



RE-EMERGING INDO-RUSSIAN RELATIONS IN THE NEW WORLD ORDER

EDITORS

Sanjay Deshpande • Chandrakant Yatanoor





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This book "Re-Emerging Indo-Russian Relations in the New World Order" discusses Indo-Russian relations in era of Globalization. Russia has Re-Emerged as a major political, economic and energy power since past one and half decade. India is one of the fastest Emerging nation in Global Politics. Indo-Russian Relations in last two and half decades have assumed a meaningful significance. The cooperation between these two countries has multidimensional implications. Indo-Russian relations cover several important areas. Mutual trust and confidence in each other have enabled them to reach a very high level of cooperation. The Geopolitical environment and multiple levels of bilateral and multilateral interactions have opened up new vistas for defining their partnership to raise the level of their bilateral relations without compromising the interests. This book will generate considerable debate to open up new ideas for dialogues on Indo-Russian relations.



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Oil and Domestic Politics in Russia

Tanaji Pol

The relationship between oil and gas wealth and domestic politics is an established fact in the so-called 'Recourse Curse' thesis. The countries highly dependent on resource revenue, the dictatorial tendencies are commonly manifested. However, there are few resource-rich countries exception to it, such as Norway and Canada; Russia is also one of the top three oil producing countries in the world. Oil and gas revenue provides a large share of budgetary revenue. This makes Russia a classic case for the examination of resource curse thesis.

Resource Curse

A large number of oil and gas producing economies are called as 'rentier state' because they survive on 'rent' derived from leasing oil and gas assets. Such 'rent' is also observed in other mineral producing economies. The rentier economy is very different from a productive economy which is devoid of any mineral resources but they survive on the basis of their competitive manufacturing capabilities and vibrant services sector.

A comparison between these two types of states brings out various postulates of 'resource curse' theory. For a productive state, revenue for

exchequer is derived through taxation on the domestic economy. For rentier state, revenue is derived by leasing out mineral resources. For a productive state, it becomes necessary to undertake economic growth-oriented plans and policies in order to levy increased taxes which results in governments' accountability towards the nation and its people. For rentier economy, revenue growth is often linked with the international prices of commodities and not with domestic taxation. This dependence on rents in rentier economies results in various negative impacts identified as variables of recourse curse theory.

For a productive state, survival lies in competitiveness; there is a sense of alarm and urgency to remain competitive, to improve economic and technological capabilities. There is work-reward causation in the productive state which seems to be broken in rentier state which results in socio-political stagnation and inertia. A typical feeling that rents will ever increase in future sets in rentier state. The ruling class becomes satisfied as the concern with them is not to bring development but to spend inflow of rents. Over the period inertia results in overdependence for elementary needs of society. Gabon is a classical example of inertia. Once a member of the Organization of the Petroleum Exporting Countries (OPEC) and called as 'wine capital of the world', Gabon depended on the import of even daily agricultural items like potato and tomato from abroad. Now, Gabon is a struggling economy because of drastic fall in oil production from its peak.

In rentier state, with a focus on expenditure, there is a tendency to indulge into large public expenditure, essentially a short cut to development. With the availability of large foreign exchange at its disposal, large industrial projects, mega infrastructure projects like dams and railway projects are undertaken. These projects are implemented even if they are not viable; however, they are condoned because of a continuous stream of mineral rents. The rentier state also indulges in seeking huge loans in anticipation that with the stream of rents debt could be repaid. In the long-run, not only it becomes difficult to sustain large projects but even servicing debt becomes difficult if there is unexpected fall or fluctuation of commodity price in international market.

Resource curse in many ways adversely affect the political climate of the rentier state. The enclavistic nature of oil and gas production creates

trouble. Oil and gas resources are not generally spread across the country; they are available in particular geographical region. The population of the region demands a larger share of revenue for their regional development which is not acceptable to the central government. The problem becomes acute when the region is inhabited by an ethnic majority. Now, demand can go from autonomy of the region to secessionism, such demands are again rejected by the central government. As a result, local movement turns violent, which is likely to be suppressed by use of force by the central government. These violent skirmishes would become a reason for purchase of weapons for the Armed Forces. Thus, a vicious violent circle starts within the country.

Mineral rents accumulated in high offices become a contested point for political parties in opposition. The ruling party resort to repression to discourage opposition. The accumulated mineral wealth facilitates government to hire security forces, equip them with the latest armament, and monitor citizens with high technology equipment. The government also indulges in extra-judicial killings, political imprisonments, and disappearance. However, it is observed that repression is not restricted to the oil-producing economy; other non-oil-producing economy could be equally repressive.

Further, rentier state affects the functioning of democracy through demoralising civil society group formation. Civil society is an integral part of democracy as it works as a balancer and pressure group on a day-to-day function of democracy. In rentier state, steady flow of revenue provides an opportunity to use largesse to demoralise the formation of civil society groups which are independent from the state and inclined to demand political rights. Similarly, civic institution and their autonomy play a decisive role in the functioning of democracy. In rentier state, these civic institutions are either missing or are directly under the influence of rulers. Incidentally, rents are derived from one source and accumulated in one office of a ruler. This facilitates ruling authority to distribute largesse and maintain a system of cronies. But, are all oil and gas-producing countries suffering resource curse?

The oil and gas producing nations could be classified between consolidated autocracies to consolidated democracies. This range could

be divided into four groups. The first group is on the side of consolidated democracies which include countries of Western Europe, North America and Oceania, Norway, Canada, Denmark, and the United States. These are leading liberal democracies. The second category includes working democracies of Latin America oil and gas-producing states like Venezuela, Mexico, and Trinidad as well as Tobago. These energy-producing countries are not only more democratic than other countries on the continent but are also more likely to democratise over the years. The third group comprises countries which are close on the side of autocracies and are mostly from sub-Saharan Africa. A clear relationship is evident with the increase in oil and gas revenue and tendencies of autocracies in this region. The fourth group comprises autocracies of the Middle Eastern region where there is an absence of democracies. Where lies Russia in the debate of resource curse? Russia could largely overcome resource curse which is explained in the subsequent section.

Fiscal Bargain

It is commonly understood that the development of democracy is closely related to the right of a citizen in the governance of state because of its contribution to the state exchequers. In oil and gas-producing countries, the state exchequer is filled with oil and gas reserve or revenue. The contribution of local taxes by citizens is negligible; as a result, the state does not oblige its citizen. The rulers live as 'rents', surviving on revenue received from leasing out mineral resources rather than relying on taxes. In many countries of the Persian Gulf, devoid of democracy is directly linked with 'rentier' states. In the Persian Gulf states, citizens barely pay taxes but they receive many services free of cost from the state like education, healthcare, housing allowances, and even guaranteed jobs. This largesse is sufficient enough to control desire for the political right.

In Russia, such largesse cannot be distributed for few important reasons. The Persian Gulf countries have a common characteristic of high per capita income. It is as high as US\$ 1,40,645 per capita gross domestic product (GDP) in Qatar. Kuwait has US\$ 73,246 per capita GDP whereas the United Arab Emirates has US\$ 67,674 per capita GDP which allows them to distribute largesse. In Russia, it is US\$ 22,990 per

capita GDP which is not as high to provide basic amenities free of cost to masses. Thus, the impact of oil revenue on the functioning of democracy is negligible. Additionally, the size of population in Russia is much larger in comparison to the Persian Gulf state; for example, Qatar and Kuwait have population 25,26,994 and 41,83, 658, respectively; whereas Russian population is many times higher and estimated to be 14,65,44, 710; as a result, the Persian Gulf like largess cannot be distributed in Russia.

The modern tax system differentiates Russia from Persian Gulf states. In Russia, personal and corporate taxes contribute a substantial part of budgetary revenue even though oil and gas is an important revenue-generating resource. The present-day tax system was implemented by the Russian Parliament in 2000-01. This newly introduced tax law substantially altered both direct and indirect taxes; as a result, today Russia has a modern and internationally competitive tax system. Russian taxes are listed and regulated by the Russian Tax Code which includes all modern forms of taxes like VAT, excise duty, personal income tax, asset tax, land tax, etc. The profit tax is calculated at 20 per cent which is one of the lowest in large economies. Some of the latest developments in the tax system in Russia included the best global tax monitoring practices which measure to stop misusing of low tax jurisdiction of tax heavens and availing unjust tax benefits. Similarly, many new incentives are offered to promote innovation and the modernisation of industries.

In Russia, not all taxation revenue from oil and gas companies is provided by a nationalised company. Private oil and gas players also contribute a significant amount. Oil from national oil companies cannot fully support Russian budget and will have to negotiate private oil and gas players. This contribution remains significantly high even after President Putin's drive to nationalise oil sector and nationalisation of Yukos, Siberneft, and Sakhalin II renegotiation. Today, private oil and gas companies may not be as large as they were in the 1990s, but even if small and segregated they have an important role to play in revenue generation and the state cannot overlook them.

Oil and Modernisation

Modernisation is closely linked to resource curse. In-fact, democracy is closely linked to modernisation of society as the prevalence of democracy

is much higher in modern society. Oil and gas producers of Europe and North America are set parameters of modernity and are a shining example of keeping resource curse away from society. Modernisation is attributed to education, industrialisation, urbanisation, occupation specialisation, accountable government, and open mass media. Modernisation helps in overcoming resource curse in multiple ways. The higher level of education in society helps in forming more articulate population which is better equipped in organising themselves and communicating on various societal issues. Modernisation also brings workforce which is better informed about their rights. The workforce initially starts developing with occupational specialisation and moves into secondary and tertiary sectors. The workforce becomes more autonomous and becomes capable of entering into bargaining and negotiations to protect their rights. However, modernisation cannot be directly equated with mere fast growth in the economy like observed in many Persian Gulf states. Modernisation, thus, is not brought about by the state but by a social mechanism.

Russia is a modern society by all standards. The literacy rate in Russia is estimated to be 99.7 per cent, one of the highest in the world and at par with any of modern societies in Europe and North Africa. It is also noteworthy that women education is equally robust in as male education estimated at 99.6 per cent. Russia also has a distinction of having the highest attainment of college-level education in the world—estimated at 53 per cent of Russian adults which is almost 20 per cent above average European society. Russia has vibrant cultural space spanning from architecture, visual art, music, and dance. Literature and Philosophy holds a special position in Russian culture. It has a rich heritage of Russian philosophy spanning over centuries and is still preserved by the Russian society. Russia has a similar rich heritage in literature. Thus, Russia is a modern society which separates itself from the Persian Gulf states.

With the vibrant modern society, Russia also possesses modern industrial economy. The GDP composition of the Russian economy is like any other advanced economy. In the GDP, services sector takes the largest share of 58.3 per cent, followed by industry with 37.5 per cent and agriculture with 4.2 per cent. The Russian economy over the years could achieve this level with successfully shedding its earlier mode of centralised planning

inherited from the Soviet days. Today, Russia possesses ample resources and mineral wealth to propel its modern industries as well as has a well-educated labour force with substantial technical expertise. The Russian economy has today well-functioning and a complete range of mining and extractive industries with products like oil and gas, coal, strategic metal, and chemicals. A vibrant machine building industries churning products from road and rail transport vehicles, agricultural machinery and tractors, construction equipment, electric power generating transmitting equipment and medical and scientific instruments. In addition, it has an unmatched military-industrial complex with products like high-performance aircrafts, radar, missile, armored vehicle, advanced electronic components, shipbuilding, and space vehicles.

Diversification

Diversification of economy is crucial in 'resource curse'; especially efforts to lessen dependence on oil and gas revenue. It is observed that nations dependent on oil and gas revenue or other limited range of products do less well in the long run whereas diversified exporter nations are associated with higher and long run growth. Sole dependence on one resource of revenue would be barely sufficient to meet the demand of growing population. In the long run, the overall prosperity and stability will demand the productive employment of masses and gaining the higher level of skills. Another reason for diversification is to meet the vagaries of oil and gas price fluctuations. Diversification self-insures national economy against possible shocks of sudden fall in prices of commodities and saves the nation from possible macro-economic shocks. Diversification helps in many ways to oil and gas producing economy. By starting to export the industries in the nation acquire the higher level of capability and competitiveness which leads to capabilities to produce and export other products in allied sectors. It also enables dynamic lean-by-doing gains.

In Russia, even if there is high dependence on oil and gas revenue, the economy cannot be stated as excessively dependent on one source of revenue. As mentioned earlier, the economy has all three sectors, viz., agriculture, industry, and service sector and has all potential to overcome deficiencies of diversification. Russia possesses highly skilled labour

which not only easily acquires necessary technology and skills but also improvise it. At present, the Russian economy is facing a tough time because of historic low prices of oil and this could be the test of strategies for diversification. The Russian government has already embarked on a path of diversification. It is promoting its military industry complex aggressively; some new products are constantly on display. This aggressive marketing was not observed before. Russia is equally promoting other mineral sectors especially diamonds, extra attention is given to reach to large markets like India for diamonds.

The importance of diversification of economy can be best seen from many emerging nations of Asia who have acquired skills to become diversified export economy. They have achieved unprecedented economic growth, in many cases, it was double digit growth. These Asian economies have outshined many mineral resource exporting economies. It is also noteworthy that many of these Asia economies are not self-sufficient in energy, they import energy commodities from across the world like China, India, South Korea, Taiwan, Hong Kong, etc. India, in particular, can share a lot of experience in export-oriented diversified economy. India is an oil and gas deficit country and relies on more than two-third of imported oil. The competitive edge in the export-led sector was achieved over decades. India's early exports were in the elementary sector of textile, steel, handicrafts, etc. A big success was first achieved in service sector exports mainly in the Information Technology. There was also simultaneous growth in other manufacturing industries like pharmaceutical, heavy engineering, ship building, and petroleum refinery. The automobile industry is a good example of export growth. It started solely with focus on the domestic market but over the years not only components were manufactured but even complete design of a car was created in the country. Today, India is home to all world leaders in automobiles and is manufacturing cars for exports. The refined petroleum products are India's largest exports today. To take manufacturing sector into a higher level, the Government of India has launched 'Make in India' programme.

Conclusion

Russia has relied on revenue derived from oil and gas exports for decades.

This revenue has had been playing a crucial role in the overall economy of Russia and this makes the nation vulnerable to 'resource curse'. Some effect can be seen at present as Russia is facing slow growth in the economy because of the prevailing low international oil prices. Another example of the effect of excessive dependence on oil and gas revenue was given during the Soviet era. It is suggested that due to similar excessive dependence on oil and gas revenue and the then prevailing international oil prices below US\$ 20 became one of the major causes of the disintegration of Soviet Union. Is Russia vulnerable to 'resource curse'? Scholars are divided over this issue, opinions range from extremely vulnerable to mildly vulnerable. There are various reasons why Russia is not susceptible to 'resource curse' like many economies in Africa and the Persian Gulf.

The Russian economy, as mentioned, is an advanced economy in comparison to many of its oil and gas producing peers in Africa and elsewhere. It has achieved much a higher level of scientific and technological skills because of not only nearly complete literacy level but also a much higher rate of prevalence of higher and technical education. This has provided the highly qualified workforce to Russia. Russia's world class capabilities in science and technology are visible in many of its products like fighter aircraft, battle tank, nuclear reactors, and other streams of biological science. Thus, Russian society is not like any other society, who are dependent on oil and gas. Besides this, there are several other sectors that contribute to the economic growth of the country. The other effects of 'resource curse' on society are like unaccountable government because of zero taxation too does not work. Russia not only has broad-based taxation but highly educated and learned society which is capable of organising themselves.

However, the present slowdown in the Russian economy indicates that excessive dependence on oil and gas revenue could result in setbacks especially in the scenario of low oil prices. It is necessary to diversify economic activity. The experience gained in many emerging Asian economies has rich experience to share in diversifying their exports. India's experience in the diversification of its export items especially moving towards higher products over the years. India with these efforts to enhance exports could register unprecedented growth level of touching

7 per cent for a decade. The export capability developed over the years and automobiles sector in India is a good example of it. Russia too has realised the importance of diversification of its exports and accordingly it is focusing on sectors like military hardware, diamonds, and nuclear reactors. Over the years in Russia, when its economy is fully diversified and its dependence on oil and gas reduced, Russia will observe the negligible impact of 'resource curse'.

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