor productivity, calculated from these indices.

**Table 1. The level of productivity in Russia and the United States in 1989, 1998 and 2008**

Year	Index GK			Index EKS		
	USA	Russia	Russia to the US (%)	USA	Russia	Russia to the US (%)
	Thousands of US \$ 1990 per employee			Thousands of US \$ 1990 per employee		
1989	47,632	15,787	33.14	71,723	32,345	45.10
1998	55,363	10,359	18.71	83,348	21,225	25.47
2008	65,524	18,750	28.62	99,686	36,995	37.11

Source: The Conference Board Total Economy Database, January 2010.

**Table 2. Dynamics of labor productivity in Russia (% of the level in the US) in 2008 compared with 1998 and 1989**

Index	2008 / 1998	2008 / 1989
GK	1.53	0.86
EKS	1.46	0.82

In Table 2 magnitude of change in labor productivity in Russia in comparison with the US is calculated according to the Table 1 on both indices, indicating a significant growth in 2008 compared with 1998 and a significant decrease compared with 1989.

1998 — the bottom of the transformational crisis, 1989 — nominally the last pre-crisis year. The increase compared with 1998 can not be considered a great achievement — it is the compensation of lost productivity during the crisis. But the comparison with 1989 does not allow us to assert that in general for 20 years the lag has increased, because the thought arises that for the total compensation there wasn't just enough time after the deep crisis of 1989–1998.

But in 2008 a new crisis came, denoting the completion of a particular cycle in which compensation stopped. It follows that the modernization under the above criteria adopted in the years 1998–2008 did not occur or was very slow.

### **Business activity**

More precisely, modernization in the literal sense of the word was developing through all 20 years. The economic structure has become a mar-

ket. In the first 10 years it was dominated by a passive, destructive phase of restructuring, in the next 10 years there were resources for investment and the process of renewal of fixed capital began, with varying intensity in different sectors. But along with it the degradation continued and, in many cases with non-covering pace of modernization. Production sometimes was maintained by the state (import duties, subsidies), but it often did not reach full competitiveness. The recent crisis has aggravated the problem in some industries, particularly hidden by the demand that was fostered by petrodollars and cheap credit. Thus, we can talk about delays in the modernization of zero years, making it virtually indistinguishable from the development under inertia.

Oppositely directed processes of modernization and the degradation change its intensity, and with them the resultant economic dynamics is changing. How these processes correspond, we can't fully observe, the resultant is mainly visible. Consequently, the explanation may be different. One of them, a popular and supported by the authorities is that the transformational crisis was too deep, mainly due to wrong policies of Gaidar's shock therapy, the collapse of the Soviet economy. Therefore, the recovery growth demanded a lot of time, it was not enough.

My explanation is different. The depth of the transformation crisis was really great, but not so much as a result of shock therapy as primarily due to large imbalances in the Soviet economy, over-ripeness of its problems. Military products demand declined sharply, and the civil showed low competitiveness in an open economy, it was easy displaced by imports. The problem of improving the competitiveness of Russian business could be solved, but it needed time and support of the state, aimed at the efficient transformation of market institutions. However, the bureaucracy set its sights on the suppression of the business as an independent social force. As a result, the natural business activities reduced, the business in order to reduce their political risk reduced the scale and investment horizon.

Let me explain the term "*natural* business activities", it will be useful for us later. This refers to the level of business activity, which is achieved under normal market conditions — the presence of strong demand for the products and the positive real (net from inflation) interest rates on deposits and loans. The inflation should not exceed 2–3%. Business activity may be lower than natural, if inflation is high and interest rates on loans are not available for most businesses. It may be above the natural, if lending rates are low, so money is too cheap and available.

In Russia, in 2003 the pressure on the business from the state increased, the political risks increased, so the natural business activities decreased. At the same time oil prices were rapidly increasing, saturating the economy with liquidity, and financial resources in the world markets were cheap because of the US Federal Reserve policy, oriented on excessive, beyond the real possibilities stimulation of economic growth. Our interest rates on deposits with all these years were negative in real terms, while the population at a low level of savings agreed on them, as the nominal income grew. However, the accumulation was kept at 18–20% — not enough to modernization. As a result, we, as in many countries, supported an *artificial* economic activity that caused overheat of the economy. It should have ended with the crisis, and it came in 2008. Russia, mainly due to the established financial reserves, very well passed the acute phase of the crisis. But the factors that support high growth rates before it, were exhausted. The level of business activity artificially maintained down to the natural limit under these conditions. In 2003–2008, GDP growth kept at 7.2–7.3% per year. This growth continued due to the increase in the number of employees by 2.2% annually, by 5–5.1% — increase in productivity. In the future, the number of employees will decrease by about 1% per year. Let's assume the rate of productivity growth will continue. Then, the maximum attainable rate will be average 4%.

But to sustain such growth in productivity, we need the money — the growth of revenues from oil exports and cheap loans that fueled the economic activity in the “fat years”, or something else, which is not yet in the economy. In the absence of new motor GDP growth is likely to fall to 1–3% per year.

To confirm my words, let me refer to one of the most influential government economists, A.R. Belousov. He drew attention to the fact that from the 6–7% growth in the zero years we lose about 5%, including 2% due to lower exports and 3% due to reduction in the rate of consumption growth: instead of 13–14% annual growth we should now expect no more than 5–6%. In addition, Belousov underlines the expected fall in investment and the pressure of competing imports. As a result of its GDP growth forecast — 2–3% per year, which almost coincides with our estimates. This is exactly the same level as the natural business activities in the current environment [Belousov, 2011, p. 89].

Another thing — vision for improvement. My opinion: it is possible to maintain a high rate only by increasing the level of business activity due to institutional changes, convincing to the business. This will take some time. In addition, the necessary institutional changes that give rise

to appreciable political risks and, therefore, are not acceptable to the ruling elite. It is about providing a real rule of law, a significant reduction of corruption on the basis of democratic public control, self-restraint on the power. In short, about democratization.

### **Inequality**

Another important feature of the Russian economy during this period — the alignment of social and political forces. The power really belongs to the bureaucracy. It established a regime close to the authoritarian. Business, representing a market economy, depends on it politically and through the corruption pressure. Together, these forces are assigned a greater portion of the proceeds. The remaining sections of the population are satisfied with a smaller part, and the gap between them on the material well-being increases in recent years.

Coefficient of funds (decile), according to official figures, was up from 4.9 in 1990 to 13.5 in 2000 and to 16.7 in 2009 (see [Rosstat, 2010, p. 190]). The distribution of incomes is shown in Table 3.

**Table 3. The distribution of money income between 20%-groups in 1990, 2000, 2009 (% of total)**

Group	1990	2000	2009
Group I (Lowest income)	9.8	5.9	5.1
Group II	14.9	10.4	9.8
Group III	18.8	15.1	14.8
Group IV	23.8	21.9	22.5
Group V	<b>32.7</b>	<b>46.7</b>	<b>47.8</b>
Share in income of the 3 least wealthy groups	<b>43.5</b>	<b>31.4</b>	<b>29.7</b>

According to calculations by the Independent Institute of Social Policy (IISP), “higher” group received in 2009 twice more real incomes than in 1991. Group IV also benefited from the reforms, but only 25%. Group III has kept the level of 1991, Group II — 79% of this level, and Group I — 55% (see [The level and way of life in Russia, 2011, p. 69]). Thus, 60% of the population either did not benefited from the reforms, or lost. The top 20% increased their share to nearly half. The

level of inequality has risen sharply. The two main layers of the population were formed: the poor who received less than a third of income for 60% of the population, and the rich — about half to 20%<sup>1</sup>.

Of course, in a market economy, the differentiation of the population by income is more than in planned. This creates stronger incentives to work and business activity. In the US, there is a fairly high level of inequality, the Gini coefficient is 0.35 — higher than in other European countries and the OECD. In addition to Mexico, where the degree of inequality, as in Brazil, it is one of the highest in the world. But those countries are characterized by ethnic and cultural heterogeneity of the population (white and colored). We with culturally homogeneous population at the level of inequality is only slightly lower than Mexico. We can conclude that we have the inequality over the top, it creates an atmosphere of distrust that prevents modernization, cooperative behavior, and hence social cohesion to solve common problems.

This situation partly explains the populist attacks from the Russian government. But we do not need the attack, but a strategy to overcome social disparities, embodied in the policy of income and reform — housing, pensions, education and health are far from over.

This is the starting area.

### **3. Word of the method: game models of E. Maskin**

Political and economic forecasting — is very ungrateful. If you still do it while trying to be honest, we must first understand that during the work you have to go to a number of simplifications that the probability of accurate prediction is practically reduced to zero. To reduce the number and magnitude of errors, people evaluate the initial conditions, determine the policy options, analyze them and choose, in their opinion, the best. After making mistakes some adjustments are introduced. Approxi-

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<sup>1</sup> In the calculations of the research team of the magazine “Expert” the situation is more prosperous: up to 85% of the population of Russia in 2008 had real incomes higher than in post-Soviet period. Yet even in these calculations, the relative poverty, the proportion of families with incomes well below the dominant in the country, is now much higher than in 1990. The “Expert” applied the criterion adopted in the EU: the proportion of population with income below 60% of median income, i.e. income of families, which more or less equal number of people have. We have a relatively poor in 1990 11% of the population, and in 2008 — 26% (see [Zhuravlev et al., 2011, p. 24–25]).

mately so did we. Baseline is a starting place. Purpose — modernization of Russia. Policy options are selected: 1) modernization from above (authoritarian), 2) a breakthrough, and 3) gradual development. Next, we analyze the options and try to construct a scenario of the country with various combinations of policy options with the external environment.

The key point is the reaction to this or that policy of the various strata of society, interest groups. The picture of social interactions is extremely complex. For the analysis it has to be replaced by the highly simplified models, in the hope that one of them “catch” the nature of interactions, the most important to implement the chosen policy options.

Such a model is conveniently represented in the form of the game, and not to have to use formal methods of game theory. The aim is to describe the expected developments in the form of the resultant of the interaction of a number of teams as agents of various interest groups. Differing rules imitate the different policy options for the foreseeable time.

As an example of such a game I will bring the model used by E. Maskin in the report at a symposium in memory of Samuel Huntington, in Moscow in 2010 at the Higher School of Economics [Maskin, 2010], to describe the process of creating a culture as a set of social norms. The basis of a game, which is called the “prisoner’s dilemma.” Two players can choose between “cooperation” ( $C$ ), which requires the application of effort, and “desertion” ( $D$ ), idleness. If they both decide to cooperate, then each (suggested by Maskin) wins 6, and taking into account the cost of 4 — a net gain 2. But if one decides to cooperate, then each will win 3, and  $C$  to receive the net result of  $(3 - 4 = -1)$ , and  $D - (3 - 0 = 3)$ . In one step,  $D$  gets the win and  $C -$  to lose. Then the second step, if both choose strategy  $D$ , no one wins anything. But if they chose to strategy  $C$ , both would have won 2. So the strategy of cooperation in a repeated game is beneficial to both, and the community, which is dominated by cooperatives, in the long term benefit, learning the strategy as a social norm, and thereby increasing the culture. If someone on this background chooses  $D$ , he will give a reason for another to desert in the next step. If the loss of cooperation is held, the community is facing collapse.

On the contrary, if the community lived for strategy  $D$ , and then found a group of mutants, who turned to a strategy  $C$ , then its benefits also become an occasion for others to go to work. In the work [Fudenberg, Maskin, 1986] show that in repeated games all outcomes lie between the  $C$  and  $D$ , the percentage of  $C$  depends on social norms, but it is impossible to obtain accurate predictions. The essence of cultural development is to increase the proportion of  $C$ .

We use the logic of Maskin to analyze policy options with changes resulting from the task of evaluating the dynamics of modernization in the respective versions. The players are government, business and society. Their behavior is determined by the level of trust as a basis for cooperation. The choice of players is determined by the trust or distrust the rules arising from the policy. Our further discussion will be qualitative, as we will not use the conventional numbers, useful for purposes of illustration. After that, using the results of the analysis of policy options, we try to construct a possible scenario that, in fact, would represent a variant of the forecast.

#### 4. Game I. Modernization from above

The essence of modernization from above is that the *state* has initiated any action and forces business and society to fulfill their requirements. A specific set of initiatives aimed at technological, structural and other changes are addressed by the state to business and society for the performance. Performance is provided by the bureaucracy, including law enforcement agencies that implement the functions, inherent in the state, of legitimate violence. The rules of the game suggest that to improve the efficiency requirements of the state its representatives may exceed their authority, including using them in their personal and group interests. Loyalty to the state is bought by closeness and impunity. This possibility stems from the fact that business and society can not control certain activities and the rules of the game.

*Business* carries out economic activities, has assets and draws on hiring staff that make up society's resources. By its very nature it is aimed at maximizing their income. Initiatives of the state addressed to it limit its natural aspirations. The interests of business and government in the framework of the modernization from above differ if the initiatives of the state interfere with business objectives, and the natural competitive market mechanism for the coordination of interests is not working. Then the state must either apply coercion, or create incentives for business people it need.

The latter will seek to gain maximum benefit from the cooperation imposed on them, and the rest will be in unequal conditions of competition. As a result, a climate of mutual distrust develops between government and business, leading to non-cooperative behavior of each party. None of the parties can refuse to cooperate, but the results may not be high and the goal of modernization is not achieved or is not fully achieved.



## Triangle of distrust

*Society* as a set of customers and employees, if it is deprived of the opportunity to control the activities of government and business to participate in the formation and operation of government, experiences distrust to the state, and to business. But this order is established by policy of modernization from above, assuming the concentration of initiatives in the state. Society under these conditions suggests that the changes will take place behind it and at his expense, to the benefit of government and business. If society has no capacity to protect their legitimate interests, it resorted to such methods as lowering the quality of work, sabotage and theft.

Table 4 shows the data from the European Social Research in 2010 on the level of trust in a sample of 20 European countries.

**Table 4. Levels of trust in 20 European countries by all types of respondents and by small business (average of 10 points)**

	Interpersonal confidence		Public institutions							
	all	small business	institutions	parliament		parties	judicial and legal system		police	
				all	small business		all	small business	all	small business
Average										
by country	5.0	5.1	4.3	4.2	5.0	4.3	5.0	5.0	5.8	5.9
maximum	6.8	6.9	6.4	6.3	7.4	5.3	7.4	7.2	8.0	8.0
minimum	3.5	3.1	2.3	2.4	2.5	2.0	2.5	2.4	3.5	3.1
Russia	4.2	3.9	3.3	3.6	3.2	3.1	3.8	3.2	3.5	3.1
out of 20	17	18	17	15	18	13	17	18	20	20

Source: ESS – 2010.

As the above data shows that Russia by the level of trust takes place at the end of the list. The maximum estimates — in the Scandinavian countries. Minimum — one time in Portugal (evaluation of interpersonal trust by small business — self employed), four times — in Bulgaria, two times — in Russia (the police — all and small businesses). Assessments in Russia of the judicial and legal system — the 17th place by all (3.8 points) and 18th — small businesses (3.2 points). Judicial and legal system and

police — everywhere embodiment of the state. In Denmark (highest estimation) — 7.4 points, in Finland — 6.9. Police in Finland (the highest estimation) — 8 points by all respondents and small business. In Russia, the evaluation of the police the lowest one — by all, and by small business. Judicial and legal system is not far away. We can conclude that both society and business does not feel trust to these institutions. Opinions of the representatives of the state in this study are not specified. But assumptions comes themselves.

Thus, the policy of modernization from above, in principle, leads to the formation of a triangle of distrust that connects all the participants in the game dominated by non-cooperative behavior. This reduces the level of business activity and the likelihood of success of modernization from above. Let's try a more difficult game. We divide the game into rounds, separated from each other by qualitative changes.

### **The first round**

Presumably this is the period of formation of institutions and structures to ensure compliance with the initiatives of the state and the ruling elite: the curtailment of democratic institutions, if any, increase in status and insurance of impunity for security forces, forming the “vertical of power” linking the federal center, regions and local government levels. Obedience of business is needed, and it is achieved by increasing the pressure on it, notably through the creation of threats to property rights. We should expect a strengthening of corruption. In order to manipulate public sentiments the media, partly education are put under the control.

This change is relatively easily treated, especially in a society accustomed to authoritarianism and tired of the instability in times of crisis. Stability, more simple rules of the game — all this at first yield positive results. What are they? The greater confidence that the order will be fulfilled, in the predictability of the players, including non-cooperative.

But in the modernization the results are not positive, because in a market economy (its basic principles is not in question) the driving force is business, and its rights are infringed. The bureaucracy, on the contrary, increased, and with it the part of the business, which benefits from a connection with the bureaucracy and shared with it, but it also loses activity because of the inequality of competitive conditions. To compensate for the lack of business activity, they try to increase the state's role in the economy. Large projects are being held with government investment and involvement of the private business. But there are no noticeable results. Modernization is connected with the risks, and this structure avoids all risk.

## **Terms of successful modernization from above**

Modernization from above (authoritarian) sometimes brings success, but experience shows that only under certain circumstances, namely:

- 1) if it is done in a backward country, located in the initial phase of the output of the agricultural stage of development, which determines the abundance of cheap labor, at best, accustomed to the systematic work;
- 2) if it is possible to borrow advanced technology, including through purchase or through attracting investment from more developed countries;
- 3) in the presence of open markets, which can export a significant share of production, selling it at a relatively low cost.

Russia is clearly not one of these countries, at least on the first and third paragraphs.

## **The second round**

The second round begins when the effects of the previously imposed institutions designed to enhance the role of central government, top, appear. It becomes noticeable decline in business activity (lack of investment, capital flight, a short planning horizon). Corruption markedly increases. Competition is weak, though at uncompetitive terms. Folding of democratic institutions facilitates the hand management, but eliminates public oversight. Growth is possible only with the influx of external rents or investments. If not, the internal motivation is not sufficient. It is clear that modernization, leading to a reduction in the lag, in these conditions is impossible. At the end of the second round, policies changes or stagnation occurs.

I think that in Russia at least since 2003, we have a policy of modernization from above. Now we are somewhere at the beginning of the second round. It was said about the results, we can assume that all the signs of the exhaustion of this policy option is available. The structure of government, created in 2003–2005 for carrying out such a policy, has become a major obstacle to change.

## **5. Game II. A breakthrough**

I will remind that a breakthrough is one of the options modernization from the bottom, which purpose is through institutional reforms and development of culture to create the conditions for the activation of

initiative and energy of people, their creative abilities. This is the main reserve of Russia to meet the challenges of the XXI century, including the development of modern innovative economy.

Modernization from the bottom reminds a model of cultural development by E. Maskin, which essence is to, starting to move from a situation of the triangle of distrust, replace it with a triangle of trust and cooperative behavior, take advantage of the potential hidden in the activation of the human factor.

I remind in this regard about two models of M. Olson:

1. State is in the service of society, when political and economic institutions set up to work in favor of citizens of the state, causing the part of the last trust and support.
2. Society is in the service of the state when the first serves as a “draft power class”, supplying resources to the state and “serviceman class”, with clear mutual distrust [Olson, 1998, p. 400–401].

Modernization from the bottom is the transition from the second model to the first, from the laws that are most profitable to violate, to the laws, profitable for most people and therefore is not an executable from the stick. The question is how to make this transition.

### **Minimum package of liberal democracy**

The most important part of institutional changes designed to increase confidence and strengthen the human factor is democratization. This thesis is controversial. So, Medvedev writes: “Democracy became the mass, when mass became the production of the most necessary goods and services. When the level of technological development of Western civilization made it possible to universal access to basic goods, to education, health care, information exchange” [Medvedev, 2009, p. 12]. I can accept. But looking at current problems in Russia, I see that the decision of the majority of them are limited by the need of more liberty, protection against tyranny and corruption, bureaucracy, public control over the bureaucracy and business, people’s trust in public institutions. We have none of this today. We should rather talk about the parallel motion, in which the next step is determined by the degree of urgency of the task. Today, the most urgent is democratization.

The essence of a decisive breakthrough is first of all the transformation of the political system, which ultimately must acquire a minimum set of attributes of *liberal democracy*. Whatever may be said about the latter, it concentrates the achievements of political culture, which creates favorable conditions for creativity and innovation development.

In addition, if we turn to other areas of economic and social life in Russia, we see that everyone do not need jerks, but calm, systematic, skilled work on the cultivation of the necessary institutions. But often, there are no conditions for such work primarily because of shortcomings of the political system, its excessive centralization and corruption, inability for many people to take part in this work, to show their initiative and energy in business, civic and political activities. Qualifications in these circumstances as a whole doesn't grow, but rather decreases.

I remind that in 1980 the main content of the restructuring was democratization. But the growing crisis in the economy was felt stronger, and eventually democratization was forced to cede to the economy. The democratic wave helped to implement market reforms, but the tasks of political transformation were pushed into the background. And even then there were shifts in the opposite direction. It is amazing how it is difficult to won democratic institutions, and how easily to lost!

We're talking about a minimum set of attributes of liberal democracy, because in order to ensure its efficiency there should be approximately at the same time the introduction of minimum complementary democratic institutions, supporting each other. Here we are getting the idea of a decisive breakthrough.

For Russia, in the present circumstances, this package can be defined as following:

- 1) elimination of *personalistic regime*, eliminating peculiar Russian political tradition of *autocracy*, which is incompatible with democracy, a *real division of powers*;
- 2) *political competition*, which assumes a multi-party system that represents the fundamental interests and beliefs of citizens, freedom of assembly and association, the rejection of formal membership in the party or the requirement of a minimum number of members of the party when registering to vote. The change in the electoral law to ensure free and fair elections;
- 3) *the rule of law* — the independence of the judiciary, equality under the law, prosecute of persons attempting to influence the judges, the change of the powers of court chairmen with the exception of opportunities for them to influence the position of judges based on their decision-making, empowerment of the jury;
- 4) *the democratic control over the executive power, the subordination of the bureaucracy to the public interest*. Adoption of the law on parliamentary investigations to identify their subjects and objects, regardless of the government. Freedom of the media;

- 5) *decentralization*. Enhancing of the role of local government. Giving more rights to municipalities, which show the maturity, the active participation of civil society, a reasonable command of finance — a sort of Russian version of the “Magdeburg Law” that encourages other municipalities to gain the same status. Permission to establish its own local taxes and fees. The elimination of positions of city managers, as an institution, which is not only contributing in the Russian conditions to the development of local self-government, but on the contrary, interfering it with the final design of the “vertical of power”.

I stress that we are talking about the rights and freedoms guaranteed by the Constitution and blocked by the current ruling elite. The list can be expanded, but the one that we have given, may be considered necessary in the first place, here and now.

### **The first round**

Hasty action is taken in the hope for a quick result. Can we count on it in this case? Imagine that with a program of the above five points you go to the polls today. Let’s assume, there is a liberal party after you, the elections are conducted fairly and honestly you have the means to organize a decent campaign. All this looks like a fantasy. But I even under these conditions, have serious doubts about the success of the tactics of the “here and now”.

The decisive breakthrough suggests that the power at the center is in the hands of a team that believes in the need for political reform and is willing to undertake them. The power of the advocates of reform can proceed either by election or by the split of the ruling elite by coming to power of one group that is democratically minded.

The win on the election in the foreseeable future is clearly excluded. In order to win elections and gain power legitimately, *supporters of democracy must first push through parliament changes to the electoral law, enable them to at least maintain an active campaign* and warn of abuse of administrative resources. I will emphasize the importance for the modernization from the bottom of the word *legitimate*. Democracy needs only a victory, asserting the triumph of law. Therefore, the degree of determination of the breakthrough will inevitably lowered by this condition.

Option of a split in the ruling elite may seem more realistic, but we need to imagine what processes are to occur in it for this, moreover, that the split for the time being is not advantageous to anyone. Note that, according to some researchers (see [Nort et al., 2011, p. 266–270]), the threshold

conditions of a peaceful transition to democracy (open access order) are: 1) recognition of the rule of law within the elite, and 2) perpetual existence of organizations — media interest, regardless of the will of the king or leader, and 3) consolidated control over the basic enforcement agencies. In any case, the opposition by splits and jerk in the elite will be very strong. The chances of radical democrats, if there are any, are very little.

But let's suppose that by some unknown way the supporters of democratic change got the power. What state of society did they face?

It should be recognized that although in the society the mood of distrust and dissatisfaction is very prevalent, they are not active.

Business is above all interested in the transformations, organically inclined to caution. The decisive breakthrough will push it by unpredictable consequences. There will be different interest groups. Those who have been associated with the previous regime, are likely to impede change. It was so in 1999: Putin owes much for the ascension to Olympus to those, close to Yeltsin, who feared for their position and status in the case if Primakov came to power. There will be, of course, groups that support democracy, as well as those who will not put all eggs in one basket. Most likely, business activity will decrease, capital flows will increase.

Society, including the opposition and intellectual part of political elite, is now, I think, in a state of so-called *quasi-stationary equilibrium Kohler* — a term taken by me from L. Ross and R. Nisbet (see [Ross, Nisbet, 2000]). It denotes the state, when the society is in a certain voltage, moreover, the “driving force” of changes face “the forces of containment” and the balance between them creates a situation where no significant changes are possible. When the voltage increases, we expect the transition to an *unstable equilibrium*. It is characterized not by the fact that changes occur in logically explainable conditions, but by increased likelihood of *mobilization*, that is, mass action, possibly for completely random occasions.

In the first round of decisive breakthrough after the key change just as I think the probability of transition to a state of unstable equilibrium and mobilization with unpredictable consequences increases.

### **Conformity**

I would like to pay special attention to the readiness of Russian society to democratic change and institutional modernization. Our politicians, except for those who have a relationship with the secret services, in general, seems alien to the idea of strategic planning policy, the

*road map* — a fashionable expression — between the ultimate goal, and original condition. This is probably correct, taking into account the uncertainty and complexity of guessing the future: get involved in a fight, and then we'll see. But still some kind of changeless carelessness on the possible negative consequences of actions taken confuses me, especially after observing the last 20 years.

However, many warned that it is important to consider the Russian traditions. When it came to economic reforms, I do not consider it possible to ignore the tradition: it was too obvious for most the need for a rapid change, too high would be a price for a gradual one, which is still, apparently, would be disrupted. But now we are talking about reforms, primarily political, the area where adaptation to the new institutions requires a different time, more difficult to influence than in the case of economic institutions, closely associated with material interests. We have seen attempts to accelerate the introduction of distortions faced diverse or rejection.

Let's refer to the Levada Center ([www.levada.ru](http://www.levada.ru)), which for many years in their questionnaires asking the question of the type of the political system preferred by citizens.

**Table 5. Preferred political systems (% of respondents)**

Year	Soviet political system	System, similar to the current	Western-style democracy
2000	45	13	25
2009	38	25	18

From Table 5 it can be seen that the present defective democracy on the verge of authoritarianism for the years 2000–2009 has pressed the preferences of the Soviet system to a lesser degree than liberal democracy, which is in last place. And even kept the Soviet leadership. The May poll by the Levada Center in 2011 gave the following ratio of responses to the question “To what extent is ‘Western’ version of the social order suitable for Russia?” (%):

- fully fit 6.6
- it can be adapted to Russian conditions 19.8
- not quite fit, is unlikely to settle down 30.9
- is not suitable for Russian conditions 35.0.

Almost 66% of the Russian representative sample reject liberal democracy, which the most complete, in my opinion, represents a real



democracy. Of course, such a public mood changes. But observations in Russia show that low scores are very stable for democracy, but in the last decade, even the conservative rollback occurred. When we are talking not about abstract propositions — whether democracy suits us but about democratization politics, especially carried out by a strong jerk, we will have to reckon with public feelings.

But this is not just superficial feeling. Russia — a country with deep-rooted traditional institutions which strengthened during the period of frequent tests of the XX century, which forced to turn to the archaic ways of finding means to live and forms of social life. In the Soviet period, all the formal hierarchical structures were built close to the feudal class and the imperial bureaucracy. Modern network structure, characteristic of a developed market economy, appeared and began to develop only in recent decades. Similar political structures of democracy are still suppressed. The struggle between traditional and modern institutions is, in a common sense, the substance of a long period in the life of Russian society, which began with the peasant reform of 1861, and has not yet been completed. The high degree of conformity leads to the rejection of the norms and values that have proven in other countries their ability to promote creative, innovative development, the modernization of society on this basis.

Let's return to the above five points of liberal democracy. The elimination of personalistic regime and prevention of its reappearance, the creation of real conditions for political competition are unlikely to attract the support of most voters. It's more likely that the latter vote for those who promise stability, power and majesty of the growth of pensions. They see no harm in a one-man rule or rule of irremovable groups for whom no laws are written. Or do not consider it significant. On the contrary, the prevailing view is that Russia needs a "firm hand". Equality before the law, meaning the rule of law takes first place in all the rankings pressing problems facing society, but apparently, the "firm hand" seems more important and the citizens tolerate for it with the sake of selective justice, unequal conditions of competition, restriction of their rights and freedoms.

In short, it is necessary to take into account the conformity of the Russian society. If a breakthrough is possible in the democratic transformation of political institutions, it must be well prepared. Public sentiments at this point should be in favor of real democracy.

## Another word of caution

Eric Maskin in the report writes about the possibilities of escaping from the trajectory of cultural development on any side trajectory. In his terms a breakthrough begins when the group of “mutants” captures the power and on behalf of the state offers business and society co-operative strategy (*C*). Business, as noted, will at the beginning refrain from taking action, preferring to either desertion (*D*), or alternate strategies *D* and *C*. The society, with the distrust to the government, can now show high confidence, even euphoria, but the new mood is unlikely to be stable. With the slightest disappointment a new distrust and conformity are very likely to appear.

Maskin, to test the reliability of its findings on the development of culture as a result of the benefits of cooperative behavior built an alternative strategy ALT [Maskin, 2010, p. 4]. Its essence is that the game begins with a strategy *C*, and then alternates between the *C* and *D*, while one of the players will not break a rule, after which all go to the continued *D*. This strategy itself provides benefits to all players, but below the cooperative strategy. If a “mutant” wants other players to return to the strategy *C*, then he will have to alternate between *C* and *D* in exactly the same as ALT player. It is very difficult, and error leads to a transition everybody to *D*. There is low utility in these circumstances of the successful “mutant” activity. There is a low probability of a return to a cooperative strategy. There are ways out of this situation, but what is important for us, we see the threat of too risky policy.

## The second round

The most undesirable developments in the second round of the game — *a new rollback*, another edition of authoritarian or close to this regime.

Warnings made to the first round: the difficulties of legitimacy of democratic reforms, conformist society and its potential resistance to changes, the threat of instability and mass mobilizations to the unintended consequences are, in my opinion, more than a good reason. I would like another attempt to democratize and modernize Russia to finally lead to success.

Another failure would be interpreted as proof that democracy is generally contraindicated in Russia, that it does not lead to the rise but the decline of the economy and welfare of citizens. Another long series of

authoritarian rule in response to another attempt to escape from his grasp is a new wave of disbelief in the vitality and future of the country.

It is possible that a policy of decisive breakthrough could prove to be successful. And it's easy to enter the least number of rules of liberal democracy — after all, once something like that happened in the early 1990's. And then, without the complexities, the society would adapt them, what in life has turned out far less successful. Fears for the fate of new attempts have forced me to describe the results of this game in dark colors, how I do not really think.

## **6. Game III. The gradual development**

The gradual development — modernization option from the bottom, but without jerks. It is anticipated that flow of institutional changes alone are not as significant, but together, step by step lead to a noticeable development of culture and increase its productivity.

The peculiarity of our country, like other developing countries, in that it seeks to cultivate in their own institutions, proven in other countries and in different cultural environments. Therefore, usually firstly the law is accepted. In its preparation, a new institution is created, and in theory, a public debate should be held, which facilitates the passage of the law and its subsequent use. In contrast to countries where the institution is born on its own soil, and the law only makes out, legalize its existence, we have a law that usually only marks the beginning of the case. Then the cultivation of the institute begins (see [Kuzminov et al., 2005]): a law generates a flow of precedents of its application, positive or negative for it. The ratio between them depends, in part, on the forces of support and resistance forces. Possible reactions are absorption (after a period of adaptation), rejection and distortion. Assimilation is characterized by the passage of the barrier of most (the norm is perceived and used by most stakeholders, it has been recognized). Rejection or perversion (the practice invests in the form adopted the different content, contrary to the spirit of the law) mean that the institution failed or drag force is stronger. Then we have to go back to the project and remodel it, so to start work again.

### **Four examples**

We have seen such processes in recent years. The fight between the forces of support and resistance, driving and restraining forces around

the assimilation of various institutional innovations, in many ways was the content of economic and social life in Russia. Here are — very briefly — four examples.

*The first example* — the introduction of a flat income tax. This tax was introduced in 2002 to replace a progressive tax scale with a maximum rate of 35%. Progressive tax collection was low; it clearly did not fulfill the function of strengthening social justice. I remind that in 1999 the State Duma during the premiership of E.M. Primakov heard the proposals to increase the maximum income tax rate to 45%.

Flat rate is a unified rate of 13%.

Such a tax Russia has introduced one of the first in the world, greatly simplifying its administration, which was important in a weak state and with poor discipline taxpayers. Flow from income tax at the same time increased by 20%. It does not mean that incomes of the population were entirely derived from the shadows, for which the tax has been criticized by detractors, though, this problem was not posed by the authors. They just wanted bigger transparency and reducing of administrative costs (see [Sinelnikov-Murylev, Trunin, 2010]). Additional effect, however, strengthened the reputation of the tax, it was imposed in several countries of Eastern Europe and other proponents of tax innovations, such as to reduce the unified social tax (USE) in 2004 justified it by the expectation of increased tax revenue while reducing its rates, by citing on the experience of a flat scale.

However, since that the adherents of social justice regularly offer to return to a progressive tax scale. But I think we will never go back to it, even if the fiscal discipline increases. The benefits of a flat scale, its practicability is too evident. And the goals of social justice can be achieved by other means, such as increased taxation of real estate, vehicles, legacies, etc.

This is an example of a successful change of the institute, with the positive precedents and best practices implementation.

*The second example* is education reform, the introduction of the unified state examination (USE). Experiments were performed with the USE for nine years. To simplify matters and reduce resistance to reform, the principle “money follow the student” was abandoned, replacing it with a per capita funding. It seems to be a technical matter, but the student is excluded from the process, in fact, the previous estimate has remained. Everything is done within the bureaucracy, and the possibility of competition between universities is largely lost.

Still desperate resists. Despite the obvious advantages of a united and independent assessment of the achievements of students that though not

always immediately appear because of lack of skills and ethics of teachers, students habits, inability to quickly produce high-quality tests and other assessment tools to debug the knowledge, parents and teachers opposed to the new system, including the best of them. Most now believe that the old system better take into account the individual abilities, it was psychic or something ...

A wave of obstruction of USE increases, especially in Moscow. But really — it's my opinion — it is just the usual interest: to help our own. It doesn't matter that young people are accustomed to cynicism and low-brow, the fact that we must have connections and not be well trained — still it's widely believed that it was, is and will be this way forever. I strongly disagree, to think so means to continue living in yesterday. We see that in other countries, more successful than we are, only a very small part of society share similar setting, which contributes to the manifestation of individual ability. While saving "our opinion", will lose in competitiveness. Meanwhile, the new system is already beginning to show its advantages: points scored in the exam are recognized as a criterion of success and attractiveness of university entrants.

*The third example* is pension reform. It does not get to balance the interests: the business wants to pay less, seniors want to get more and to pay nothing, putting all the cares on business and government. The state, more precisely, the ruling elite avoids the unpopular decisions that increase the political risks.

In reality, the reform started in 2001. They abandoned the previously introduced principle of insurance, went to the USE at a rate of 35.7% of payroll. In 2004, USE reduced to 26%, and with the regressive scale for a number of sectors — up to 24% effective rate. As a result, it formed a growing deficit of the Pension Fund, moreover, that the reform involved the formation of the accumulative part of pensions. It eventually had to be the basis of the pension system, taking into account the aging population. The distribution of the implementing the principle of solidarity between generations, would eventually cease to exist, although it still presents even in the most advanced countries in the majority of the pension funds. The accumulation of the pension fund is designed to ensure the emergence of "long" money in the financial sector. Lobbyists from the state proposed in the difficult situation to opt out of storage, go to the formation of a voluntary system of pensions, which would cause severe shocks over time among citizens who received low incomes and were not inclined to save. When then in 2007 they decided to once again raise the USE and go back to the insurance principle, business opposed. The

president gave up under pressure and ordered to reduce premium rates, which again exacerbated the problem of pension deficits.

The solution is known, but it's unpopular: it is necessary to introduce compulsory pension contributions for all employees, even if small. This arrangement exists in all countries, exceptions are just us and Australia. We should also rise the retirement age, though at first for those who is 20 years until his retirement. We should improve the conditions of voluntary pension insurance, consider whether to pay the state pension to wealth people, who does not need.

Is that all? No, because a substantial portion of the population has extremely low incomes that do not allow them to make even small contributions to the pension and health insurance, as well as taking home loans to purchase homes. This is the case, when gradually, small steps will not solve the case. The question is not only about a low level of economic development, low productivity, but also about the need for major institutional changes, including increasing public sector wages and the opening of the budgetary network to influence markets.

I will not describe here that I'm willing to offer and have already proposed (see [Yasin, 2002]), it would take too much space. And the problem I rise now is different. I want to show how the fear of a greater resistance to the new institution and of the negative precedent, we do not accept institutional solution that solves the issue. The unresolved issue undermines the confidence of investors and future pensioners. State gives just with partial solutions, allowing to postpone a decision in principle, but also complicates matters.

*The fourth example* is the story of Eugene Chichvarkin, one of the most successful Russian entrepreneurs, the creator of "Euroset". Several years ago, law enforcement officials confiscated his imported phones, accusing him of smuggling. The prosecution has not been confirmed, but the product was sold. Chichvarkin himself addressed to the court. Perpetrators were not accused, but the prestige of the "cops" was damaged. It was a bad precedent I. When the freight forwarder of Chichvarkin company stole goods to his own profit, the company's employees decided not to call to the police and to deal with a thief in their own way. This is negative precedent II. Law enforcers have taken the case to the note, and when there was a suitable moment to take revenge, started a criminal case on Chichvarkin, forced him to sell the business and go abroad. This was the lesson for all Russian businessmen, not the first and probably not the last. It is negative precedent III, clearly indicating the insecurity of property rights, justice inability to perform its functions, including the effect of increased in recent years the impunity of power structures.

All these examples are well known. The whole our economic and social life is formed of these elements. In the struggle over the content of this form of life processes in which interests of different groups are facing, the direction of the resultant force, which determines the development of society, is indicated. If negative precedents dominate, reflecting the predominance of traditionalist forces, then we have to deal with the trajectory of stagnation, and possibly degradation and decline. If, however, the positive precedents begin to dominate, aimed at the development of culture, increasing the creative potential of society, it is appropriate to talk about modernization. If there is modernization, even a slow one, without jerking, accompanied by noticeable ups and downs, but with a resultant positive, then we are dealing with a *gradual development*.

### **The first round**

But the gradual development in our case is a variant of modernization from the bottom. In other words, to enhance the business and all sectors of society in order to increase crop productivity and on this basis to accelerate the development of the economy, it suggests a gradual (as opposed to a decisive breakthrough) movement of decisions and independent action down, the change of the model “the state takes a toll on society” (the second model M. Olson) on the model of “the state serves society” (the first model M. Olson). Accordingly, the level of trust between government, business and society must increase.

The gradualism and decentralization, thus, are the specific properties of the game. A prerequisite for the game to give these properties is the initial focus of the ruling team to carry out such policies. Such policies should be publicly declared, the society should be able over and over again to make sure that the declaration is confirmed by real actions and results. It follows that in the ruling team at least a partial change should occur, it must be diluted at least by new people infected by the ideas of transition to democratic modernization.

Gradualism will be guaranteed by the presence of representatives of the same team. And therefore, by the collisions of different views, the struggle of conflicting interests. Therefore, it is important in the first round to implement measures that do not cause the most violent conflicts, but at the same time allow the formation of institutions to promote a competitive market economy and democracy, to intensify the increasingly wide circle of business and society. This means one thing — a step by step self-limitation primarily of federal executive authorities, the public rejection of its certain prerogatives, including implicit.

For the first round, in particular, the accelerated promotion of a *package of social reforms suits* — housing, pension, health and education. In this case it is preferred that even during the authoritarian regime, but with the prospect of further democratization, more difficult, unpopular steps of these reforms were made, for example:

- *for the housing reform* — the primary housing market de-monopolization, the beginning of the transition from the sale of apartments in new houses to their lease, the construction of tenement houses. Simplifying the registration of land ownership. The condition — reduction of inflation to a level that ensures the availability of mortgage;
- *for pension reform* — the introduction of compulsory pension contributions since the beginning of working life, raising of the retirement age. The condition is improvement of wages of state employees and changes in the network of budgetary establishments, taking into account the state of the labor market;
- *for health care reform* — the introduction of mandatory private health insurance to pay for all insurance policies, which contribute by the state of minimum free medical services;
- *for education reform* — the completion of the introduction of the USE and the beginning of the introduction of government individual financial obligations (GIFO), providing competition between universities and the closure or conversion of those that do not provide accepted standards of quality and do not attract sufficient resources.

All such measures should be discussed and was pilot-tested with the participation of the public.

The gradual shift from authoritarian to democratic modernization from the bottom is also appropriate for the beginning of a new stage of *reform of local government*, the bond with the activation of civil society. The fact is that with the turn to state capitalism in 2003, there were also changes in the institutions of federalism and local self-government. The governors are now appointed, wanted to bring the “vertical of power” to the mayors, the centralization of finance has increased, while the influence of voters on the lower level of government has been reduced to virtually zero. It is clear that democratization in the gradual development must begin here, where the revival of the democratic institutions will create a grassroots basis, without affecting at first “the tops”. But we must keep in mind: it’s a return to what it was and we won’t like it all. The fundamental question is to give cities and municipalities, especially the more experienced and successful ones, the right to establish and collect local



taxes and fees, marking the beginning of the transition to a competitive form of fiscal federalism, to reduce the level of centralization of local authorities dependent on voters to a greater extent than the governors and federal transfers. Once the cities of Europe were given “Magdeburg Law”. We might need something like that, too, including mitigation and increase of survival rate of new institutions.

Another direction of the first round — *the rule of law*: judicial and law enforcement system may be relatively independent of changes of other institutions, in advance, so that people are better prepared to play by new rules. The key point — series of unprecedented penalties for security forces implicated in the arbitrary, self-serving use of the right to legitimate violence. You will also need a lot of work to improve laws to exclude the possibility of different interpretations to finish with the *interpretative law*. But it should be clear that the law takes effect when its supremacy is recognized politically when this recognition breaks the equilibrium of political forces.

Because in the ruling team and in the community there will be opposing groups: liberals and force men, doves and hawks, reformers and conservatives, the gradual modernization of the bottom will be trade-offs between them. In fact, the gradualism itself, its scope will be determined by the outcome of ongoing trade, concessions, maneuvers, explicit and hidden public view. Viscous and sometimes painful struggle, not always winning, traces of which are deposited in the form of inconsistencies in the new institutions, traps, bearing new challenges. Let me remind that critics of the peasant reform of 1861 were reproached it for its half-conservatism, which led to the revolution in 1905. But it was the fruit of compromise. That is, apparently, the price of gradualism, an undoubted negative option, which always poses a threat to stop and retrograde motion.

Any positive steps towards modernization from below, though gradual, and therefore, democratization will probably be supported by most of the intellectual elite, civil society organizations. Conservatives oppose, condemn deviation from tradition and narrowly defined national interests. The Left and the Communists will support the modernization of the bottom at first, because they are interested in democratic institutions to achieve more in their understanding of social justice. But in many ways, the reforms they would be in opposition.

In public, the media is inevitable wave of criticism of the federal government for being slow, that many will be interpreted as a consequence of uncertainty or struggle in the manual because each step: one trying to act, others — to dilute the essence of the goals of action are not achieved. The criticism is often unfair. The hard way! It is necessary to demonstrate posi-

tive changes in the growing pace, urging people to the hardness of the authorities' intention to limit yourself, to change their status — from the domination of the ministry. If at least some significant changes there will be no development will be under option or upgrade of inertia at the top. The triangle of distrust will persist when the task is to build a change in him.

Business will meet a change in policy with the usual skepticism and for a long time, until he has conclusive evidence to respond positively with the risk for capital, will not. Therefore, the economic dynamics may be uncertain.

Meanwhile, the contribution of the private sector is important. For technological modernization we need large investments in sectors of the economy that have a chance to become competitive in the world, or at least on the domestic market. It is necessary to ensure the re-enterprises with modern equipment, training employees, improving productivity as a result, at least by 50% of US level. It requires strong motivation, confidence, willingness to take risks, to plan for many years. Legal guarantees and financial support of the state without this won't be sufficient.

Society will probably be positive, but will passively support the change. You can expect such conservative reactions, as in the case of USE. But as a limitation of the bureaucracy and the business in its pursuit of profit is possible only with consistent democratization, including first of all freedom of speech, rule of law and political competition.

### **The second round**

If a project of gradual reform would be elected, in the second round, there should have been, in my view, the events on the content related to the events of the first round of the decisive breakthrough.

Indeed, sooner or later, but the minimum package of liberal democracy in the way of modernization from the bottom is still to be realized, by the way, the entire package to form a complex of mutual support for democratic institutions, as was the case with market institutions in 1992–1994. This is a critical point in the way of institutional modernization from below. This is its possible division into stages: first, changes in the party and electoral legislation to ensure the legitimacy of subsequent decisions, then the guaranties against personal power, etc. After that the “lower classes” are connected to the activities for which they are still just observers. The fact that these measures of democratization preceded by gradual steps, in general, is able to convince the business and society that the authorities act purposefully: you have to prepare people for their conduct, reduce the likelihood of foreseeable negative consequences.

In principle, we cannot exclude the stop of the change, like the one that occurred in 2003–2004, due to conflicts between rival groups of

elites. But it seems in this case less likely. Economic dynamics are unlikely to be the same as in 2004–2008, but we should rather expect low growth, stagnation or even a growing lag. In these circumstances, the authorities will be difficult to maintain a quasi-stationary equilibrium, the voltage may rise, threatening the stability of the regime. But it must be understood: either upgrade stops, or it can continue only with the implementation and operation of major democratic reforms. Even if they occur in a more moderate pace, we still should expect an increase pressure in favor of the assumption of various political forces to participate in solving social problems, in the public political activity, and therefore — to political competition, the struggle for power.

If in the first round of the gradual reform local government reform begins, focused on decentralization, it is now focusing on empowering cities and municipalities with the right to self-administration of taxes and duties, the work is started to create conditions for free local elections, civil society and grassroots democracy. Local elections are more important than the federal. It prepares the next democratic reforms at higher levels. Reforming in education, health care, pension system, the housing market and public services also provides significant opportunities for enhancing skills of the population and formatting of grassroots democracy.

If the authorities, who have taken the project of gradual development, will try to do it seriously, will develop plans for its implementation, and approaches to resolving conflicts between the forces of reform support and resilience, for adaptation of new institutions, for overcoming their barriers to distribution. Of course, all those difficulties, which have been described in relation to the first round of game II “The decisive breakthrough”, will occur. Maybe, stretching time and more and more apparent exhaustion of modernization from above will soften some of them. But surprises are possible. Problems related to real democracy and the adaptation of institutions peculiar to it, still cannot be avoided. Success will be judged by the changes that will occur with the triangle of distrust, how the level of trust and cooperative behavior in society will increase, including public institutions.

## **7. The findings of the games in the modernization**

So, the games are played. What are they shown?

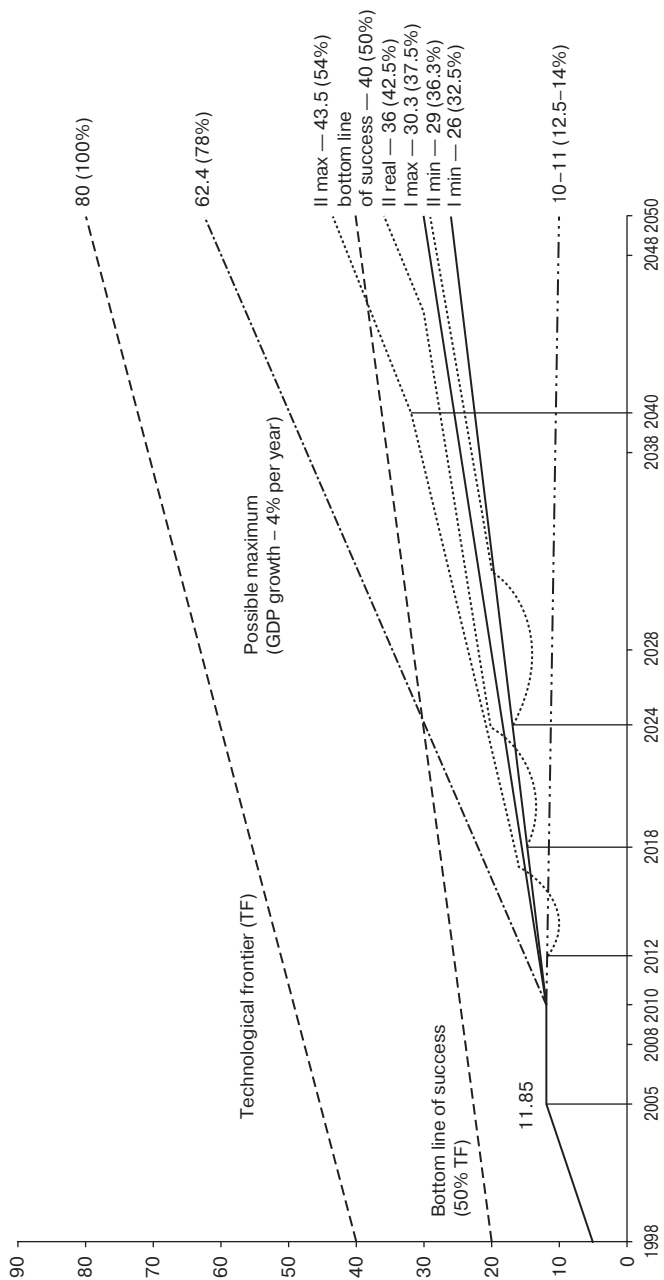
We agreed not to consider them as predictions, but only as a reflection on possible future events and processes under various assumptions. And they lead us to certain conclusions.

First, we estimated the initial position in Russia, and outlined a range in which events may occur within a wide range of policy options: from the inertia development or modernization from above to a decisive breakthrough, especially in the field of democratization.

Second, *these two extremes of the policy with a high probability lead to the destabilization and the new major shocks*. The difference, perhaps, is that under the most conservative first option, apparently, much longer period is needed before the changes happen that could lead to some positive results, if they can be obtained at all. A crisis, which in this case is to be expected, accompanied by a spontaneous protest mobilization, will be stronger. The explanation is simple: *the ruling elite, which is responsible for the policies, at the time of instability, will remain in power, and is likely to resist*. The forces, which may come to replace it, will most likely be accidental, because they will not pass the selection in at least partially democratic process.

This is the third main conclusion, which is a little bit unexpected for me. I have always believed that Russia is ready for democracy; we only need to quickly carry out democratic reforms and to comply with the rules of the reforms introduced. Now I come to the conclusion that *a gradual development towards modernization and democratization are most likely and preferable to other policy options*. Of course, the movement in this scenario will have to expect a terrible slow development: small steps, clashes, constant verbal battles, the apparent defeat in the individual battles, multiple transitions from euphoria to melancholy and back again. This is a longer process than a breakthrough in a successful outcome. But overall, taking into account the distribution of subjective probabilities for a given interval of time, this is the way most reliably and at lower cost that could lead to the goal.

As an example of the country's history I will take the period between 1905 and 1913: the defeat of the revolution, the dispersal of I and II State Duma, the success of agrarian reform, frustration, murder of P.A. Stolypin. These are the events. Yet on the background of economic recovery with the rooting of market relations, the gradual assimilation and the spread of liberal democratic norms and values seem undeniable. And the more they take root, the weaker the influence of the revolutionary socialist, of a radical camp and the conservative forces. If Russia did not get involved then in World War I — now it is even unclear for what, because it is difficult to consider reasonable the motives to capture the straits or to protect of Orthodox Christians in the Balkans — its history would have been different.



**Figure 1.** Dynamics of GDP per capita of Russia under different scenarios of development in comparison with technological frontier

And today, calming the emotions, we must prepare for a protracted struggle, compromise, not enough consecutive decisions, institutional traps, typical modernization scenario of gradual development. However, even in this case we would have to go through a critical period with the introduction of minimum complementary institutions of liberal democracy.

In fact, this scenario in the article “Forward, Russia!” was supported by Dmitry Medvedev, perhaps for other reasons. I can assure readers that I have come to this conclusion independently. The gradual development creates, perhaps, the best conditions to meet the challenges facing the country — feasible voltage without excessive loss from external factors. But the answer to the main challenge may be successful only if we *can free up the initiative and energy of the people through democracy*, getting rid of bureaucratic discretion. In this way we overcome the cultural barrier to improve the innovation potential of Russia to the level of developed countries. This is probably our only chance.

## Scenarios for the future

### Scenario I

Now let’s see what we can do under different scenarios. For the basis we take the *inertial scenario*, modernization from above (scenario I), coming from the fact that significant institutional change will not happen. This scenario is realized now.

But compared with the period before the crisis of 2008–2009 the situation changed, there will not be uprapidly rising oil prices and cheap money in the future. If the oil price will keep all the years of more than \$100–105 per barrel and even grow, with its growth below the rate of growth of world economy because of energy efficiency, the price of oil will not, as before, accelerate growth. This is the opinion of experts. The Russian economy does not show any other special attractive properties: insecurity of property rights, corruption, bureaucratic arbitrariness, legal nihilism — everything is stored.

An increase of productivity by 5% annually implies a high economic activity, followed by investment in the necessary quantities and with growing efficiency. I’ll stress — firstly business activity, a favorable climate for business, while investment and efficiency — the result. In 2002–2007 we had gross fixed capital at the level of 18–20% of GDP with require of 25–30%. And the efficiency is usually low. Input of 1 kW of installed capacity of coal power plants costs \$2,500 vs \$1,800 in the EU and \$720 in China. One kilometer of highway is worth \$10–15 million for us vs \$2.5

million in Australia, Canada and Sweden (see [Bessonov et al., 2010, p. 32]). Without these institutional changes we fail to significantly improve the performance.

At what growth under these conditions can we expect? Realistic rates — 1–2% growth over the next 40 years. This means that by 2050 GDP per capita will increase by approximately half (1.49–2.52 times), up to \$26 thousand, or to approximately 32.5% of the technological frontier. This will be the maximum for this scenario (see Fig. 1).

A more generous assumption — not to take the middle and the upper limit of this range, average annual growth of 2%. Then in 2050 GDP per capita will be at \$30.2 thousand, or 40% of the technological frontier. We take these figures as the maximum.

One might ask: Is not it little, just 2%, because in 2010 the GDP grew by 4%? I think it is no longer increasing. First, in 2010 there was a “bounce” after the crisis of 2008–2009. During this period the economy has been invested significant financial resources from the reserves accumulated previously. Also we were affected the post-crisis growth in commodity prices. Such a favorable situation in the future is difficult to expect. Secondly, it is a period of 40 years, during which the scenario of modernization from above is preserved. Over the years, we should expect less from it. Let conduct major projects financed by public funds and borrowed funds to force big business, this model is valid now. It will not be able to give higher rates for the whole country. Experts expect either sliding to stagnation. This scenario means that the major modernization does not work, it will perform about the same as in 2004–2010.

## Scenario II

Under scenario II starting from a certain point, for example 2018, due to a combination of circumstances, movement under inertia changes to trajectory of *modernization from the bottom with a gradual development* (curve II). In principle, the transition can happen at any time.

In the process of motion along this trajectory some changes occur, including in a package of liberal democracy, but they takes quite a long time: preparation, in particular, public opinion, conducting changes themselves and subsequent adaptation. Previously the most significant reforms in the social sphere are held, referred above to the number of unpopular. This implies significant institutional investment. Large-scale privatization are also carried out, and as a result the share of public sector reduces from 50 to 15–20%. The reform of local government reduces the level of centralization.

For all these reasons, switching to a different trajectory extends over 4–5 years, and possibly accompanied by some decline compared to the inertial trajectory on an average 1% of GDP last year before the change. Then the made changes begin to give positive results: confidence of business and population in the state increases, business activity increases, foreign investment rises. Citizens become more active. As a result, the growth rate increases on an average 3% per year. By 2050, GDP per capita amounts to about \$36 thousand, or 42.5% of the technological frontier. Postponing the start of reform until 2024, with a similar scenario, we would have in 2050 about \$29 thousand GDP per capita, which is not very different from the results of the inertial scenario and modernization from above. We intentionally complicated options. The last of them will take a minimum of scenario II.

Let's suppose now that preparations for the implementation of the basic package starts immediately after the presidential election in 2012. This allows to gain time. Positive results of institutional changes affect the past. Growth in average is held at 3% per year, and in 2050 we reach the 48–49% of technology level. With favorable developments we can be assume that in the last 10 years of development under this scenario rates raises to 4% per year, which is expected, given a longer adaptation of society to the conditions of democratic modernization. Then at the end of the billing period GDP per capita would reach \$43–44 thousand, or 54% level of technological frontier in 2050.

It would be much less than the potential maximum, but it would exceed the lower limit of the success of modernization. Russia would have been on the road, open to new developments in the movement to the technological frontier, already in the community of developed countries, with a sense that the historical challenge it could give a convincing positive answer.

We use these figures as the maximum for scenario II. And the figure of \$36 thousand income per capita (42.5% of the technological frontier), achieved by changing the course in 2018, with an increase in the rate to 4% per year over the past five years, is considered a realistic option for this scenario.

### **Scenario III**

Now, to complete the picture, we need to consider another scenario. Suppose that in the near future there will be adverse events, such as lower oil prices to \$50–60, and such “low” prices will stay as it was in



last cycle, for 20 years. Capital outflows are possible, which significantly reduces the investment potential. Institutional reforms are not carried out. The ruling regime, in contrast, seeks to prevent the destabilization by straightening the power. Or vice versa — worsening the crisis leads to the power of radicals and they are trying to salvage the situation by a decisive breakthrough. And in fact, in both cases unintended consequences are possible, accompanied by a cascade of crises, when the previous wave pushes the next one.

If you look back at the developments in Russia, say, since the fall in oil prices in 1986, we must recognize that it can be interpreted that way. Indeed, the rise in the years 1999–2008 was mainly only after reducing the growth of the transformational crisis. During this period, the qualitative changes that would have led to large-scale modernization, did not happen. And then, once again, the crisis began, which outcome is not clear. Abroad, it is often the way they interpret the evolution of Russia over the past 25–30 years — as an almost continuous fall from superpower to a developing country.

I am convinced that the charge capacity, resulting from market reforms in Russia is far from being exhausted, and if it is supplemented by democratic institutions, it is possible to give the public the confidence that the new Russia, overcoming cultural barriers, can stand on a par with other developed democratic countries. But for this you need to remain the strategic line for the modernization for a long time, for the participation of the widest possible range of citizens. The previous methods by which the past rulers of the country raised the country, now will not lead to success.

Without extremes, let's assume that *pessimistic scenario III* involves the maintenance of GDP per capita at current levels or, at worst, its decrease by no more than 10% by 2050. This would mean 14–17% of all the technological level and the inability to overcome the lag ever. In the era of former innovation factors that have supported Russia's competitive advantages in the global balance of power — large population, military superiority, abundant natural resources — in the same scale will not work.

## Part II

### The long-awaited surprise

The first part of this work as a self-report of fund “Liberal Mission” was signed into print August 24, 2011. It used as I noted, the materials of two final chapters of second edition of my book “Will democracy take root in Russia,” which came out of the print January 16, 2012. It is clear that I did not have access to it at least for the last two months of 2011. In these works, as a reader has seen, I proceeded from the fact that the range of options for development in Russia is largely predetermined by 2050 and that significant fluctuations experienced by the country after years of crisis should not wait, especially at the beginning of the period. It seems that we have crept into the political and economic stagnation from which it will be difficult to get out. The intentions of the ruling elite to maintain power without any major institutional and structural changes that it had built for itself after 2003–2004, led to the danger of the growing lag. This was said in Part I. I warn you, I did not make any changes in it and do not intend to make.

#### **8. Election of December 4 and March 4**

However, December 4, 2011 parliamentary elections took place, which brought unexpected results. The people of the conformism of which I wrote with bitterness, suddenly announced their desire to live in a democratic country. I apologize, I confess. With great joy. Rough estimates suggest that the majority of voters this time voted against the “United Russia” (“Edinaya Rossia”) — the party in power. The fact that the authorities have resorted to illegal methods of voters persuasion and direct election fraud in bigger than normal level, in my opinion, is of less importance. Also this time the attention of citizens to the elections and to the honesty of their holding was high, so it was impossible to hide the scale of abuse.

With the participation of well-known political scientist, D.B. Oreshkin, a project “Citizen Observer” was organized. He covered in Moscow 131 polling station, this is 4% of all voters. In addition, data from 245 sites equipped with a CPEB (complexes of processing election ballots) was available to observers, which also reduced the possibility of manipulation, which observers of Oreshkin also sought on the section 131.

The resulting data are shown in Table 6 in comparison with the final official figures for Moscow.

**Table 6. Comparison of the sampling results and the official results of general elections to the Duma in Moscow on December 4, 2011**

Territorial Election Commissions (TECs)	Turnout (%)	Party (% of who were present)							
		United Russia	CPRF	Spravedlivaya Russia	LDPR	Yabloko	Patriots of Russia	Pravoe delo	Not valid
Selection of "Citizen Observer" (131 area)	54.3	30.3	23.6	16.2	11.9	13.2	—	—	2.1
The sample with the CPEB (245 area)	54.9	30.0	23.6	16.2	13.8	11.9	1.7	1.1	1.7
The official results for Moscow, all	61.7	46.6	19.4	12.1	9.4	8.6	1.3	0.8	1.7

**Table 7. The difference between official and sample data on turnout and the share of parties in votes received (%)**

TEC	Percentage turnout	Share of the parties				
		United Russia	CPRF	LDPR	Esseri	Yabloko
Official data — "Citizen Observer"	+7.4	+16.3	-4.2	-4.6	-4.1	-2.5
Official data — areas with CPEB	+6.8	+16.6	-4.3	-4.4	-4.0	-3.4

Source: Oreshkin, 2012.

Table 7 shows the difference between the declared and actually received (in samples) results. We see in the two samples that there were 16.3 and 16.6% supporters of United Russia less than in the officially announced results. The difference is affected by the decline in the share of other parties, as well as over estimation of attendance and assignment of all in favor of the party in power. In addition, according to the Levada Center poll in Moscow, conducted December 8–16, 2011 on a representative sample of 1,000 people with errors less than 4.3%, the share of United Russia was 32%, meaning 15% less than general results [Levada Center, 2011]. Mathematician S. Shpilkin [Shpilkin, 2012] assessed the extra votes of United Russia in 15%. It is shown that only United Russia's number of votes in the election process was closely correlated with the turnout, the other parties were not revealed in such a connection.

Of course, Moscow is not all Russia, samples are representative, but still their bias can cause questions. We probably will never be able to fully establish the truth. However, the available data is enough to make roughly the correct conclusion: yes, the ruling party lost the parliamentary elections with a score of about 35 : 65%. At the last elections in 2007, it scored 65%, and only now officially lost 14%. If it was in 2007 attributed the voices in the same scale, yet 50% of them it won. And now absolutely lost. However, the authorities have approved the official data from the recognition of its victory: 50% of the votes and an absolute majority of seats.

My first reaction was of two kinds. From the side of the authorities — a numbing, though trouble was expected, we were prepared. At the inter-regional conference of United Russia in Yekaterinburg in late June 2011 to the question about what he would do after the presidential election, Putin said the phrase, which can now be considered historic: “Go wash: in the hygienic sense, and politically” (Newsland, 30.06.2011). But this, I suspect, he did not expect.

From the opposition — a wave of excitement and demonstrations — from Chistye Prudy on 5th and Bolotnaya on 10th of December to Sakharov Avenue on December 24th and Yakimanka again from Bolotnaya — February 4. Chistye Prudy have reminded by aggressive police and riot Triumphant area of 31th every month a year ago, but the other rallies, which got tens of thousands of people together for the first time since the early 90's, looked different. They gathered people of different views, they could freely express their ideas with the expectation, of course, of the limits of tolerance of others. Organization was over the Internet. And

the police has changed, it has become peaceful. The organizations of opposition were created — League of voters and Citizens movement.

It seemed that the results are seen.

The authorities have taken an important step forward, hoping to reduce tensions, and even split the opposition, which united all political forces, devoid of the power by the monopoly of Putin elites and United Russia. December 23, President Medvedev made an address to the Federal Assembly, which contained proposals for political reform in the direction of democratization. Of course, all this was due to December 4.

The first thought that came to my mind under the influence of a wave of public euphoria: I have brought disgrace, with my latest forecasts, with the concept of Asian conformism of Russians and other peoples of Russia. But with the accumulation of facts and a through comprehension of them I strengthened the belief that it's too early to draw conclusions.

On March 4 presidential elections were held. Although it has long been clear that Putin apparently would win again and become president of Russia, when it happened, the society and the opposition were not ready for this. What opposition leaders said and did, meant a daze about it, as the authorities felt after December 4. It was a triumph for the power. Everyone began to think that presidential elections had canceled the parliamentary elections, blew the raised wave of democratic hopes. Everything was back to its place.

Putin received 63.6% of the votes on March 4: less than its 2004 election (71%) and less than Medvedev in 2008 (70%).

But it is sufficient that its victory was considered a legitimate and compelling. There were, of course, fraud, and the overwhelming advantage of the government's candidate in the media, and the availability of administrative resources for the power hierarchy, and the law on presidential elections and the selection of candidates.

After the victory of Putin, his opponents can observe the following basic types of reactions:

- First, to save repetition of the old fighting spirit of the arguments that were suitable in December and January, but lost most of the force. We can argue about the legitimacy of the presidential elections held three times, but as for that this election should be canceled, there is no reason. Stubborn of the opponents who are likely to hold on to old arguments, works against them.
- Dive into despair: even though there was no chance, many were hoping for a miracle. And when it did not happen, the mood was

spoiled. Note, the reactions are, mainly from the sphere of emotions. That itself says that it is time to think.

## Uncertainty

The period between December 4 and March 4 was a time of uncertainty. There is a natural assumption that the uncertainty after the presidential election is over, all the threads of power again in the hands of the ruling elite, and it will continue to manage the process, step by step, nullifying the effect of the opposition. Confrontation between the government and opposition, which raised its head after December 4, thus will be put to the limit. Let me remind you that this could be similar to the suppression of democratic institutions in 2002–2005 from the acceleration of the old NTV, Khodorkovsky's trial to the adoption of amendments to the electoral law and cancelation of the election of governors. I also remind the law on extremism and harassment of NKO. This are tough politics.

This option is possible, but the repetition of the same way should raise the idea that this is unlikely to achieve the same result. It's one thing when the government supported by the majority of the population, and there was a hope that the stiffness will not only succeed in strengthening the position of the ruling elite, but also in economic development, and improvement of the satisfaction of the majority society.

But now the situation is different. Support for the power of the society is no longer assured. Society is split.

N. Zubarevich offers such a grouping of Russian population: residents of large metropolitan areas — Russia-1, the population of medium and large urban industrial cities with low competitiveness of products according to international standards — Russia-2 and Russia-3 — a vast rural periphery, small towns and villages. In Russia-1 people are more secure, mobile, and adequate, they will survive the crisis easily. Russia-3, too: the people are out of politics and survive “on earth”, patriarchal values and behavior patterns are stable. But the Russia-2 is not immune from the crisis, it needs a stable job and salary. Russia-1 wants the change, it is against Putin. Russia-2 — for stability, it is ready to support him, he still helped them. Russia-3 is indifferent, but is easily manipulated (Novaya Gazeta, 03.09.12).

The opposition politically represents Russia-1. On December 4 elections against the United Russia it was supported partly by Russia-2 and Russia-3; but then, according to L. Radzihovsky, meetings, reflecting primarily the mood of Russia-1, caused a flow of sympathy from

their sometimes too harsh slogans (Echo of Moscow, Special opinion, 7.03.2012). Maybe he's right.

Another consideration. The mass of voters is always a "swamp" easily manipulated. Now the gap between the results of Putin's and United Russia is 30%. They moved from opposition to Putin for various reasons. Perhaps most important of these was the personality of Putin, a symbol of stability, pulled over Russia-2, -3. I will add the factor of national regions, with strong cultural differences. Stability is also a major interest of the ruling elite. The opposition was left alone with the Russia-1.

Another complication: the assumption of monolithic of selected groups, including the elite, is too strong. The fact is that the elites reflected the interests and views of all groups. There are also groups that believe changes are inevitable, exactly as opposed to them supporters of maintenance in the integrity of the newly constructed political pyramid.

In the long term impact of the citizens of Russia-1 will continue to grow, they are the main carriers of knowledge and culture, that are becoming more and more important in the postindustrial society. To win their support, at least partly, the ruling elite must change the policy. Pased time showed that, although under Putin economy and prosperity grew, this was achieved not by rigidity. Rather, it intensified the discontent in the society because of rising inequality, corruption, bureaucratic arbitrariness, since it does not interfere, but rather contributed to these phenomena.

It should also be noted that after the December elections, the legitimacy of the legislative branch has become very questionable. But despite the excellent results of the presidential elections, knowing well the methods by which these results were obtained, the authorities should have to show concern and the legitimacy of the executive branch.

The results of the presidential elections were predetermined; the outcome was predictable. On the contrary, the results of parliamentary elections were unexpected. And, although the raised wave of rallies would had to subside, with high probability we can assume that any more or less significant reason may raise it again. And it will rise whenever such occasions in the current environment appear.

All this should make the ruling elite to conduct a cautious internal policy, offering at least announced steps toward democratization and some relations with the opposition, including the negotiation and institutionalization of some of its parts.

On the opposition side there was also an understanding of the arising uncertainty. Heightened perception of freedom of assembly and as-

sociation soon after December 4 was later supplemented by the threat of repression, which was reminded once again by began persecution of some media (at first rather hints) (case of Taisia Osipova and Alexei Kozlov). Even more important for the opposition should have been a feeling that the initial mass support for anti-government actions, noted mainly in Moscow, could fade away. The development of the protest movement for honest elections, demanded new themes, new forms that would have been able to maintain a sharp awareness, attract new supporters. What exactly should be done, it was not clear.

Elections December 4 marked the main force in the political arena — the ruling elite and the opposition, including parliamentary and extra-parliamentary party organization. The nature of the relationship between them can be defined, roughly speaking, the two politics — *confrontation* or *negotiation* with the compromises and concessions, and with different combinations of these forms.

### **Confrontation**

There are at least two questions on which the convergence of positions and arrangements seem to be impossible.

First. The opposition believes that the government is illegitimate. Large-scale electoral fraud has put it outside the law. It is advised from above to deal with each case. This is impossible in volume and is associated with accusations of thousands of chairmen of election commissions, which were pushed to the falsification by superiors or their assistants.

Power, of course, cannot admit this interpretation of events. And under no circumstances accept the opinion of the opposition.

The second question. The opposition demands for the recognition of parliamentary elections and their results unfair and for a new election.

Power under any circumstances cannot agree on this either.

If for discussions these two questions are put forward, it is impossible to reach agreements. This is the confrontation, which can develop into large-scale destabilization and repressive actions of the authorities.

Each party wants to achieve complete victory. And if it happened, it already knows, that would tell to the other side. But a complete victory is difficult to achieve and is associated with greater risks. For the opposition, it is quite obvious after the March 4 that power is able to do almost everything. But for the ruling elite, there are serious risks of overly rigid



policies. The mood of stubborn opposition to the authorities intensified after December 4, and to pacify them as before is impossible. In Russia, people express their opinions not only by voting, rallies and strikes, but also by theft and sabotage, which is more difficult to handle. But the authorities still need to think about the growth of the economy.

## **Two scenarios for the economy**

Let's see two scenarios (two pairs) for the new conditions, the same that are shown in Part I: modernization "from above" (authoritarian) and the gradual development, beginning from some liberalization. Modernization "from above" is fully consistent with a hard line in domestic politics, but in these circumstances is completely unsuitable for solving the challenges facing the economy. Even more unsuitable than it seemed in the summer of 2011: increase in business activity — the only factor that promises hope for success — in this scenario will not work.

To the description of this scenario from Part I, I will add a feature, given to our economy recently by the IMF Resident Representative in Russia Odd Per Brekk: "A high non-oil fiscal deficit (deficit without oil revenue, which in 2011 reached 10% of GDP), relatively high inflation, the dependence from oil prices, impossibly high government spending, cutting in the pension system. In this scenario, the country will in the medium term have sluggish economic growth — in the range 3.5–4%" (Nezavisimaya Gazeta, 27–28.01.2012).

It's essentially the same as our scenario I, but with growth rates of Odd Per Brekk suffered a surpluses. His office — the IMF, has reduced the growth forecast for the Russian economy in 2012 from 4.1 to 3.3%. And what will be then? The global crisis has not desist, and evidents of the rise we have in this scenario are not visible.

Scenario II for the economy: with the same political course but with relatively liberal tactic. It's character can be understood from Putin's articles, published as his program before the election. These are the main points of importance, as they seem to me.

1. Reduce state involvement in the economy and the extent of government regulation. State capitalism is canceled.
2. Privatization, which is not fiscal, but structural.
3. To form a favorable investment climate, we should creat conditions for increasing economic activity, by changing for this the style of law enforcement agencies. This point is especially important.

4. Competition. Putin did not disclose the subject, but, speaking about innovation, he rightly observes that the demand for innovation creates competition. Clearing the field for fair competition is almost the same as fair elections.
5. Reduce inflation by making great and positive in real terms savings and affordable loans and the terms of the normal functioning of the pension system.

It is described shortly and incompletely. Sending you to the original source (Vedomosti, 30.01.2012).

Overall, it's not bad, convincingly for economists. As the general public will respond — hard to say. This economic scenario with a liberal turn of the content meets the requirements of the economy and more like a script from the scenario II Part I. It certainly would improve the situation, though after quite a long time. But all of these items were in the Gref program, prepared by the instructions of the president in 2000. Since then, the state's role in the economy increased, the amount of the nationalization exceeded the amount of privatization. In the economy, there is no equal terms for competition. Inflation has declined enough, only in the last year, it approached the level that meets the requirements of the normal development of the economy. And separately about paragraph 3: they talked about the improvement of the business climate for all these years, but now it is not better than 12 years ago. As for the work in this area of law enforcement agencies, there was no talk about it at that time. Then the problem was the bandits, so called “roof” and the fact that the police was struggling badly with them. Now, law enforcement agencies, according to the country's leaders need to restructure its work not to worsen the investment climate. It turns out that this is a new problem, which we didn't have before or which seemed insignificant.

Another question — the possibility of this scenario with no change in policy. I believe that without a serious democratization, at least at the level of Medvedev proposals based on the comments of opposition, this scenario won't go. It won't give the confidence to business and society. And the public rise is needed.

It all inspires doubt that this scenario of economic policy during the presidential elections with expected domestic policy will be successfully developed.

However, the institutional modernization on the path to liberal reform would be very beneficial for the economy under different policy options. It can be supported by business and by many of the parties as long-term strategy which would allow a national consensus with acceptable

variations. Most likely, however, either this scenario is not driven to the end, as it was with the Gref program, or be replaced by domestic politics.

## **9. Negotiations, compromises and concessions. The gradual development?**

Thus, the opposition to the end is most likely to lead to the victory of the ruling elite, but with further very doubtful prospects, the worst consequences of which I do not even want to describe. The defeat of the opposition would be extremely harmful to the public mood, which was revived after the December 4, and inspired us for hope to the rise of civic activism.

There is another way that allows you to get away from the extremes of each side to save face, even if its opponents are set critically and cautiously to it. Putin does not see with whom to negotiate. This is extreme. Organizers of rallies require exposing of the party of crooks and thieves and the immediate holding of new elections to the Duma. This is also extreme. Another way — to agree. It is crucial to identify subjects in which you can find agreement.

### **Arguments “for”**

Those in power fear the negotiations, they do not want to share power because they are afraid to lose the authority and afraid of fear of the opponents in front of their power, as well as the excitement of the crowd, when it turns out it is impossible to stop the violence. They have something to lose. They want stability.

The opposition wants justice and power. But it is objectively different teams with different objectives, together striving for democratization. This problem causes them to stick together, seeking common effort to vote or to increase their representation in the Duma; more stable position in possible changes.

Thus, democratization in terms of stability. The time has come to recall in a different context the December letter of President Medvedev to the Federal Assembly with proposals for political reform aimed at democratizing. I do not know all the motives that moved Medvedev, I do not know the attitude of newly elected president to his proposals, even after the publication of articles on this topic. Maybe he was thrown after December 4, to relieve stress, to show interest in the changes, to pave the path to under-

standing society. But the fact remains that the step was taken by the authorities. The opposition ought to make a move. The Medvedev's draft contains proposals to cancel almost all the innovations introduced in the party and electoral legislation in 2004–2005, therefore, the adoption of these proposals creates the conditions on a new election to change the composition and the personal representation of parties in State Duma, cut, and then possibly to eliminate its dependence on the executive power, in any case increase the representation of the supporters of democracy in the Duma.

In addition, each takes a step forward, keeping the principle positions, but giving the possibility to the opponents-partners to negotiate, to compromise. At the same time, the parties have a continuous pressure on each other, leading to a new compromise. Thus, the proposals of the opposition to the law on political parties either to increase the minimum number of members, or allow the blocks, did not meet the understanding. Well, it is understandable why. It is necessary to insist! Well, isn't it the same gradual development? Negotiations with the aim of democratization in terms of stability are extremely difficult, but create the best conditions for the economy, to the option of the democratic modernization.

### **Examples from the history**

History provides many examples of democracy in this way. In the UK, after the Glorious Revolution of 1688, of course, the parliament succeeded, which did not allow the returned king to return power. But members of parliament were not elected in essence, they were nominated by local elites. As early as 1760 there were the names of parties, but the parties themselves did not exist. The right to elect and be elected has been associated with the property. In 1830, parties and elections existed, but not everywhere. At this time there was a desperate struggle for democratic representation: up to 1832 the major industrial centers of Birmingham, Manchester, Leeds had no representatives in parliament [North et al., 2011, p. 359–361]. The Industrial Revolution was accompanied by popular discontent, including the Luddite rebellion in 1811–1816, riots in the Spa-Fields and others [Acemoglu, Robinson, 2006, p. 20]. Democratization looked like a battle between rich and poor. On the event of the election reform 1832 one of the leaders of the British Conservatives in the XIX century, viscount Kreyborn wrote that the struggle for reform is a battle "...not between parties, but between the classes, and part of the great political struggle of our century — the struggle between property... and just a number" [Ibid., p. 48]. D. North and his colleagues, however, pay attention primarily on the intra-elite struggle for political influence, particularly through the redistribution of seats in parliament. At the same time registra-

tion of voters was firstly introduced [North et al., 2011, p. 361]. Later, Tory under the leadership of the Disraeli helped reduce the electoral qualifications, to increase the number of poorly educated and conservative voters, and thus gain an advantage against urban liberals. And in 1928 the UK introduced universal vote right. Almost 100 years of democratization step by step, as Acemoglu and Robinson note: without derogation.

Another example is from France. Revolution of 1789 occurred in the country almost without representation and electoral institutions. It all had to be created. During the XIX century there were experiments with different constitutional forms of government, combinations of the legislative and executive branches. From 1789 to 1875 France had 11 constitutions. Only a few have demonstrated stability. Parties appeared later, but the Royalists and Bonapartists competed in the parliaments of different types with Republicans. Together, they represent conservative and liberal, even left-liberal side of the political spectrum. Both were elitist.

Before the revolution of 1848 the right to vote was very limited, but during it the Republicans gave it to all adult men. In 1848 the Republicans had hoped to attach support of the society, but the result was unexpected. Of the 900 seats in the Assembly Left won only 70–80, 300 sites were given to moderate rural Republicans, who were such only in name. Others were opposition. In addition, in the Assembly Louis Napoleon Bonaparte was elected. At the end of the year on the re-election, he received 5.5 million votes out of 7 million voters. The conservative reaction? “It was not just a nostalgic vote for the well-known name, it was the peasants’ revolution against the entire political class” [Tombs, 1996, p. 386 (quoted from: North et al., 2011, p. 373)]. After a radical revolution — conservative policy: restrictions on the press, the restoration of the influence of religion in schools, cuts of voting rights to one-third.

But in 1851, Bonaparte asked the Assembly to restore universal voting right, but not for the reason for which later Disraeli in Britain and Bismarck in Germany acted, taking the example of Bonaparte? There was a demand on the conservatism of poorly educated rural people.

And on December 2 the same year Napoleon made a coup d’état. Plebiscite of November 21 in 1852 restored the empire.

Question to readers: doesn’t all this look familiar?

Nevertheless, in 70–80’s of XIX century in France the persecution of political parties stopped and normal political competition appeared. In 1881, laws on freedom of press and assembly were passed. The fact that ultimately, none of the factions could monopolize the use of laws and other institutions led to an agreement to comply with the rules, which made democracy sustainable and workable.

Acemoglu and Robinson have cited examples of several countries, one of which is important for comparison with Russia. I am referring to Argentina, which for 200 years, counting from 1810, the year of the proclamation of its independence, could not, until recently, create a stable democratic regime. At the same time, Argentina is populated almost exclusively by the descendants of Europeans, so that racial explanations of cultural factor is excluded.

The authors note that the democratic form of political system was established by President Boris Mitre back in 1853 but from the beginning the dominant conservative groups representing agricultural exporters oligarchy — they controlled Argentine economy basis — constantly manipulated democratic institutions. Another feature of Argentina — the active military, traditionally accustomed to taking part in policy.

Increase of dissatisfaction with the arbitrariness and manipulation of conservatives led to the creation and strengthening of the radical party, which in 1916 first came to power. A single strong conservative party in Argentina could not be established, the old elites were increasingly losing positions. Therefore, in 1930 military coup overthrew the radical, the elite democracy was seen as destructive as it prevented the export of agricultural products. The military authorities have given the power to the Conservatives, and they returned to the machinations that provoked the audience. The result — a new coup d'état in 1943. As part of the military junta the figure of Juan Peron appeared, who for years had to play a key role in Argentine politics. In 1946 he was elected president, and made a turn in favor of the workers, protectionism and import substitution. A political machine for the state control over the labor movement was created.

Removal of Peron in the 1955 because of the coup was followed by a series of military coups, rebellions, civil governments with little authority, fighting for the attention of the military, this lasted until the War of the Falkland Islands (Malvinas) in 1982. It showed all the negative consequences of ignoring the democratic norms and their abuse. There were practically no attempts to negotiate. Win! It is an experience for those who are currently undergoing a process of democratization [Acemoglu, Robinson, 2006, p. 23–27].

### **The plan of democratization**

I allow myself to go back to our affairs and to present a plan for the democratization for us. It is based on the results of recent elections and Medvedev proposals on political reform. Its base is the idea of gradual

development, which is realized through negotiations and mutual compromise and concessions instead of confrontation.

1. The opposition to support the proposals of D.A. Medvedev on political reform, especially those aimed at the democratic transformation of the party and electoral legislation.

As a first step, they are the most important. After them, we can be discussed in the Duma the issues that are impossible or meaningless with its obedience, as now.

I assume that in the government camp, these proposals are supported by definition. So the parties that are in opposition on other issues, may enter into negotiations on Medvedev's proposals — about the content, wording, the subsequent adoption.

Thus, I consider appropriate, that the opposition, including outside parliament one, legitimized on December 4 and by the subsequent mass meetings in support of fair elections, not only support the proposals of Medvedev, but raise them on board. It should be actively involved in work on the new party and electoral legislation, seeking to minimize the hooks that would allow the authorities in the future, by manipulating them, get on the election only those results that they are satisfied with. As a result we should get tangible positive changes in the composition and representation of parties involved in the Duma elections, and in the Duma itself.

2. To participate in the negotiations, taking into account the common interest of all opposition forces in the development of democracy, I would consider important to strengthen the Civil Movement and the establishment of the Round Table as an organ of the general discussions and decisions, including the representation of the Civil movement in the negotiations, organization of agencies for comments and suggestions on the prepared bills. Then the government and the current State Duma will have someone to hold talks with and it should be a major center of force to be reckoned with. It's not about my sympathies for the opposition, not all of its troops are sympathetic for me, but it is important to take into account the illegitimacy of the current Duma and to prepare a more complete representation of the new.
3. The State Duma, elected on December 4, 2011, adopts new laws:
  - on the election of the leaders of the Russian Federation by direct vote of the inhabitants of the region;
  - on the introduction of a simplified procedure for registration political parties;

- on the abolition of the need to collect signatures for the elections to the State Duma and regional legislatures bodies;
  - on change of the order of the State Duma elections, including election of specific deputies from constituencies;
  - on change of the order of formation of central and regional electoral commissions, with a view to ensuring the independence of their work from all the authorities and the individual political parties.
4. After the adoption of this legislation, under pressure from the opposition, accumulating strength for political struggle, the new special election are held in the State Duma. The need for this is related to the increased legitimacy of the parliament, and most importantly — to continue its legislative and oversight activities in a more representative composition. Elections are receded by the formation and registration of political parties in accordance with new legal norms, as well as reorganization of the electoral commissions.
  5. Newly-elected State Duma, if it will allow, its more representative staff makes decisions about the future plan of legislative work, including amendments to the Constitution of the Russian Federation, providing it consistently democratic character, as well as changing the order of presidential elections in the Russian Federation, unless the new constitution will provide such a position or significantly alter its powers.

The question about changes in the Constitution and the choice of forms for the supreme power belongs to the most complex and controversial. Even so it should be postponed for at least the second stage of democratic transformation. The main task — to get rid of the tradition of autocracy, which has now become disastrous for Russia. Without going into the debate, I note only that a parliamentary republic with a government responsible to the Duma does not give an absolute assurance: in providing a stable majority for the ruling party, Prime Minister can remain a leader as much time as he wants, and for this you need only to master the technique of manipulating elections. The experience is available.

Proposals of L. Shevtsova, I. Klyamkin and M. Krasnov (Novaya Gazeta, 09.01.2012) take into account the many nuances, but still it gives us a sense of the fragility: limitation of the powers of the President in Russian practice is easy to avoid, if you create the appropriate institutional basis. Does it allow to sustain the immaturity of our political culture? It should also be noted that changes to the Constitution will probably be discussed with the President, with the fullness of its current mandate.



I would like to remind that in Part I of this work, I wrote about the problem of legitimacy in the implementation of option “a breakthrough” and the need to first push through Parliament the changes in the party and electoral legislation. Then it seemed extremely difficult for me. The new situation, and Medvedev’s initiative greatly facilitate the solution, allowing at the same time, to postpone the issues that will likely cause a formidable odds.

The above five points are unlikely to be readily accepted. And should not. But I think that if it succeeds, they will make a significant move of Russia to democracy. It will be possible due to the election results on December 4 and Dmitry Medvedev’s initiatives. I want to emphasize this, because both of these events constitute steps towards the two sides to avoid confrontation. If all this will be a success, then we will not need to form “a breakthrough”, which under the same conditions as recorded in Part I of this work, has been associated with considerable risk.

There are no guarantees. But I will take it upon myself to say: if we implement something close to the proposed plan of democratization, then, we can get the result in a smoothed form of “a breakthrough” to democracy. This will be a more important achievement than the outcome of the presidential election. Do not consider me to be groundless optimism, but, first of all, hope needs an anchor. Secondly, it is only the beginning of hard work on democratization and modernization.

## **10. How institutions are created**

I want to return to the French experience. I remind that by the beginning of the Revolution of 1789 in France, there was almost no practice of representation and elections. The establishment of institutions has only just begun since the revolution, and democratization process lasted over 100 years old. During this time, intense competition between elite groups was accompanied by the use of laws to restrict the activities of the opposition press and freedom of assembly, by manipulating elections, so political opponents could not get power. There were also cases of violence, but they rarely were the result of intra-elite squabbles, but rather an expression of dissatisfaction with the wider classes, only partly excited by political conflicts.

Nevertheless, the authors [North et al., 2011, p. 374–375] note that in this process no one faction could not get a permanent advantage. In France they respected the idea of a representative legislative body

in which the factions could not only compete, but to seek consent to cooperate. It was traditionally a strong career bureaucracy, not devoid of professional knowledge and certain moral principles. There have been an elite and self-organization, beyond the limits of state institutions. As a result, temporarily defeated in France didn't remain without institutional and organizational support.

It can be argued that in Russia there is now the situation considerably different. Only similarity is that in 1989 we have in terms of democratic institutions, almost nothing like the French in 1789. Due to the Soviet totalitarian tradition, even in the market economy in the last 10 years the government has consistently found ways to “run down” on the self-employed entrepreneurs to support the opposition with money. The same applies to the media, with rare exceptions leaving to authorities the possibility to shape attitudes and opinions of the majority. It's amazing, but the apparent myth of a conspiracy of the U.S. State Department against Russia was supported by the workers of the Urals, delegated to a rally in support of Putin (Gazeta.ru, 23.02.2012). On other issues, such as “free” trip to Moscow the same people have absolutely objective judgments (Gazeta.ru, 2.23.12). Our culture is now lower than in France of the second half of XIX century.

Now I want to emphasize that, after the success of the first steps as a result of the democratization of the new Duma elected on the new laws, we will have to continue cultivating more and more complex institutions. Democracy is institutions.

In Part I, I gave four examples, which resembled not building, not cultivation, but often struggle. Here are three examples that are important for the urgent work.

### **Judicial independence and the USE**

In putting forward a plan of democratization and warnings against the illusion, I want to clarify my vision of the nature of our future institutional change.

A simplified plan for democratization was based on the wider spread need of voters to respect their dignity and rights, as well as the willingness of at least part of the ruling elite to take a step forward. That's why we got the relative simplicity of this step. More complicated tasks we have further. Other necessary institutional changes are more difficult, they will cause some controversy in the society and especially in the intra-elite groups.

Institutions do not usually built on a single plan or design. They are grown, cultivated over several generations. Those who are starting out, can not see the result. Those who will then use the result, most of them will not know who and for what started out, what battles were deployed around the plagues of their problems and policies of the solution. I think it necessary to say this to explain the views on the difficulties that we still have.

I'll be back to the USE, which has already been discussed above. In early 2012 I went to the hospital where I had the surgery. A woman, who recognized me, came to me and asked a question: soon will they cancel USE? Apparently, she decided that now due to the new democratic trends, they will undo all that were implemented in the first Putin's ruling period, (including Medvedev's presidency). I said never! Then, in the song of veteran-paratroopers against Putin, I again heard the people's demand — to remove the USE.

If you ask Russian citizens, whether they support the independence of the court, I think most of them do not hesitate to answer "yes". They rightly believe that we have unsecured independence of the court, because it contradicts the interests of power and the rich. But if they also ask whether they support the USE, most probably answer "no". Why not?

Meanwhile, judicial independence, which is designed to be guided only by the law, but not by graft of the rich or instructions or wishes of influential friends of the authorities, and on the other side USE as a domestic version of the universally recognized independent national test of knowledge for high school graduates — *is essentially the same thing*: generally recognized in society as being more reasonable in most cases, rather than the views of one or another, as well as the motivations that with no reason give the proper privilege one over another. The difference is that in our situation, the introduction of USE in our country is supported by the state and meets with hostility of significant part of society, while judicial independence is formally supported by the state, but in fact the bureaucracy is interested and traditionally tries to keep the tools of pressure on judges' decisions.

The specific feature of the period we are living in, firstly, is that the generally accepted rule or norm is applied to all impersonally and objectively, we still consider as an innovation, often copied, and used as the formal model, to which we usually get used with great difficulty. The institutional system of an earlier era is prevailing, where in parallel, first, the personal disposition of the ruling elite, or laws adopted by it in their own interests operates.

Secondly, the acts of buy-sale, applied to administrative and legal decisions, as the exchange of goods, and this is a bribe, corrupt deals — have spread with the rise of a market economy, ahead of the right. Third, customs, traditional norms established in the first archaic social environment also influence life. We can add a fourth element — the very impersonal legal rules, institutional innovation. It should be understood that while the opposition of other forms of social order described does not work, more or less independent and efficient judicial system, supporting these standards in their practice, they have little chance to reach the desired size spreading.

The process of cultural development, as we have seen, consists in fact that cooperative behavior is beneficial to all, but at any given moment, some subjects preferred their private and immediate interests. In pursuing them, they cause distrust and opposition to others, inhibiting the extraction of the benefits inherent in cooperative behavior [Maskin, 2010].

We are accustomed to the old order. In the case of the USE, this means that maybe it's not Andrei Fursenko came up with bad topics and tests, but we are afraid to lose a fair assessment of our children, and even more of the swagger of the rivals, who seek access to the unfair privileges. Similarly, people with power or wealth, are afraid of an independent judiciary, and judges who have judged only according to law and justice, as it also would mean for them the loss of certain privileges. But they themselves are subject to risks from other elite groups, and are to think that the impersonal objective rules are ultimately beneficial for them. Let us remember the famous case of “Three whales” textbook for an explanation of such a situation, it suffered a loss of all participants of the events. Actually not all: The Chairman of Moscow City Court, Olga Egorova, in early 2012 again reminded about herself (about her participation in particular the “three whales”), after an exhaustive report of T.G. Morschakov the Presidential Council on Human Rights and Civil Society, came up with excuses about the obviously wicked judgment on the second process of Mikhail Khodorkovsky and Platon Lebedev. They say she has all-powerful hand in the highest spheres. The Moscow City Court has confirmed the decision to ban registration of the party PAR-NAS — the most powerful, apparently, of the opposition.

### **Economy, business and “the main instrument of power”**

But the main problem is that on its own judicial reform will not give significant results. The point is that under current conditions and for the next 15–20 years, economic growth can be achieved mainly due to high

business activity, competition, and thus improve the organization and business initiatives. Business as shown above, is now under pressure from the government and bureaucracy, above all, powerful, and in these conditions will not be laid out. Today I invite the witnesses to such an authoritative person like Putin. In the “Vedomosti” on 30.01.2012 in the number of its pre-election program articles he published an article “On the problems in our economy”. For the question raised above, it says the following:

“...Business climate in the country, its attractiveness for long-term capital facilities is still unsatisfactory. Over the past few years on the initiative of President Medvedev, we started a series of reforms aimed at improving the business climate. However, significant changes have not yet happened... It’s not a tax regime — it is overall competitive — and not the absence of legislation that meets modern requirements... The main problem — lack of transparency and accountability to the public in the work of state representatives, customs and tax services to the judiciary and law enforcement system. To call things their name (wrote Putin. — *E. Y.*) we are talking about systemic corruption. The costs for businesses may vary — you may pay more or less depending on the degree of “arrangement” to you certain people within the state machinery. Rational behavior for entrepreneurs in this case — does not comply with the law, and to find sponsors and negotiate. But such a “deal” business, in turn, will attempt to suppress competition, to clear a place on the market, taking advantage of affiliate officials... rather than to raise the economic efficiency of their businesses”.

The question is: under such circumstances, if you do not rely on natural resource rents, can we expect economic growth, productivity, and even ahead of the competition, modernization? And further:

“To clear the field for a business that is ready to win in fair competition — is a fundamental, systemic problem ... We have to change the state itself, executive and judicial power in Russia. Dismantle the prosecution bunch of law enforcement, investigative, prosecutorial and judicial bodies (the chain does not appear once in the reasoning of the author. — *E. Y.*). We need to exclude from the criminal laws all vestiges of Soviet justice, all the clues that allow you to make the economic argument of the criminal case against one of the participants”.

Sorry for the long quote. But it too well explains the pivotal issue of the modern Russian economy. Relationship of different parts of the “principal instrument of power” — I called so in my book chapter on law enforcement agencies, the list of Putin there weren’t only secret service — with government and business. In the chain we can see self-inte-

rest, and the impunity granted as a reward for loyalty and willingness to support each other, to charge non-guilty in order to save the prestige and the right to continue to create outrage.

I allow myself to refer in Part I of this work, which develops the same ideas, supplemented by some conclusions. It also important for us to emphasize the inherent order of restricted informal, personalized communication in one of the vital components of the state mechanism to neutralize and remove and replace impersonal rules is particularly difficult. But it is to be done.

I do not know how. On the contrary — it is clear, we saw how it was done. And to replace the limited access with the open in this environment is not an easy task. If I see real progress of the current government in its decision, I'm ready to go to the supporters of Mr. Putin. But the application is made. And who can do it — we'll see.

### **Natural state, the order of open access and democracy**

Now I will immerse the reader in the theory.

In the work [North et al., 2011] our regular orders described above called the order of restricted access. This means, in particular, that elite or some elite group in it have the privileges to which access is limited for the rest of the population. Limited just by the origin, relationships, money. There is also the customs and laws, which, thanks to the benefits of limited access can be bypassed. The authors called natural the states, which are dominated by restricted access procedures. They are natural because the majority of current and former human history had it that way. Modern Russia is also now a natural state in this sense.

The authors also describe a new, qualitatively different social order — the order of open access, which assumes control of violence, domination rules (institutions) of persons, impersonality of relations governed by the rules and open access to public services for everyone, too, by the rules. In fact, the procedure of open access is an economic and political competition introduced into the framework of impersonal rules. North and colleagues justify the view of the development of human civilization, according to which various elite groups in the community, seeking to reduce the risk of violence towards themselves from the other elite groups or the general public, by step-by-step introduction agree to the rules, first for the elites, reduce such risks. Then, these rules apply to everyone.

Developed democratic countries — are the countries already living in the open access order, achieved a high level of development and prosper-

ity largely due to it, its merits, and not due to natural resources or military conquest. Of course, this result is not immediately apparent. It was formed in Western Europe, mainly as a consequence of market capitalist economy in the XVII–XX centuries. The combination of market competition and the desire to introduce it into healthy frame, with a decrease risk and increase useful results, over time, led firstly to a multiple increase in wealth.

Secondly, the labor force of the personal slave of people, as it was thousands of years, was transformed into a formal equal rights with employers subjects of the transaction. An increasingly important role qualification meant. There is a concentration of employees in large enterprises, thereby simplifying the organization of collective action. I will not attract attention to the growing threat of social revolution of the working class in the spirit of Marx, as the experience of many countries has shown its destructive nature and the low capacity in comparison with capitalism for creative creation. But I want to emphasize the increasing role of social and labor costs as a factor of production, which contributed to a more equitable and trusting relationships between classes in society, to a more modern institutions as regulators of human relations.

Third, the rapid development of economy, science and technology, the industrial revolution led to that ultimately wars between major powers have become too destructive, and therefore impossible. Such consciousness of the truth is not immediately perceived. Prominent state leaders are already operating with a fundamentally new institutions, did not immediately realize that these tools require a rethinking of reality. “People who unleashed The First World War, — wrote Robert Cooper, the famous theorist of European foreign policy, — believed that she would be like a short-lived war of their childhood, and did not realize that the industrial age provides smooth, almost infinite delivery to the front of people and arms” [Cooper, 2010, p.10].

After several decades in the “postmodern world” (similar to an open access order from Cooper) it appeared that “the acquisition of territory is of no interest. Acquisition of new subjects from the perspective of most states seems a nightmare”. “Today, Europe is almost entirely composed of States which have ceased to be guided by the territorial imperative” [Ibid., p. 49].

Please note that R. Cooper and D. North and his colleagues are unlikely to discuss ideas together, which we talk about here. Meanwhile, as we see, they think and write about something similar. You can accuse them of idealism, in wishful fantasies that sooner or later will break the

brutality and cynicism of the real world. However, it seems to me that these colleagues are realists more than some of our supporters of “zero-sum game”. They just see that many of our realists cannot even imagine. And they see it in life, in society and in the relations between the countries with the procedure of open access. With such as we are, of course, they have to switch to other rules.

Natural states differ in their levels of development, and quite substantially. Let me remind you that many present-day country with the procedure of open access were not so long ago the natural state. They are located near a group of countries that are on the verge of a transition from limited access to the open. Russia among them. Her transition to the new quality is of great importance to the change in its life.

Cultural shift: after, or in its process in the country should see a lot of things that did not exist before, and much of what has been a tradition, characteristic of the Russian mentality, will lose its influence. It may be, of course, done differently. But if this cultural shift will not occur or it is too late, it will be our strategic defeat in the world competition, which may no longer be possible to compensate. And we should blame ourselves.

Now, however, I would like to emphasize that the institutional changes that are coming to us, are very complex and controversial. They will meet resistance in the community, even when eventually they will do it good.

In an interview with Nobel laureates in economics, which was held at an investment forum in the presidential election campaign, Putin with a hidden irony noted that some reforms are unpopular and poorly linked with democracy. This is how he would justify himself, although his reign was terminated without the need for democracy and meaningful reforms, not counting the first two years, was not done at all. Yet there is a contradiction. In my view, this means that modern forms of democracy require a balanced combination of political competition and civil participation on the one hand, and on the other — the professional solutions of issues that do not require extensive discussion, but rather the opinions of experts. I would say that democracy Schumpeter, not Rousseau. Without idealistic exaggeration. But excluding the political monopoly.

I would note that the democratization process in the UK, France, USA, which took place at the same time that industrialization put an emphasis on the contrast between rich and poor. At a later period the center of gravity has shifted to the political competition in policy confrontation with the dictatorship and authoritarianism, as the generation of the late industrial age and increased bureaucracy. In the second period class conflict subsides. However, restrictions on freedom and competi-



tion reduce the opportunities for development. In turn, “failures” of the market more and more damped the establishment of legal and institutional framework. The procedure of open access, apparently, stands for, I think a balance of this combination.

## 11. What is changing?

Perhaps the events of December 2011 gave rise in some quarters of Russia’s liberal intelligentsia and middle class, some euphoric expectations. In fact, thinking about possible changes in the course of events under the influence of political change 2011–2012 do not give a reason for excessive optimism. Graphic scenarios shown in Figure 1, does not change significantly. But let’s not hurry. I will try to present the results of its analysis of possible changes.

Today we can say that the ruling elite, first, made a step towards negotiations, although not completely parted with a dollop of confrontation. For the country it’s a chance to resume the process of democratization.

If this is a chance to be implemented, at least in part, one could argue that we get, in terms of Part I of this paper, the smoothed version of the “decisive breakthrough”. The difficulties of change in political legitimation of the system will be removed and, consequently, the beginning of the transition from scenario I (modernization “from above”) to the scenario II (democratic modernization) will be possible after the presidential election of 2012 recall, it was discussed in Part I of this work, when we still knew nothing about the developments since November 2011, but have tried to outline the most favorable conditions for economic dynamics. They are likely to increase. We really can begin earlier the necessary institutional changes, unless, of course, this possibility is not to be missed.

Second. Above, we again identified three options for economic development, now pointing on their specifics of domestic and economic policy. Below (see Table 8), we will accompany them to estimate the probability of selection and the possible success of the implementation. Estimates — my subjective, they refer to periods prior to December 4, 2011 and after December 4, and March 4, 2012, after the election festivities. The probabilities of selection options range from 0 to 1. Assess the possibility of success (in the modernization and economic growth), this is a weighted index of growth of magnitude of some characteristics of success if you select this option.

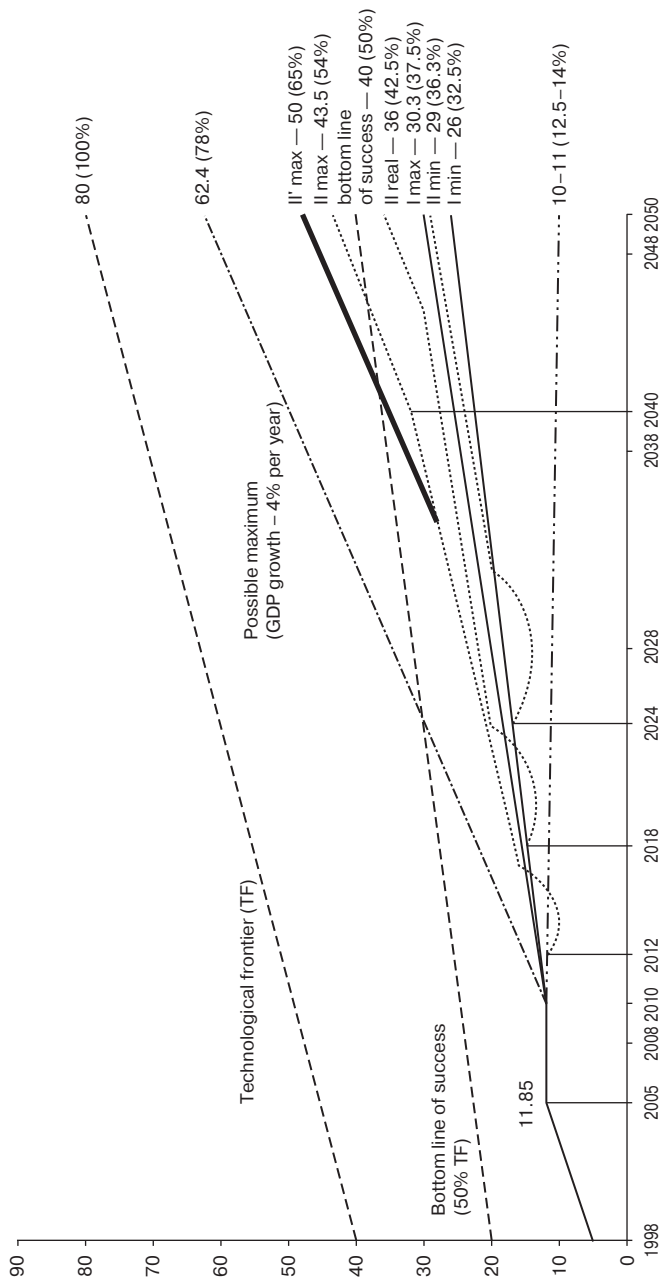
If you later decide to continue interest in such estimates, it will be neat to build indexes and interview qualified experts of their choice and assessment of success.

**Table 8. Estimates of selected options for the development of selection probabilities and possibilities of success (2020)**

Options	Up to 4.12.2011		After 4.03.2012	
	Probability of choosing	An index of success	Probability of choosing	An index of success
1. Rigid internal policies and modernization from above	0.35	0.1	0.05	0.1
2. Rigid internal politics and liberal turn in the economy	0.5	0.2	0.8	0.4
3. Democratization and modernization of industry	0.15	0.5	0.15	0.9

Briefly comment on my grades. Up to December 4, I was expecting that, despite the hopelessness of option I the power will choose it with probability of 35% for the index of success of 0.1, because they will focus on stability and minimal risks, especially for their situation. Option II has a higher index of success, so with the same domestic policies it would be chosen with a probability of 50%. But option III, although it is the most effective because of the high risk assessment would be choose with a probability of 15%.

After March 4, 2012, in spite of the excitement of past 3 months, but also inspired by the victory at the elections, the government actually stopped to consider I option, because it showed the riskiness of a strict policy when there is no progress in the economy. Option II is regarded as the most promising — the probability of selecting 80%. A higher index score reflects the increasing success of their, and my confidence in the effectiveness of a liberal turn. If you want to improve mood, positive perception of the people of this option. Option III — from this point of view, even better, but the risks increase. Therefore, the probability of selection is not increased.



**Figure 2.** Dynamics of GDP per capita of Russia under different scenarios of development in comparison with technological frontier (with scenario II' max)

Overall, the results of the scenario shown in Figure 1, does not improve.

But if we consider that the events that occurred in Russia in late 2011 increased the probability of movement to the best of the featured scenarios (scenario II max), and if the best choice is made and execution of its policy choice better than average success, then we will be able to reflect these developments in the movement in this scenario increase in the growth rate from 3% to 4% annually not over 10 years, as in Figure 1, and over 15 years until the end of the billing period (see Fig. 2). This would mean access to the 2050 level of GDP per capita of about \$50 thousand, which is equivalent to 62.5% of the technological level of that time or the use of the potential of the Russian economy (% of possible maximum) by 80% — it would be a very good result. One could say that the modernization took place.

Of course, all told — guesswork, and not a real scientific outlook. The only thing I can bring to the study — the simplest arguments and their own intuition. But they at least suggest that nothing is impossible in these achievements. In November 2011 I would not say that. And now I'm confident that this could be the effect of events in December 2011. Of course, it may not be. We expect the worst but hope for the best. Go ahead, boys.

## Conclusion

Of course, our primitive reasoning and calculations do not include even a hundredth of all the successes and failures that will occur in reality, forcing some way to respond to them. I just tried, based on approximate estimates of the most important indicators, to agree on the approximate value in the future for the major policy options. Naturally, the description of the effects of developments in each of these options, as well as the consequences of changing the course of modernization, is largely the fruit of my speculation and opinion, fueled by experience and intuition. If someone tells me that can offer more accurate results, I will allow myself to doubt.

Two alternative scenarios are outlined — “modernization from above” and “modernization from below — the gradual development” — are, in my opinion, the best basis for policy choices. Option of decisive breakthrough can be represented by a maximum scenario II, if it is realized well what is extremely unlikely. And at least for it — it is a pessimistic scenario, in case of serious complications.

In fact, the most likely development will be between these two alternative scenarios. Sure, some institutional changes will be made, and we will have to talk about modernization from below. The composition of the leadership and the general political and economic situation will depend on how severe the changes will be and when they will occur. Our analysis shows that the excessive delay in the reforms, particularly democratic, is almost tantamount to a rejection of them, and therefore, increase the likelihood of the worst effects of inertia. Benefits from a gradual upgrade, will be probably the largest, if major changes are to begin no later than 4–6 years and during this time economic, social and public sentiments will be prepared for them.

I can be reproached for the understatement of growth, such as in scenario I. Government experts expect not 1–2 but 2–3% growth, and then the differences between the scenarios be erased. In fact, I somewhat underestimated the possibility of both scenarios, as can be judged by the large gap between the potential for growth of 4% and scenario forecasts. The gap emphasizes the still growing lagging behind in the field of institutional changes and the slowness of change.

Actually, the differences between scenarios I and II are explained by the growth of institutional failure in the scenario I because of the fear of

change in the ruling elite. This should be understood by the Russian elite, and it is more important than any quantitative predictions.

It is clear that part of the elite democratization, and other required institutional changes may be associated with image and material losses. But it's worth it. Be an elite — is the duty. Otherwise, you are ballast, which should precipitate to free up space to others, the young, whose "hearts are alive to the honor".

Acemoglu and Robinson's quote: "In non-democratic society, the elite gets the policy that it wants to, in a democracy, citizens have more influence to get what they want. Because in a democracy, the elite loses, of course it has a natural incentive to oppose it or overthrow it, but the majority of democracies arise when they are created by the elite" (quoted from [North et al., 2011, p. 263]).

All in all, what did I mean by painting forecasts in a disturbing picture? I appeal to the elite: "Guys! You will do it. And then others will come".

Good luck!

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