

## **Chapter 5**

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### **Russia**

#### **Tension with the West, and the Diversification of Foreign Relations**

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In Russia, amid ongoing antigovernment protest movements and against the background of a number of terrorist incidents, President Vladimir Putin has been seeking to limit the impact of these developments in his bid for reelection in the March 2018 presidential election, and has been working to realize stable governance of the country. Even after the inauguration of President Donald Trump, Russia has still found no opportunity to improve relations with the United States and Europe. The Kremlin is, instead, working to raise Russia's global profile through intensified diplomatic activities with countries in other regions. Russia's relationship with China is the most important among its international relations in East Asia. The government has been steadily promoting ties with China through participation in high-level forums on international cooperation, such as a meeting on the Belt and Road initiative (BRI) held in Beijing, as well as summit meetings, but differences of interests and focus are also observed between the two countries.

Regarding the North Korea issue, Russia has from time to time been exhibiting a unique pattern of behavior. Even so, its fundamental stance is to continue calling for the easing of tensions in collaboration with China. Russia also places great importance on its relations with Japan, from the perspectives of its own development as well as regional diplomacy. Progress is slowly being made under the economic cooperation agreement reached with Japan in 2016, as well as through joint economic activities on the four islands of the disputed Northern Territories.

The Russian economy is recovering gradually, but the government has not yet achieved the vital conditions for sustained economic development, and this might affect the Kremlin's ability to maintain stable rule over Russia in the coming years. Consequently, the Putin administration positioned 2017 as a period during which it would prepare the ground for sustained economic development. As a first step, it introduced a new fiscal discipline regime and set an inflation target, among other measures to create a framework for future fiscal and monetary policy. Other notable developments in 2017 included various activities in the economic field that were coordinated with Russia's diplomatic initiatives. For example, in the energy sector, which is the most important for the Russian economy, the Organization of the Petroleum Exporting Countries (OPEC) and Russia systematized their cooperative ties through talks at the highest level, with the goal of stabilizing global crude oil prices. In addition, to ensure Russia's access to export markets and funding sources, initiatives have been pursued to strengthen

capital ties between Russian companies in the energy sector and their counterparts in India and China.

Zapad-2017, a large-scale military exercise conducted in Russia's Western Military District, is believed to have been primarily prompted by the confrontation with the North Atlantic Treaty Organization (NATO). During 2017, Russia continued to pursue military operations in Syria. This allowed the military to put its new systems into practice in actual warfare conditions, and thus gain valuable experience, while at the same time raising Russia's profile as a political and military presence capable of influencing the direction of events in the Middle East. Moscow has also been strengthening diplomatic ties with many of the Middle East nations.

Russia has also been implementing measures to strengthen its military capabilities in East Asia and the Arctic region. New military divisions have been set up, military exercises conducted, and surveys carried out in preparation for the creation of new military bases. The Russian military has also conducted joint maneuvers with friendly countries such as China, and has made steady progress in reinforcing cooperative ties through weaponry export contracts and other means.

## **1. Internal and External Policies Subsequent to the Start of the Trump Administration**

### **(1) Domestic Governance Aimed at Realizing Long-Term Stability**

Throughout 2017, ahead of the presidential election scheduled for March 2018, Vladimir Putin worked to present to the Russian people his vision of the most appropriate way to lead the country over the next six years. Continuing on from 2016, the Putin administration appointed a number of promising young politicians to posts in the federal government and as regional leaders. In this way, Putin has been laying down a human resources network that will be able to maintain the current administrative organization even after his next six-year term as president comes to an end.

In terms of the achievements and significance of the Putin administration, Putin puts priority on ensuring that Russia is a strong and politically stable country, and thus national defense and the maintenance of law and order are important issues. In April 2017 in Saint Petersburg—during a summit meeting between Putin and President Alexander Lukashenko of Belarus—a terrorist bomb attack occurred on

the city's Metro system, resulting in 14 fatalities. Then, in September and October, a number of anonymous telephone calls threatened the bombing of public facilities all over Russia, forcing urgent evacuations on successive days. In response, the Russian authorities felt that they had to interdict or restrict communications over the Internet so as to maintain public security, and they took steps to ban the use of a number of social media platforms that relied on servers located outside Russia, including Line. Previously, in July, Russia had passed a law prohibiting virtual private networks (VPNs), which could be used to circumvent Internet connection regulations.

These moves by the government provoked opposition. Protests were held in Moscow, Saint Petersburg, Novosibirsk, and elsewhere in July and August against the aforementioned Internet access restrictions, as constituting infringements of freedom of speech. In 2017, the group led by Progress Party leader Alexei Navalny stepped up its activities in comparison to the period prior to the State Duma elections of 2016, and Navalny himself wrote a number of articles on his blog and elsewhere exposing corruption on the part of high-level government officials. Navalny had first come to public prominence in 2011 as one of the central figures in anti-government demonstrations, and he gained a growing number of supporters through his statements via social media. He ran for mayor of Moscow in the 2013 election, garnering 27 percent of the vote. In the event that support for Navalny increases further, this could erode Putin's current overwhelming political dominance. The Putin administration is thus thought to be keeping a close eye on his moves.

In March 2017 Navalny launched a campaign that accused Prime Minister Dmitry Medvedev of corruption, and organized rallies in ninety-five Russian cities. A subsequent opinion poll showed that support for Medvedev had fallen. Also at Navalny's urging, his supporters staged demonstrations in many cities across the country—notably Moscow, Saint Petersburg, Vladivostok, and Khabarovsk—on October 7, which is Putin's birthday. In December, Navalny filed his registration as a candidate in the 2018 presidential election with the Central Election Commission, but this was rejected on the grounds that Navalny had been found guilty of embezzlement. In response, Navalny called for a boycott of the election.<sup>1)</sup>

On numerous occasions from autumn into winter, informed sources stated that Putin would soon be announcing his intention to seek reelection, but time and

again it failed to happen. Finally, at a meeting of young volunteers on December 6, he announced to great acclaim that he would probably enter the race if there was sufficient public support. Then, in response to a question put to him at a meeting held the same day at an automotive plant in Nizhny Novgorod, he unequivocally stated his intention to seek reelection.<sup>2)</sup> In this way, Putin revealed his intention to ride a wave of support from young

people and blue-collar voters to win reelection. At a large-scale press conference held on December 14, while not giving any details of his specific policy plans, Putin listed among his priority areas the development of Russia's infrastructure, health, education, advanced technologies, and labor productivity.<sup>3)</sup> According to Russia's Public Opinion Foundation (FOM), an opinion poll conducted in late December showed overwhelming public support for Putin as a presidential election candidate, at 68 percent, with other candidates receiving 7 percent or less.<sup>4)</sup> The reelection of Vladimir Putin is thus seen as a foregone conclusion.

The central point of interest with regard to the Putin administration is whether or not he can succeed in making full use of the strong public support he currently enjoys to forge—over the next six years and beyond 2024—a governing framework that will deliver a stable Russia. For this reason, although Putin will have to attempt full-scale reforms, including of the economic structure, between now and the end of the election, he is thought unlikely to unveil any specific policies that might weaken his popularity with the voters.<sup>5)</sup> Thus, it appears that the Putin administration during 2017 quietly engaged in laying the groundwork for reforms to be implemented in 2018 and thereafter.

## **(2) Continued Tense Relations with the Main Western Nations**

For Russia, the United States is the source of most security-related problems on the European front, but at the same time it is a key partner in dealing with international terrorism, among other issues. For these reasons, Russia's

fundamental desire is to develop its relationship with the United States in an appropriate direction, and the election of Donald Trump—who had expressed the wish to improve relations with Russia—was welcomed by Moscow. However, due to the emergence of a variety of problems within the United States following Trump's election, the US president's relationship with Russia has been unstable. For the Russians' part, they have been unable to find any concrete way to break the deadlock, and relations are deteriorating.

Both before and after Donald Trump was inaugurated as president in January 2017, American media circles were already awash with rumors and claims that the Russian government and Trump's campaign team had colluded in inappropriate activities. On January 6, 2017, the United States Intelligence Community released a report on alleged Russian interference in the US presidential election. According to the report, the Russian authorities had disclosed to large numbers of US voters—via government-controlled media channels as well as social media—inside information obtained by means of computer hacking, with the aim of influencing the results of the 2016 presidential election. By so doing, it was alleged, Moscow had attempted to undermine public faith in the US democratic process.<sup>6)</sup>

Subsequently, suspicion that Donald Trump himself and/or top officials in his election campaign team had colluded with the Russians to influence the election result began to grow, culminating in an ongoing potential scandal generally referred to as “Russiagate.” The Federal Bureau of Investigation (FBI) initiated a criminal investigation, and a series of departures from their posts of officials in the Trump administration ensued. Believing that further sanctions against Russia were necessary in retaliation for Moscow's interference in the election process, Congress passed new legislation enforcing sanctions, which also targeted Iran and North Korea as well as Russia. Moreover, the legislation included provisions requiring the president of the United States to seek the agreement of Congress in the event of either applying or lifting the said sanctions. President Trump criticized this legislation on the grounds that it limited the negotiating powers of the executive branch of the US government without due cause, but nonetheless signed it into law.<sup>7)</sup> The Kremlin responded by reducing the number of accredited US diplomatic staff on Russian soil.

In the United States, meanwhile, suspicion had been growing for a number of years that Russia was developing ground launched cruise missiles (GLCM), which would have an effective range in violation of the provisions of the

Intermediate-Range Nuclear Forces (INF) Treaty. In March 2017, Congress heard expert testimony to the effect that the weapons system in question—the SSC-8—had reached the operational phase.<sup>8)</sup> In retaliation, Russia asserted that the missile launchers which the United States was preparing to deploy as part of its European missile defense were equally in violation of the INF Treaty.<sup>9)</sup> As the New Strategic Arms Reduction Treaty (New START) is due to lapse in 2021, the United States and Russia will have to begin negotiations on new measures to control the deployment of strategic nuclear weapons, but a number of experts in the United States fear that the currently ongoing failure to implement the provisions of the existing INF Treaty will have an adverse influence on the situation.<sup>10)</sup>

While recognizing that its relationship with the United States is deteriorating, Russia has been maintaining a dialogue with the United States and in this way leaving open the possibility of improving its relations with the Trump administration. In talks with President Xi Jinping of China, President Trump on April 6 announced that he had authorized limited cruise missile strikes in Syria in response to the Assad administration's use of chemical weapons.<sup>11)</sup> In response, President Putin criticized Trump's action as a violation of international law, in that the United States had attacked Syrian government positions despite the United Nations having confirmed that the Assad administration had destroyed all its chemical weapons. Putin stated that this event had worsened Russo-US relations.<sup>12)</sup> Nevertheless, United States Secretary of State Rex Tillerson visited Moscow as scheduled and held talks with Putin and Foreign Minister Sergei Lavrov.<sup>13)</sup>

In May, Lavrov visited Washington and held talks with President Trump and Secretary of State Tillerson.<sup>14)</sup> Then, at a G20 summit in the German city of Hamburg in July, Putin and Trump held their first one-on-one meeting.<sup>15)</sup> This was followed in November by further talks between the two leaders at the Asia-Pacific Economic Cooperation (APEC) summit held in the Vietnamese city of Da Nang. In the previous October, at a meeting of the Valdai Discussion Club (a forum for international experts) held at Sochi, President Putin gave a speech in which he attacked the sanctions imposed on Russia by the US Congress, but it was notable that he refrained from direct criticism of President Trump.<sup>16)</sup> Within Russia, the view is gaining ground that whereas President Trump himself is adopting a positive stance on improving relations between the United States and Russia, his efforts are being hampered by Congress, where an anti-Russian stance has taken strong root.<sup>17)</sup>

Meanwhile, sporadic conflict continues here and there in Ukraine. For instance, in February 2017 fierce fighting erupted in the city of Avdiivka, located in Donetsk Oblast (province) in Eastern Ukraine. While the parties involved have managed to avoid an escalation of military conflict beyond this region, Russia's 2014 annexation of Crimea and its involvement in the conflict in the eastern part of Ukraine remains a fundamental reason why both the United States and the member-states of the European Union regard Russia's actions in this region as unacceptable. The EU is also following the lead of the United States in maintaining economic sanctions against Russia, on the grounds that there are no signs of any improvement with respect to Ukraine-related issues.<sup>18)</sup>

As is the case in the United States, European countries are becoming increasingly concerned that the Russian authorities are attempting to manipulate public discourse in both the conventional news media and via social media channels to damage valued concepts such as democracy and the unity of the European Union.<sup>19)</sup> In the case of the French presidential election, at the Kremlin in March, Putin talked with National Front leader Marine Le Pen, who has called for French withdrawal from the EU and for an end to the sanctions against Russia. Presidential candidate Emmanuel Macron claimed that his campaign had been subjected to computer hacking,<sup>20)</sup> but soon after Macron was elected president, Putin visited Paris and sought to build ties with the French leader.

In the face of constantly mounting distrust of Russia, no political leaders have emerged in either the United States or Europe who are capable of implementing policies that favor Russia. For this reason, Russia has been unable to discover any opportunity to effect a fundamental improvement in its relations with these countries. The Russian authorities are thought to be avoiding any hardline measures that might exacerbate the situation, and to be awaiting a more favorable opportunity.

### **(3) Involvement in East Asian Developments**

East Asia is another part of the world where Russia is focusing on strengthening its diplomatic presence. In particular, Russia has positioned China as its most important strategic partner. Not only is Moscow working to maintain a stable relationship with Beijing, but there has been an increasing number of opportunities for the two countries to demonstrate common ground in dealing with international issues. However, the governments of both countries are taking care not to be

bound by specific ties of alliance with one another, and are leaving themselves ample leeway to pursue their own interests.

In May 2017 Putin was the most honored guest at a forum held in Beijing to discuss China's BRI. However, the route to Europe currently being promoted most enthusiastically by China within the overall BRI runs through the countries of Central Asia and then via Turkey, and is thus unlikely to have much beneficial impact on the Russian Far East, which is the region on which Moscow is focusing most heavily in the drive to further develop its infrastructure. In addition, according to some Russian experts, insufficient resources are being invested to ensure the actual implementation of this initiative.<sup>21)</sup>

On July 4, President Xi Jinping paid a visit to Moscow as part of a tour of European capitals, and held a meeting with President Putin. Putin bestowed on Xi the Order of St. Andrew the Apostle, an honor hitherto bestowed on only two other non-Russians—President of Kazakhstan Nursultan Nazarbayev and President of Azerbaijan Heydar Aliyev. In a joint statement, the two leaders emphasized that relations between their countries were currently better than they had ever been before; they jointly expressed opposition to the United States' missile defense plans as being a threat to world strategic stability; and in reference to the situation on the Korean Peninsula, they called on the Democratic People's Republic of Korea (DPRK) to exercise self-restraint in nuclear weapons testing, and on the United States and the Republic of Korea (ROK) to exercise similar self-restraint with regard to joint military exercises.<sup>22)</sup>

As can be seen from this, the fundamental undertone of Russo-Chinese relations is one of cooperative development, and relations are characterized by a large number of bilateral communication channels, including frequent summit meetings. Having said that, the differences in the two countries' interests that have been pointed out in recent years remain in place, and in addition, attention is focusing on new issues arising as a result of China's economic and military development. For example, it has been said that Russia and China are practicing a form of "division of labor" in Central Asia, with Russia taking the lead in national security matters and China taking the lead mainly in economic development. But it is by no means certain that China will be content in the future to continue limiting its role to the economic sphere, and experts in the security field in Kazakhstan have pointed to China's having begun to undertake activities in the security field, too.<sup>23)</sup> Moreover, concerns have been raised in Russia

regarding maritime norms and China's involvement in the Northern Sea Route.<sup>24)</sup> In this way, from Russia's perspective, there are issues that can be ignored for the time being but are likely to become problematic in the future, and it is thus necessary to keep in mind that such future developments are implicit in the Russo-Chinese cooperative relationship.

The Korean Peninsula situation, which became a major talking point in 2017, is one of the issues that Russia is tackling in collaboration with China. In parallel with the aforementioned July 4 summit meeting, the foreign ministers of the two countries also issued a joint statement, in which they stressed that both North Korea on the one hand and the alliance of South Korea and the United States on the other should exercise self-restraint in military activities and move on to the next stage in solving the problems that beset the peninsula.<sup>25)</sup> Moscow and Beijing refer to this approach as a "roadmap." Moreover, Russia places emphasis on the maintenance of the nuclear non-proliferation framework, and remains opposed to the possession of nuclear missiles by North Korea. And while the Russian government does not believe that economic sanctions alone can resolve the issue, it also believes that the interests of other countries in the neighborhood of the Korean Peninsula—not just the United States and North Korea—should be taken into account. Consequently, it emphasizes the importance of a framework for dialogue encompassing the six-party talks, among others.<sup>26)</sup>

As a result of the closeness of the relationship between North Korea and China, there is considerable tension in the relationship, but Russia is more easily able to gain the ear of the Pyongyang leadership because of its comparatively neutral position, and this is why Russia now and again exhibits a unique pattern of behavior. In response to North Korea's missile test-firing on April 15, the United States submitted to the United Nations Security Council (UNSC) a draft statement criticizing the DPRK's moves. This took place just after a US-China summit meeting at which the two parties had agreed to exert pressure on North Korea, and Beijing did not object to the US draft statement. Russia, however, announced its opposition to the statement on the grounds that its wording did not call for the resolution of the issue through dialogue. After the US statement had been amended in line with the Russian objection, it was issued by the UNSC on April 20.<sup>27)</sup>

China cut the volume of its trade with North Korea as part of overall efforts to apply pressure on Pyongyang, but the volume of trade between North Korea and Russia rose. Moscow gave permission for the DPRK ship *Man Gyong Bong* (a

cargo-passenger ferry) to dock at Russian ports, but the ferry's run was cancelled between August and mid-October. Choe Son Hui, head of the DPRK Foreign Ministry's North American bureau, visited Moscow in September and held talks on the cause of tensions in the Korean Peninsula.<sup>28)</sup>

These various actions by Russia are, however, of limited impact. When President Putin and South Korea's President Moon Jae-in held talks on September 6, Putin expressed skepticism regarding the effectiveness of economic sanctions, but the UNSC passed a resolution on the 11th of the same month calling for further sanctions against North Korea.<sup>29)</sup> China continued to consult with the United States and took a hardline stance against North Korea, but while the volume of trade with that country has been falling, China remains overwhelmingly the most important presence for the North Korean economy. Russia has insufficient leverage with respect to the North Korea problem to affect China's initiative, and there is no evidence that international efforts to change the course of the DPRK's leadership have made any significant headway thanks to Russia's intervention.

Russia's main interests in the Asia-Pacific region include maintaining a stable relationship with China and pursuing economic development, expanding its presence through such means as contributing to solving the Korean Peninsula problem, and promoting the introduction of investment and technology that will help develop and support the economy of the Russian Far East. Russia's relationship with Japan is closely involved in these issues. By inviting Japanese Prime Minister Shinzo Abe and South Korea President Moon Jae-in to the Eastern Economic Forum held in Vladivostok in September 2017, the Russian authorities sought to emphasize the importance of economic ties with these two countries. Russia has a good relationship with China at the moment, but in the event that this relationship were to deteriorate at some time in the future, Russia would have to turn elsewhere, and it has been suggested that Russia is seeking to build a better relationship with Japan in order to have an alternative partner in the region.<sup>30)</sup>

In 2016 Japan and Russia agreed to move forward with economic projects based on a "cooperation plan," and to engage in joint economic activities on the four islands that comprise the disputed Northern Territories so as to pave the way toward the signing of the long-awaited post-WWII peace treaty. Despite this, Russo-Japanese relations have not been going smoothly on all fronts, and a clear difference has emerged between the two sides' views on national security issues as well as the Northern Territories question. On June 1, 2017, in response to a

question posed by a Japanese journalist, President Putin attacked the US plans to expand its missile defense system, claiming that this was being done under cover of the pretext of countering threats from North Korea. He also made reference to Russian suspicion that if the disputed northern islands were to be handed back to Japan, the United States might install military bases there.<sup>31)</sup>

On June 15 a briefing for Japanese officials and journalists was held at the Russian embassy in Tokyo, at which the Russians again expressed concern about the US plans for missile system deployment.<sup>32)</sup> Then, on the 23rd, Russian customs officials seized a number of textbooks from a teacher of the Japanese language who was visiting Kunashiri Island on a visa-less exchange scheme, but as this could be viewed as an example of the Russians demonstrating their jurisdictional authority, the Japanese authorities stated that this action was unacceptable.<sup>33)</sup> In this and other ways, including the staging of military exercises (discussed in more detail later), the Russians have been emphasizing their stance that the four northern islands are unequivocally Russian territory.

Nevertheless, in order to achieve gains over the long term, Russia has been working to improve relations with Japan by taking account of Japan's needs. During Prime Minister Abe's visit to Moscow in April, it was made clear that progress was being made on items agreed for cooperation, and that the Russians intended to maintain a continuous development of the bilateral relationship. Regarding the joint projects relating to the Northern Territories, in August progress was made on simplifying procedures for travel to and from Japan and the northern islands without need for a visa, and a party from Japan visited the

territory and held discussions on cooperative projects. In the security field, too, in March 2017 another Japan-Russia Foreign and Defense Ministerial Consultation ("2+2" Ministerial Meeting) was held, the first since 2013.<sup>34)</sup>

In September 2017 Nikolai Patrushev, Secretary of the Russian Security Council, visited Seoul and then Tokyo, where he held talks with his Japanese counterpart



**Prime Minister Abe and President Putin, together with cabinet members from both governments, hold talks at the Eastern Economic Forum on September 7, 2017 (President of Russia)**

Shotaro Yachi (Secretary General of National Security Secretariat), as well as with Prime Minister Abe.<sup>35)</sup> The most notable instance of Japan-Russia exchange activity in the defense field was the visit to Vladivostok paid by the Japanese escort destroyer Hamagiri on November 20-25, where it took part in a joint search-and-rescue drill.<sup>36)</sup> This was followed by a visit to Japan by Valery Gerasimov, Chief of the Russian General Staff, a visit that had been postponed from March 2014. On December 11 Gerasimov met with Katsutoshi Kawano, the Chief of Staff, Joint Staff, as well as with Minister of Defense Itsunori Onodera, and stressed the importance of Russia-Japan cooperation in the defense sphere.<sup>37)</sup> The Russians' main motive for strengthening ties with Japan is the hope of obtaining economic cooperation that would help in the development of the Russian Far East, but it is also thought that they are planning further development of the overall bilateral relationship whose effects will go beyond that limited aim.

## **2. Short-Term Response to Increasingly Uncertain Economic Environment, and Measures to be Taken over the Longer Term**

### **(1) Russian Economy Showing Gradual Recovery**

The Russian economy began recovering slowly from the latter half of 2016, with this trend continuing throughout 2017, for an annual growth rate of 1.5 percent. The economy thus finally showed signs of emerging from the stagnancy it has been suffering since 2014. Particularly notable was that the government succeeded in keeping the inflation rate for 2017 down to its target of 4 percent. The wage increase rate exceeded 4 percent, and real disposable income was also up slightly. As a result, the feared increase in domestic criticism of the Putin administration's economic policies failed to occur.

However, a close look at the results of an opinion poll conducted in November 2017 reveals an interesting development. That is, while public approval for Putin as president exceeded 80 percent, public approval of the federal government's performance was under 50 percent.<sup>38)</sup> Moreover, in April of 2017 public approval of the Putin administration's achievement was highest in the areas of national security and foreign relations—where the administration was seen to have improved Russia's international standing and made progress in updating the armed forces—and very few respondents believed the administration's

achievements were insufficient. The second-highest approval ratings were garnered by the administration's achievements in the economic field, where economic growth and stable income levels were received positively. Even so, many respondents felt that the administration's achievements in this field were not yet good enough. Thus, support for and criticism of the administration's handling of the economy were roughly balanced. In addition, the poll showed that the Russian public's greatest concern about the future was focused on possible rises in the price of goods and consequent worsening of poverty levels, as well as fears of unemployment.

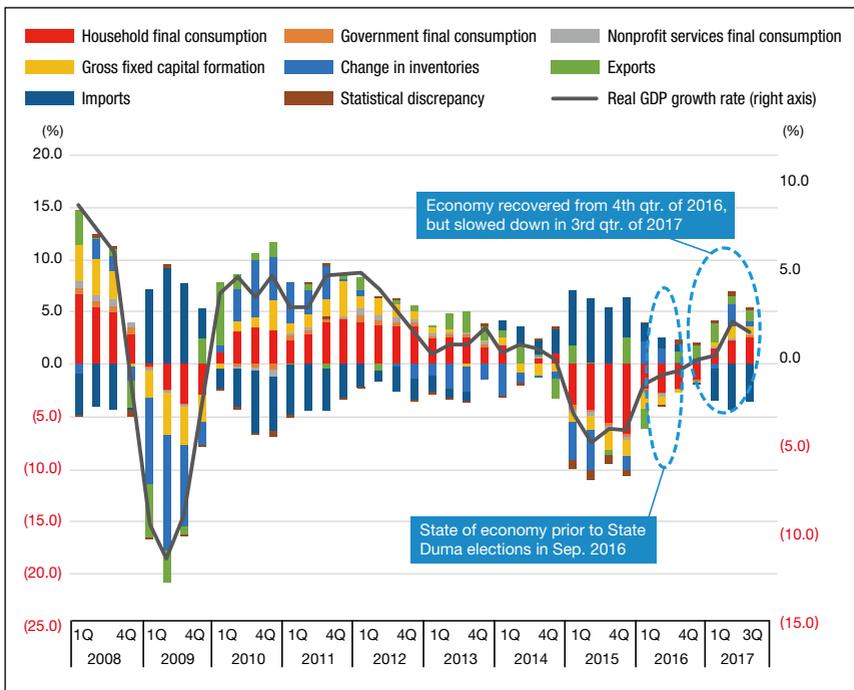
From these poll results, we can see that while the public are appreciative of Putin's leadership, they are also highly critical of the government's economic policies, and that what they are seeking is not merely relief from the current difficult economic circumstances, but also economic measures that will give some degree of guarantee that daily life will become easier in the future. In other words, the most critical issue for Putin in operating stable governance of Russia is to put the country's economy—which is currently amid a recovery trend—on the track of sustainable growth. The Russian central bank, too, in designing its monetary policy for the 2018-2020 period, assumes that the economy has recovered. While maintaining the economic stabilization policy it has been following, the bank has stated that the government's top-priority tasks are to ensure the conditions necessary for sustainable economic growth and to create new incentives.<sup>39)</sup>

The question is whether sustainable economic growth is possible under the economic policies currently being implemented. An overview of the Russian economy's recovery would suggest that the major background factor is the gradual recovery of the global economy, thanks to which the volume of world trade is increasing and global oil prices are stable, enabling Russia's exports to drive overall economic growth. Exports have been buoyed up by the introduction of the floating exchange rate system in November 2014, and the resultant decline in the exchange rate of the ruble has improved Russia's terms of trade. Meanwhile, consumer spending, which had previously been recording a sharp slump, bottomed out, with private consumption focusing on domestically manufactured goods. The production volume of such goods had been increased as part of the government's import substitution policy in response to the economic sanctions imposed on Russia by the United States and the EU.<sup>40)</sup> Consumer spending levels were able to

rise because the central bank succeeded in holding down inflation rates through a high-interest rate policy. This led to a slight increase in real disposable income (including pensions).<sup>41)</sup>

In addition, the amount of debt repayment made by Russian corporations fell sharply as a result of their reduced ability to raise funds in international financial markets due to the economic sanctions imposed on Russia. This led, paradoxically, to a reduced capital outflow, and thus the country’s balance of payments has been comparatively stable. In combination with the measures to maintain high interest rates, which helped keep the ruble stable, this was a major factor. Additionally, price rises for domestic agricultural products, whose production volume increased thanks to the import substitution program, were held down, partly thanks to good summer weather in both 2016 and 2017. As a result, crop yields were favorable

**Figure 5.1. Russian quarterly GDP growth rates yr-on-yr (breakdown by contribution ratios of principal factors)**



Sources: Compiled from information obtained from the Russian Federal State Statistics Service

and food prices remained stable.

In this way, whereas the economies of energy-exporting countries have been stagnating since 2014 due to the fall in prices on the global oil market, Russia's economy has staged a more rapid recovery than those of the other energy-exporting countries, and it can be argued that one of the reasons for this success has been the sanctions imposed on the country and the Russians' response to those sanctions.<sup>42)</sup> During this period, Russia's central bank bought dollars to build up the foreign currency reserves. The central bank also revoked the banking licenses of banks that held large amounts of bad debts, and took other steps to consolidate domestic financial institutions and strengthen the banking sector. In the background to this is the fact that the federal government debt in 2016 exceeded the initial forecasts, whereas the inflation rate improved rapidly. Moreover, amid a global economic recovery, the United States took a cautious stance on raising interest rates, and as a result, investors willing to hold high-risk investments did not withdraw their capital from emerging markets such as Russia.

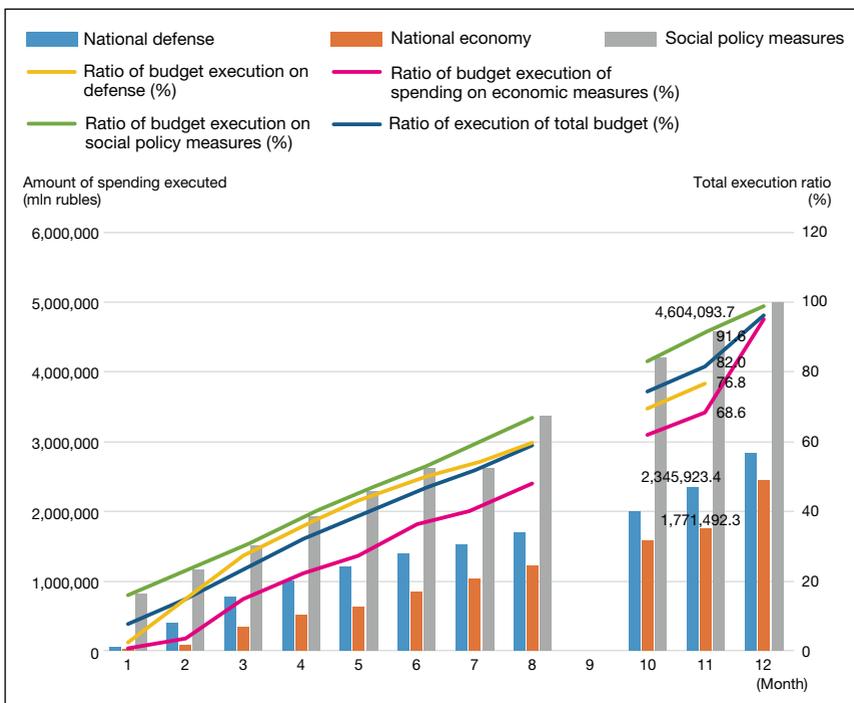
Even so, the Russian economy's recovery cannot really be described as firm. At one point in the spring, the global economy's recovery stalled and crude oil prices slumped.<sup>43)</sup> As a result, the weakness of the Russian economy's underpinnings, and its vulnerability to uncertain external factors, became apparent in a number of ways, including a drop in consumer spending. In the summer, the pace of recovery of the global economy once again picked up, and it was hoped that the Russian economy would also regain its vigor, but in fact, consumer spending was limited almost entirely to food and other daily necessities, whereas sales of large durable items such as homes and automobiles were sluggish. This was due to a weak trend in home mortgages and consumer loans against the backdrop of a leveling out of the expected inflation rate.<sup>44)</sup> Looking at the supply side, under the government's import substitution program, from the latter half of 2016 domestic production volumes expanded in agricultural products and machinery manufacturing. However, rather than benefiting from large-scale capital investment, this was largely limited to the production of components,<sup>45)</sup> and with the slowdown of production under the import substitution program in the second half of 2017, the economy's growth also slowed down.<sup>46)</sup>

The Russian government has been under pressure to deal with the recent weaknesses of the country's economy, as described above, and with the uncertainties of the global economy—notably fluctuations in global oil prices.

The Ministry of Economic Development, in particular, has been pushing ahead with prioritized budget allocations to sectors that are deemed vital to sustainable social and economic development, under the government’s priority programs and projects. The Bank of Russia, too, has been promoting investments within the country through a policy of cautiously lowering interest rates while keeping a close eye on a possible hike in the price of goods, against the background of an inflation rate that has been stable at around 4 percent. However, the government has been unable to put forward a bold economic policy adhering to fiscal discipline, whereby it would not follow the pattern seen hitherto—of expanding expenditure when international oil prices rise. Such a policy would enable Russia to be prepared for worst-case scenarios in global oil prices, which are volatile.

In view of these factors, even though the Russian economy in 2017 finally

**Figure 5.2. Execution of federal budget**



Sources: Compiled from information obtained from the Russian Ministry of Finance (figures for September unavailable).

achieved positive growth, if the administration merely maintains the current policies it will be unlikely to realize the sort of sustainable economic development that the Russian public is hoping for in 2018 and thereafter. That being said, there is naturally a limit to the effectiveness of the sort of measures resorted to in 2016 at the time of the elections to the State Duma, when the administration sought to whip up a feeling impending crisis in order to obtain increased public support. In view of this, the administration cannot hope for political stability unless it leads the economy along a steady growth track.

## **(2) Economic Policies with an Eye on the Post-Presidential Election Period**

The Russian economy faces structural problems. Firstly, while the increase in real disposal income has led to the recovery of consumer spending, thanks to the fact that the inflation rate has been held down, the majority of salaried earners are public sector workers—civil servants or employees of state-run enterprises<sup>47</sup>—and a high percentage of wage-earners work for companies that are dependent on government procurement. Thus, when this outlay is added to pension payouts, it is clear that government expenditure serves to prop up wage levels. Moreover, the domestic manufacturing sector, which is on a recovery trend, is being underpinned by the government's import substitution policy, and the international competitiveness of products supplied by Russian industry is weak. That is to say, government expenditure is driving the economic recovery, but the government's revenues continue to depend on energy exports, and the size of these revenues will vary greatly, following movements in global crude oil prices. Amid this situation, it will be difficult to increase wage levels, and the administration will have to continue putting its faith in measures to keep commodity prices stable through the maintenance of the current high interest rate policy.

The next factor that should be noted is that the economic sanctions imposed on Russia affect a very wide area of Russian society. Specifically, the sanctions imposed on the major banks have weakened the banks' funding ability. As a result, domestic companies—particularly small and medium-sized enterprises—are receiving insufficient amounts of investments or bank loans. Consequently, investment in the technology needed to raise companies' international competitiveness is sluggish. On top of this, the sanctions are limiting Russian companies' access to foreign capital, particularly from Europe and the United

States, in the form both of direct investment and technology licensing agreements. Thus, a vicious cycle has been set in motion, whereby companies that suffer from inferior international competitiveness have access only to the relatively small domestic market, and their growth prospects are thereby further limited. Additionally, companies in the energy industry, which is Russia's leading industrial sector, need both to improve productivity and to develop new resources, but there are not enough funds available, nor do they have access to the required technologies. Finally, against the backdrop of a high expected inflation rate, consumers' propensity to save remains low, and with the interest rate on loans set at a high level, few people are taking out bank loans, and thus the banking sector's fundamentals remain weak.

The number of people in Russia's labor force is following a long-term declining trend, and thus, to be able to realize sustainable economic development and assure the population of a stable standard of living, it is desirable to supply internationally competitive goods—based on high productivity—to both the domestic and overseas markets.<sup>48)</sup> The problem is that this will require technological innovation, which, in turn, will need funding and the introduction of new technologies. Additionally, any attempt to switch the focus of Russia's industrial activities from the energy sector to non-energy sectors would be fraught with risk. If we take the two factors of continued economic sanctions against Russia and an uncertain and volatile external environment as given, one feasible direction that the government could take to solve these problems is not to invest in fields which currently are inferior in international competitiveness, but to focus investment—both of funds and of technologies—on fields that are already internationally competitive and that can be expected to have a knock-on effect on other industrial sectors. This would help these sectors to lead the development of the economy as a whole, but it would require the procurement of funds and technologies from countries other than Russia's traditional source, i.e. Europe. These new source-nations could then be cultivated as export markets for Russian products.

In this light, a reexamination of the economic, fiscal, and monetary policies proposed by the Putin administration during 2017 reveal that it is precisely this direction that has been under consideration. Firstly, regarding economic policy, the Scientific and Technological Development Strategy that was drawn up in December 2016 called for the promotion of innovation, but this did not refer to the sort of revolutionary technology that might transform the whole face of

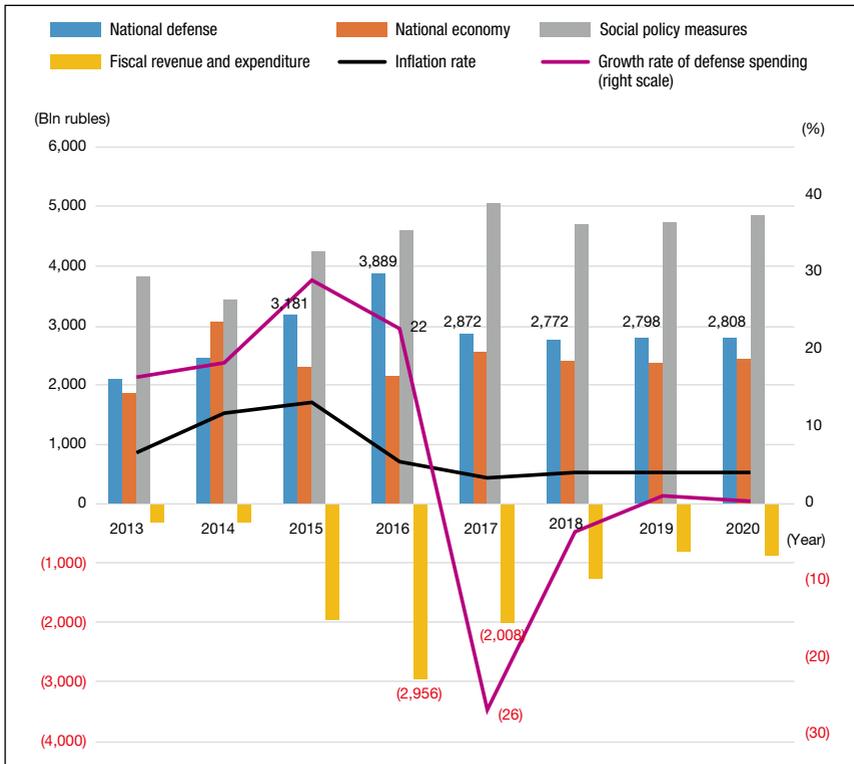
Russian society and its economy. Rather, it referred to the development or importation from overseas of technologies that could raise the level of productivity of Russian industry—which has long suffered from inefficiency, and has lost its competitiveness in the international market—to the point where it becomes internationally competitive. The Strategy specified the energy sector and national defense industries as innovation focal points.<sup>49)</sup>

Next, regarding fiscal policy, if we take a close look at the government's budget allocation bill, a reshuffling of budgetary allocations can be seen. While the spending appropriations for such items as the science and technology development program, the economic development and innovation economy program, and the industrial productivity improvement program were increased sharply, allocations for certain programs that had hitherto been emphasized—the telecommunications and electronics industry program, the pharmaceutical and medical industries program, the aerospace program, and the Far East & Maritime Province (Primorsky Krai) Development Program and others—were left unchanged or even decreased.

Additionally, on July 29, 2017, the federal budget revision law was passed, under which budgets from 2019 will be compiled and enforced under a new system of fiscal discipline.<sup>50)</sup> The principal point to note regarding this legislation is that it prevents the government from implementing expenditure that exceeds the total amount of revenue estimated from oil and gas sales (calculated on the basis of the benchmark global crude oil price as well as the forecast exchange rate, among other factors) plus revenue from other sources.<sup>51)</sup> In this case, the price of the Urals reference oil has been set at the 2017 level of \$40 per barrel, with an index-linked per annum rise of two percent in 2018 and beyond. The purpose of this introduction of a new level of fiscal discipline is to firmly maintain the benchmark crude oil price forecasting mechanism, which has a conservative tendency. By so doing, it is hoped, the authorities will be able to implement budget spending without being greatly influenced by external factors.<sup>52)</sup>

Regarding monetary policy, the prime focus is on ensuring stability in both the price of goods and the monetary system. The government hopes to maintain a good balance between consumption behavior and investment behavior through cautious manipulation of interest rates based on a specific inflation rate target. At the same time, the authorities intend to continue consolidating the banking sector through appropriate testing of each bank's competence, and thereby to strengthen the banks' lending performance. On this basis, before the drafting of the three-

**Figure 5.3. Russian federal three-year budget movements**



Sources: Compiled from information obtained from the Russian Ministry of Finance and the State Duma.

year federal budget for 2018-2020, the central bank issued a cautious forecast for the growth rate of real GDP during that period, at between 1.5 and 2.0 percent per annum.<sup>53)</sup>

At the end of August 2017, the Ministry of Economic Development revised its forecast for the economy’s growth to 2 percent or over, an upward revision from the 1.5 percent forecast it had issued in April.<sup>54)</sup> The government then drew up the budget bill on the basis of this forecast, and submitted it to the Federal Assembly on September 29. In this budget bill, on the assumption that fiscal policy and monetary policy measures would be implemented in a comprehensive and integrated manner, the GDP growth estimates were set somewhat optimistically at 2.1 percent for 2018, at 2.2 percent for 2019, and at 2.3 percent for 2020.<sup>55)</sup> This

budget bill submitted by the government features an upward revision of the GDP growth rate forecast compared to the budget bill announced by the Ministry of Finance in July, and in line with this, the total expenditure figure also rose slightly.<sup>56)</sup> However, in accordance with the newly introduced fiscal discipline standards, the scale of total expenditure was strictly limited, and even spending on national defense for 2018 was cut by 3.4 percent from the previous year, at 2,777.2 billion rubles, while the budget figure for 2019 was held down to a very slight increase, at 2,798.5 billion rubles. Behind these budget decisions can be seen the belief that the government's success in managing the economy and the country's finances over the next three years will be a crucial factor in determining the future of the next administration.<sup>57)</sup> The government's budget bill was passed by the Federal Assembly in late November and signed into law by President Putin on December 5.<sup>58)</sup>

Amid these across-the-board restraints on spending, not excluding national defense expenditure, the Russian military-industrial complex has been positioned (in the National Security Strategy unveiled in December 2015) as the driving force of innovation-led economic growth,<sup>59)</sup> and in line with the State Program for the Development of the Military-Industrial Complex, announced May 2016, the authorities have been making continuous efforts to upgrade innovation capacity in both the military and civil fields through greater efficiency in procurement as well as the production of high-tech consumer products.<sup>60)</sup> Moreover, while few details about the developmental direction to be taken by the military-industrial complex were given in the new State Armament Program, which was the focus of considerable attention, at the annual expanded meeting of Defense Ministry officials held in December 2017, President Putin made it clear that the State Armament Program would be implemented from 2018 as scheduled.<sup>61)</sup>

### **(3) Russia's Carefully Developed Overseas Energy Policy**

The Russian government is following a policy of economic diversification that centers on rescuing the economy from its excessive dependence on energy exports—which are highly sensitive to external factors—but the energy sector seems likely to remain as important as ever in the near future. For example, the government has compiled budgets that envisage a very gradual tailing-off in the percentage of total federal revenue accounted for by oil and gas, from 39.4 percent in 2017 to 35.9 percent in 2018, 33.7 percent in 2019, and 33.4 percent in 2020.

To make this possible, production by other domestic sectors such as agriculture and manufacturing will have to grow, and thus these sectors must be supplied with comparatively inexpensive energy to help them become internationally competitive. In other words, to diversify its industry and realize sustainable growth, Russia must continue investing in the exploration and development of new oil and gas resources, must maintain export levels, and must supply energy to the domestic market at affordably low prices.

The problem with this plan is the long-term sluggishness of global crude oil prices since 2014. This not only negatively impacts Russia's revenues from oil exports, but also has a major adverse effect on natural gas export prices, which are based on long-term contracts pegged to oil prices.<sup>62)</sup> For this reason, Russia has up to now placed strong emphasis on cooperation with OPEC, which is able to influence the direction of overall crude oil prices, and these efforts toward cooperation bore considerable fruit in 2017, when Russia made great progress in further strengthening its ties with the OPEC member countries, particularly Saudi Arabia.

At a meeting of the OPEC Conference held on November 30, 2016, the thirteen members agreed to institute a concerted production cut—which had been considered unlikely up to then—of 1.2 million barrels of crude per day for six months starting in January 2017. In response to this, Russia promised to reduce production by 300,000 barrels per day, on condition that the OPEC countries abided by their own production cut commitment.<sup>63)</sup> As the representative of the non-OPEC oil-producing countries, Russia adjusted cleverly to the OPEC production cut decision. On October 24, 2016, OPEC Secretary General Mohammed Barkindo and Russian Minister of Energy Alexander Novak held a meeting as part of the OPEC-Russia Energy Dialogue. They agreed to promote further cooperation between OPEC and non-OPEC oil-producing countries, and on October 29 representatives of non-OPEC nations attended a high-level OPEC committee meeting, and announced that they were ready to cooperate with the organization. At the OPEC Conference held following these preparatory moves, agreement was reached on reducing oil production, and at the same time a high-level monitoring committee was set up to monitor compliance with the terms of the agreement. In addition, agreement was reached on the institutionalization of a cooperative framework with non-OPEC oil producers. Following this, on December 10 a ministerial meeting of representatives from the OPEC and non-

OPEC countries was held, at which the non-OPEC oil-producing countries voluntarily vowed to cooperate in the production cuts initiative. At this meeting, the Joint OPEC/Non-OPEC Ministerial Monitoring Committee (JMMC) was established, with members from Russia and Oman representing the non-OPEC side. It was agreed that the meetings of this committee would be chaired, alternately, by Kuwait from OPEC and Russia from the non-OPEC side.

The JMMC consists of five representatives, three from OPEC and two (Russia and Oman) from the non-OPEC oil-producing countries. The committee is charged with analyzing the data available and evaluating the degree of compliance with the production cut agreement by both OPEC members and non-OPEC countries. The committee's evaluations will be taken into account in decisions by OPEC's board of directors and the OPEC Conference. By holding the chair of the JMMC, Russia will gain access to information on OPEC members as well as becoming involved in OPEC's decision-making process. In addition, because Saudi Arabia was the chair-nation of the 2017 OPEC Conference, Energy Minister Alexander Novak was able to liaise closely with Khalid bin Abdulaziz Al-Faleh, Saudi Minister of Energy, Industry and Mineral Resources, who acted as chairman of the conference. In effect, this constituted a cooperative framework consisting of the world's two leading oil-producing countries—Saudi Arabia and Russia.

The focus of the JMMC's work was on analysis and evaluation of data to help determine whether or not OPEC should extend the period of implementation of the concerted production cuts when the first period ended, and the first opportunity to put this to the test came on May 25, 2017. At the JMMC meeting on the previous day, it had been decided that the joint reductions should be extended for nine months to the end of March 2018,<sup>64</sup> and the OPEC Conference adopted this suggestion and duly passed the extension period.<sup>65</sup> At the ministerial meeting of representatives from the OPEC and non-OPEC countries held the same day, the cooperative relationship was confirmed, and in line with this, the non-OPEC countries also extended their period for production cuts to the end of March 2018.<sup>66</sup>

Thereafter, too, the JMMC continued to operate as a forum where the OPEC and non-OPEC countries could share data on oil market movements, and the conditions were made ready for the OPEC Conference to be held on November 30, 2017. During this period, Russia not only acted as the representative of the non-OPEC oil-producing countries, but, in its position as the chair of the JMMC, also took a positive role in coordinating moves among the individual OPEC



**Salman bin Abdulaziz Al Saud, King of Saudi Arabia, meets with Russian President Vladimir Putin at the Kremlin on October 5, 2017** (President of Russia)

members. These countries were facing a serious environment because of the reduction in oil production, given the various complicated political and economic factors involved, relating to Iran, Iraq, Venezuela, and others. OPEC Secretary General Mohammed Barkindo praised Russia's contributions, and went so far as to propose that the coordination framework between OPEC

members and non-OPEC countries that had been established as a temporary measure to facilitate the joint oil production cuts be made permanent.<sup>67)</sup> At the November OPEC Conference, the joint production cuts were extended to the end of 2018.<sup>68)</sup>

Meanwhile, the relationship between Saudi Arabia and Russia became still closer following the elevation to the title of Crown Prince in June 2017 of Mohammad bin Salman, who had been energetically promoting an economic reform plan. Before becoming Crown Prince, bin Salman had held meetings with Putin on a number of occasions, and after his elevation to the country's second-highest royal rank, he simultaneously held the posts of deputy prime minister and minister of defense. He thus held the reins of power with respect to both Saudi Arabia's economy and its national security, and was therefore a central figure in the bilateral relationship. At a meeting with Putin in Moscow on May 30, prior to his elevation to the rank of crown prince, Mohammad bin Salman arranged for a visit to Russia by his father, Salman bin Abdulaziz Al Saud, King of Saudi Arabia. On October 5, King Salman became the first reigning Saudi monarch ever to visit Russia.

At the summit meeting between King Salman bin Abdulaziz and Putin, proposals were discussed for expanding bilateral cooperation, including in the fields of economic and military affairs. Cooperation accords were signed on the use of space development programs, and in science and technology, and memorandums were exchanged between government ministries and agencies on more detailed aspects of the proposed cooperation. These included memorandums relating to purchases by the Saudis of Russian-manufactured military equipment

as well as the production of such equipment within Saudi Arabia. The two governments also agreed to jointly establish an energy-related investment fund and a high-tech-related investment fund, both with an initial funding of one billion dollars.<sup>69)</sup>

Meanwhile, Saudi Arabia, which is seeking to strengthen its ties with Russia, is believed to be similarly aiming to remedy its economy's overreliance on energy exports, to which end it is proceeding with economic reforms initiated by Crown Prince Mohammad bin Salman in 2016, centering on the construction of high-tech cities. The country aims to use the income generated from the listing of the stock of Saudi Aramco to provide the funds required for these reforms, and it needs to raise global crude oil prices—which hold the key to Saudi Aramco's asset value—to the required level. Saudi Arabia is also thought to need the cooperation of other countries in securing advanced technology.<sup>70)</sup> Additionally, some observers believe that the country is seeking to move away from its traditional rigidly patterned foreign policy to a more flexible one,<sup>71)</sup> to enable a more effective response to current global conditions.

Russia also took steps during 2017 to strengthen its cooperation with Iran. On November 1, Putin paid a visit to the Iranian Supreme Leader, Grand Ayatollah Ali Hosseini Khamenei. Putin subsequently met separately with Iranian President Hassan Rouhani and Azerbaijani President Ilham Aliyev and also held a summit meeting with both these leaders.<sup>72)</sup> At these meetings, it was confirmed that the cooperation agreements between the OPEC and non-OPEC nations were bearing fruit, and the leaders discussed the idea of a similar agreement among gas-producing countries. Subsequently, in December, a memorandum was signed and exchanged between Russia's Gazprom and the Iranian oil ministry concerning the development of Iran's gas resources and the construction of a pipeline from Iran to India via Pakistan.<sup>73)</sup>

Russia has also been carefully pursuing its energy strategy in Asia. A representative example is the purchase in August by the largely government-owned Russian oil company Rosneft of a 49 percent stake in the Indian oil company Essar Oil.<sup>74)</sup> This acquisition is a first step toward entering the Indo-Pacific petrochemical products market, which has been posting remarkably strong growth. Moreover, crude oil produced by the Venezuelan state-owned oil company PDVSA, in which Rosneft has an equity stake, is already being imported into India.

With respect to China, in January Rosneft signed a new long-term supply

contract with the government-owned oil and gas company China National Petroleum Corporation (CNPC).<sup>75)</sup> In July, Rosneft signed a strategic cooperation agreement with the Chinese energy conglomerate CEFC China Energy (CEFC),<sup>76)</sup> and in September the scope of this agreement was expanded and a crude oil supply agreement was signed.<sup>77)</sup>

Meanwhile, in September agreement was reached whereby CEFC would become a shareholder in Rosneft after acquiring a 14.16 percent equity stake in Rosneft, which it will purchase from the consortium of Glencore plc (a Swiss-based commodity trading and mining company) and the Qatar Investment Authority, which holds a 19.5 percent share in Rosneft.<sup>78)</sup> As a result of this, Rosneft will acquire an opportunity to enter the fast-growing Chinese downstream market, while the Chinese side will be able to participate in Russia's upstream energy sector. In this way, ties between the Chinese and Russian energy sectors will be reinforced through strong capital ties. In fact, Russia's VTB Bank has indicated its willingness to loan CEFC a portion of the funds required to purchase the Rosneft shares.<sup>79)</sup> These moves by Russia, aimed at strengthening ties with India and China, have been described as having geopolitical aims.<sup>80)</sup>

In the field of natural gas, apart from the signing in April of a long-term loan agreement between Gazprom (which would play the central role in the proposed Nord Stream 2 pipeline to Europe) and major West European energy companies, there have been no particular developments.<sup>81)</sup> In the background to this is believed to be the fact that demand prospects for Russian natural gas have worsened, apart from in the European market.<sup>82)</sup> In contrast to Russia's vigorous moves in the oil market, the country appears to have made no new initiatives in the natural gas field, in light of poor demand prospects.

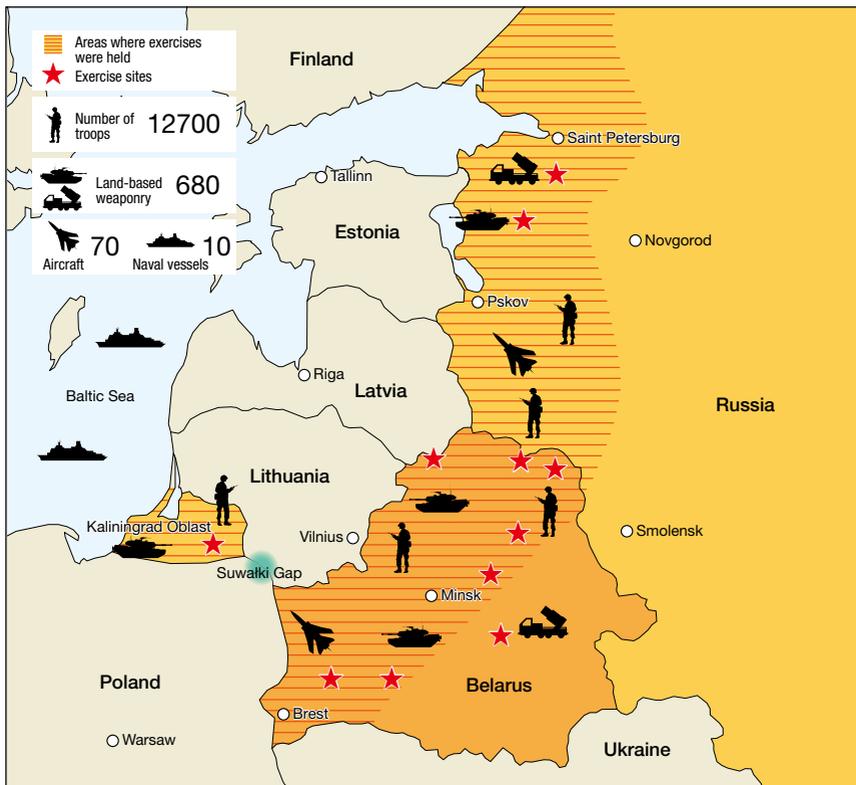
Meanwhile, in the field of natural gas projects, particularly distinctive was the large number of agreements that were concluded by Gazprom in October with domestic high-tech companies and research institutes relating to the development and supply of innovative technologies, centered on import substitution technologies.<sup>83)</sup> This can be looked at as a way of building up industry-academia collaboration that can make possible future exploration for natural resources and their development without the need for reliance on foreign technology, which is largely being denied to Russia by the West's economic sanctions. This aligns with the measures prescribed to create the Stage 1 (2017-2019) mechanism under Russia's Science and Technology Strategy.

### 3. Military Activities and Measures to Build Up Russia's Military Capabilities

#### (1) Russia Displays Military Presence in Europe and the Middle East

To summarize the Russian armed forces' combat exercises, each year the various military districts take it in turns to host exercises for strategic leadership staff, and in the period September 14-20, 2017, the Zapad 2017 exercise was held—primarily in the territory of the Western Military District. As this was Russia's first military exercise on the Western front in the area of the Baltic Sea since 2013,

**Figure 5.4. Military exercises by Russian and Belarusian forces (Sep. 2017)**



Source: Compiled by the author, based on an article in the *Rossiyskaya Gazeta* (Sep. 21, 2017); figures issued by Russian Ministry of Defense.

NATO has been on high alert, and has been flying Airborne Warning and Control System (AWACS) aircraft in the area where the exercises take place. The Russian Ministry of Defense announced that the exercises—held near Saint Petersburg, in Kaliningrad Oblast, and on Belarusian territory—were aimed at combating terrorism. In 2017 they involved 7,200 Belarusian troops and 5,500 Russian troops for a total of 12,700 troops.<sup>84)</sup> The Vienna Document released by the Organization for Security and Co-operation in Europe (OSCE)—a document concerned with confidence- and security- building—mandates that a signatory state accept observers for exercises involving at least 13,000 troops. While the Russian Ministry of Defense claimed that the number of troops involved in Zapad 2017 fell short of the number required to trigger this provision, some analysts have insisted that the actual number of troops involved was well in excess of 13,000.<sup>85)</sup> On September 18, President Putin, Minister of Defense Sergey Shoigu, and other government officials observed a live firing exercise at a maneuver area in Leningrad Oblast. As a special, limited concession, the Russian authorities invited military attaches from over sixty countries to attend the exercise. On Belarusian territory, exercises were conducted close to the Suwałki Gap (near the Polish-Lithuanian border), and analysts argue that the exercises were based on a scenario in which Russian Federation troops would pass through this area on the way to Kaliningrad Oblast in the event of an emergency.<sup>86)</sup> At the same time, test-launchings of the RS-24 Yars intercontinental ballistic missile were also conducted.<sup>87)</sup>

In the Military Reform Plan on which Russia embarked in October 2008, the country's ground forces were, in principle, to be reorganized, with the brigade as the basic unit. Later, however, in the western part of Russia, brigades were reorganized into divisions, among other changes. This indicates a trial-and-error approach to military reorganization.<sup>88)</sup> The Russians also took various steps to upgrade their military capabilities, as instanced by the holding of exercises involving two-hundred and fifty T-72 tanks in October 2017 in the Chelyabinsk area.<sup>89)</sup> Defenses have been bolstered along Russia's borders with the deployment at important military bases of S-400 surface-to-air missile systems as well as land-to-ship missiles such as the Bal and the Bastion. According to the report "Russian Military Power," published by the US Department of Defense in 2017, Russia is building an anti-access/area denial (A2/AD) capability, including through the use of the above-described missile systems.<sup>90)</sup> As part of this kind of

border defense system, in the Arctic and the Sea of Okhotsk region, too, the Russians are building new bases to augment their military capabilities. The Arctic region is one of the areas where the Russian military are working to strengthen their operational capabilities, which are seen as insufficient because of the severity of the natural environment there. At the parade held in May on the anniversary of victory over Nazi-Germany, specially designed Arctic versions of the Tor and Pantsir surface-to-air missile systems were unveiled as a way of displaying the country's Arctic-theater military capabilities to both the Russian public and foreign representatives.

While Russia is not making any moves to resolve the confrontation with NATO, it is trying to make it less likely that an unforeseen contingency will occur. At Baku in Azerbaijan, Chief of the Russian General Staff Valery Gerasimov held talks in March and September with General Petr Pavel, the Chairman of the NATO Military Committee, which served to improve communications between the two military organizations.<sup>91)</sup> In July, in line with the Prevention of Incidents On and Over the High Seas Agreement (INCSEA) signed between the United States and the Soviet Union in 1972, the regularly scheduled annual meeting was held at Newport in the United States. Although this meeting was not held in 2014, it has been held every year since 2015, which demonstrates the two sides' commitment to crisis management.

In Syria, Russia continues to conduct military operations in support of the regime of President Bashar al-Assad, and this theater of operations has afforded the Russian military considerable valuable experience. The aircraft carrier the *Admiral Kuznetsov* was in operation on the high seas from October 2016 to February 2017, conducting carrier-based aircraft drills in the eastern Mediterranean before launching attacks on positions held by enemy forces in Syria, during which a fighter plane crashed into the sea. In January 2017, while off the coast of Libya, the carrier was visited by Field Marshal Khalifa Haftar, leader of the Libyan National Army, who held a video conference with defense minister Shoygu. Some observers believe that Russia plans to use its influence to help solve the problem of the current Libyan political strife and disunity.<sup>92)</sup>

In Syria, thanks to the support provided by Russia in addition to Iran and Hezbollah, following the fall of Aleppo in December 2016 the Assad regime has further expanded the area of the country under its control, and in November 2017 it took complete control of Deir ez-Zor and went on to retake Abu Kamal (located

on the border with Iraq) from the Islamic State of Iraq and the Levant (ISIL). Abu Kamal was ISIL's last significant stronghold. The support rendered by Russia to the Assad regime has been primarily in the form of air support, but it has also dispatched military advisors. In June, the *Admiral Grigorovich* and the *Admiral Essen*—two of the latest class of frigates—and the Kilo-class submarine *Krasnodar* launched Kalibr cruise missiles from the Mediterranean at ISIL targets within Syria on several occasions, according to the Russian announcement.<sup>93)</sup> In this way, the Russian Navy was able to obtain valuable operational experience with new precision-guided weapons systems, thereby raising its operational readiness in other military theaters.

Russia's influence on the military situation in Syria has the side-effect of enhancing the country's diplomatic presence across the whole of the Middle East. Since January 2017 Russia has held a series of conferences in Kazakhstan on the issue of peace in Syria, with the cooperation of Iran and Turkey. Having satisfied himself that Russia had achieved its military objectives, President Putin on December 11 visited Khmeimim Air Base in Syria and announced that the principal Russian military units in Syria would be pulled out, but that the bases at Tartus and Khmeimim would remain in operation.<sup>94)</sup> As the Syrian situation had transitioned from the military operation stage to the stabilization stage, a number of Russian experts have opined that Moscow will now have to seek foreign policy cooperation with a wider range of regional partners.<sup>95)</sup>

## **(2) Developments in Russia's Military Capabilities in East Asia and the Arctic Region**

Russia's current concept for military-use construction in its Far East region was established in 2015 in the form of a plan for the construction of coastal defenses. Under this plan, defense capabilities would be improved along a line stretching north from the Kuril Islands—which consist of what Japan regards as the Chishima Islands and the Northern Territories (the disputed two islands and two islets)—through the Kamchatka Peninsula and into the region of the Bering Sea and the Arctic Ocean surrounding the Bering Strait.<sup>96)</sup> The main purpose of this is to protect the Sea of Okhotsk, which is used by Russian ballistic missile submarines. In November 2016 the Russian military transported Bal and Bastion land-to-ship missiles to the islands of Kunashiri and Etorofu (known as Kunashir and Iturup in Russian), which are part of the disputed territories, and in February 2017 Defense

Minister Shoygu announced the formation of a division covering the Kuril Islands. In response to this, at the Japan-Russia “2+2 meeting” of foreign and defense ministers held in Tokyo in March 2017, Japan’s Defense Minister Tomomi Inada and Foreign Minister Fumio Kishida decried this move, stating that the deployment of missiles was irreconcilable with Japan’s position on the Northern Territories. They also stated Japan’s concern about reports on the deployment of a new Russian Army division on the island chain, and made it clear that this was unacceptable to Japan if it involved the four islands of the Northern Territories.<sup>97)</sup>

At an August 18 meeting of the Defense Ministry Board, Minister Shoygu stated that the process of reorganization of military units would be optimized by December, and that further progress would be made in equipment upgrading.<sup>98)</sup> The Russian military leadership are examining options for the building of a new base for the Pacific Fleet, and in both 2016 and the summer of 2017, the ministry of defense and the Russian Geographical Society conducted an examination of the island of Matua in the central Kuril Islands. The islands of Paramushir and Rasshua have also been surveyed. In November 2017, *Izvestia* reported that the Russian military intended to station Bal and Bastion surface-to-ship missiles on Matua and Paramushir.<sup>99)</sup> Analysts have pointed out the difficulty of the natural environment on these islands if they were to be thus employed, as well as the investment in infrastructure that would be required,<sup>100)</sup> but in any event, the Russians are thought to be examining and planning options for the deployment of troops and the construction of bases as part of their coastal defenses.<sup>101)</sup>

As part of recent equipment upgrading, two Borei-class nuclear-powered submarines have been deployed on the Kamchatka Peninsula, and the above coastal defense capability is thought to be mainly to ensure the ability of these submarines to operate in the Sea of Okhotsk. In July 2017 the new-class corvette *Sovershennyi* was commissioned at Vladivostok and was equipped with SS-N-25 antiship cruise missiles (similar to the Bal surface-to-ship missiles). Already, in April of 2017, antisubmarine war games were conducted using the Tu-142M3 patrol aircraft.<sup>102)</sup> Then, in August further antisubmarine exercises were conducted in the vicinity of the Kamchatka Peninsula.<sup>103)</sup> On August 10, military exercises involving 1,000 troops were commenced on the islands of Etorofu and Kunashiri,<sup>104)</sup> and on the 29th, exercises were conducted on various islands of the Kuril chain under the scenario of repelling an attack from the sea, involving 2,500 troops.<sup>105)</sup>

Russian aircraft have continued to conduct patrols in the region around Japan,

forcing fighters of the Japan Air Self-Defense Force to scramble in response to Russian planes a total of 398 times during 2017.<sup>106)</sup> Russian military moves in response to United States forces in the Pacific region have also been noted. A Russian military aircraft approached Anchorage on four successive days in April,<sup>107)</sup> and in May the US aircraft carrier the USS *Ronald Reagan* was approached by a Russian patrol plane off the Korean Peninsula.<sup>108)</sup> While no major incident has resulted from these approaches, the Russian military continues working to enhance its capabilities in this marginal area of the Pacific Ocean, including equipment upgrading, reorganization of military units, and maneuvers.

### **(3) Contribution to Russia's Diplomacy of Joint Military Exercises and Weapons Exports**

The Russian government is using joint military exercises and the export of weaponry to enhance its foreign policy initiatives. The Zapad 2017 exercise described above doubled as the “Shield of the Alliance 2017” joint exercise with Belarusian troops.<sup>109)</sup> The joint military exercise of the Collective Security Treaty Organization (CSTO)—made up of Armenia, Kazakhstan, Kyrgyzstan, Tajikistan, Belarus, and Russia—was held from October 3 to November 20, with the participation of troops from Russia, Armenia, Kazakhstan, and Tajikistan. A joint military exercise predicated on resistance to the activities of ISIL in Central Asia by the Commonwealth of Independent States (CIS) was held from May 23 to June 1 in Tajikistan (which hosts Russian military bases), with the participation of Russia, Belarus, Armenia, Kazakhstan, Kyrgyzstan, and Tajikistan.

In 2017 Russia and China once again conducted the Maritime Cooperation joint naval exercise for the sixth straight year. As was the case in 2015, in addition to East Asia, part of the exercise was conducted in European waters. In the July 21-28 period, the Russian and Chinese navies engaged in defense drills against submarines, surface warships, and aircraft in the neighborhoods of Saint Petersburg and Kaliningrad. In East Asian waters, Maritime Cooperation exercises were held in the September 18-25 period, starting from Vladivostok. Taking part were the Russian destroyer *Admiral Tributs* and the submarine rescue ship *Igor Belousov*, along with the Chinese missile destroyers *Shijiazhuang* and *Daqing*, and submarine rescue ships, among others.

Japan's Ministry of Defense announced that from 11 a.m. to 7 p.m. on September 24, six Russian and Chinese warships, including the missile cruiser

*Varyag*, passed through La Pérouse Strait (Soya Strait) into the Sea of Okhotsk. This group of ships did not include a Chinese submarine rescue vessel. The Russian and Chinese warships arrived in Aniva Bay,<sup>110)</sup> at the southern end of Sakhalin Island, and the closing ceremony was held at Vladivostok on September 25. It was announced that this had been the first joint drill between the two countries for submarine rescue vessels.<sup>111)</sup> During October 19-29, Russian military forces also conducted joint exercises with Indian military forces near Vladivostok as part of Indra-2017, when the two sides engaged in their first land, sea, and air drills, including a landing drill.<sup>112)</sup> Both the Sino-Russian and Indo-Russian exercises reflected close bilateral relationships, and they have afforded the military units engaged in them an opportunity to foster ties of trust and to experience different types of drills in new geographical locations. Apart from these limited achievements, however, it is not thought that they have made more high-level joint campaigns possible.

Russia is also cooperating with China in the field of weapons technology. Of the twenty-four Su-35 fighters for which China signed a purchase contract in 2015, the first four to be delivered arrived in southern China at the end of 2016, and this was followed by the delivery of ten more planes in December 2017.<sup>113)</sup> Progress has also been made in the production of S-400 surface-to-air missiles for China. A sales contract for S-400 missiles to India was also signed in 2016, and export agreements on the missiles for 2017 have been reached with Turkey and Saudi Arabia. Exports of weapons not only contribute to the profits and development of the Russian defense industry, but also help construct lasting ties with the buyer countries. Table 5.1 below shows the main exports during 2017. The Russian government is thought to be aiming to enhance its diplomatic presence through joint military exercises and cooperation in weaponry technology with a wide range of countries.

**Table 5.1. Principal developments in Russian arms exports during 2017**

Importer	Transaction
China	Ten Su-35 fighters delivered Production of S-400 surface-to-air missile systems
India	Renegotiation of joint production project for Sukhoi Fifth Generation Fighter Aircraft (FGFA)
Vietnam	Delivery of Kilo-class submarine and Gepard-class frigate
Indonesia	Negotiations on contract for Su-35 fighters
Thailand	Contract for Mi-17V-5 transport helicopters under consideration Decision made to acquire helicopters, including Mi-28 attack helicopters
Philippines	Signing of defense procurement cooperation agreement Delivery of AK-47M rifles
Turkey	Contract for purchase of S-400 surface-to-air missile systems
Iran	Preparation for joint production of Ka-226T helicopters; test flights
Syria	Delivery of PMM-2M amphibious bridging ferries
Saudi Arabia	Signing of memorandum on S-400 surface-to-air missile systems, etc.

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