

Increase in oil revenue amid unrest in Arab world gives Russia some breathing room

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With the price of oil climbing to more than \$100 a barrel, Russia has a little more weight to throw around on the world stage, and it is doing just that. The stepped-up flow of petrodollars into the government's coffers relieves what had been a worrisome budget deficit and lessens the urgency of reform. Good relations with the West - and especially the "reset" with Washington - are not quite so pressing when the economy here is in good shape.

Russia is benefiting tangibly from the turmoil in the Middle East and North Africa. Urals crude sold for \$113 this week, up from \$75 a year ago. Of that, \$76.50 goes into the Russian treasury. And the spike in oil income has compensated for growing weakness elsewhere. It arrived just as Gazprom - the natural-gas giant that until recently was a potent weapon in Russia's foreign policy - has seen its clout in Europe washing away amid a flood of competition.

An emboldened Prime Minister Vladimir Putin was in Brussels in late February angrily lecturing the Europeans on energy policy and the uprisings in the Arab world. After months in which Moscow and Washington have tried to put their differences over Georgia on a back burner, President Dmitry Medvedev two weeks ago accused the country of threatening the security of the 2014 Winter Olympics, to be held in Sochi, near the border of a breakaway region of Georgia. Earlier this year, Russia's warming relations with Poland went sour over the handling of the investigation into the plane crash that killed Poland's president and other top leaders this past spring. But with increased oil revenue also comes the danger of complacency. Bureaucrats, defense contractors, pensioners and workers in construction and finance all stand to gain from the money coming in, along with the oil companies. But the cash also feeds corruption, encourages increased financial opacity and discourages attempts to shake up the system - all of which could spell trouble for Russia down the road.

"All of the dominant groups in Russia get a share of the increased oil revenue," said Alexander Auzan, an economist and adviser to Medvedev. "Yet it contradicts their long-term interests." It's a powerful prop for the status quo - which Auzan and others say is unsustainable.

But as Sergei Guriev, head of the New Economic School in Moscow, pointed out, any change is going to involve a cost for someone, so why take the risk if the money is flowing in?

Russia is currently the world's largest oil producer. When the price last spiked, in 2007, Moscow was flooded with money and people close to Putin were suggesting that Russia was genuinely self-sufficient and had no need to engage more deeply with the West. The economic crisis the following year brought that talk to an abrupt end, and Medvedev began pushing for a Western-oriented program of modernization and diversification away from dependence on energy exports. The Kremlin moved to stimulate the economy in 2008 by increasing government salaries and hiking pensions by 35 percent. Now it is stuck with those increases. With oil revenue providing 40 percent of the Russian budget, the Gaidar Institute for Economic Policy here has calculated that at any price less than \$105 a barrel the government will be in the red.

That tempers any inclination toward hubris, said Daniel Treisman, a political scientist at UCLA who follows Russian developments. The Kremlin was looking at a difficult financial crunch, with parliamentary elections coming late this year and a presidential election next March, so the timing of this rise in revenue is more a relief than a goad to aggressive behavior.

"We don't need high prices," said Leonid Grigoriev, an economist and former World Bank adviser. "We need good relations, a long-term market and reasonable prices," which he put in the \$70-to-\$90 range.

Russia will not turn its back on the West, by any means, he said. But, especially in an election year, its leaders may be more vocal in pointing up differences with the West. In 2010, Russia had enough problems at home that it was actively trying to avoid them abroad; now, with money to address domestic issues, that caution may not be so evident.

Treisman, like many others, did not think much would ever come of Medvedev's modernization plans - it's not the sort of change, he said, that can be ordered from the top down. But the oil bulge makes the Westernization of the Russian economy less likely. It helps big companies - which, Grigoriev said, already dominate the economy to a much greater extent than in other developed countries - and it hurts small ones, where jobs and creativity tend to be nurtured.

Information technology firms, with high labor costs, will suffer, Guriev said, and they are central to Medvedev's vision for the future of Russia.

Part of what got Putin so riled up in Brussels was Europe's treatment of Gazprom, a gigantic state-owned operation that at one time had unchallenged sway in the European energy market. Gazprom was a powerful tool in the Kremlin's hands, useful when threatening Ukraine and a reminder to the rest of Europe that Russia had to be given its due.

But that was before American companies began extracting cheap natural gas from shale deposits, and before developments in liquefied natural gas (LNG) technology made inexpensive transportation by ship possible.

Qatar set up a new LNG port to ship gas to the United States, but when it couldn't compete there it turned to Europe instead. Today, Europe can buy gas cheaper from Qatar than it can get by pipeline from Russia. European companies have been renegotiating their contracts with Gazprom - downward - and the European Union has insisted that Gazprom divest itself of its pipelines. Russia will still sell gas to Europe, said Pierre Noel, an energy expert at England's University of Cambridge, "but the pricing regime is changing." Gazprom, he said, will eventually have to change with it.

But the turmoil in North Africa has temporarily masked even Gazprom's difficulties. When the Libyan gas pipeline across the Mediterranean was shut down, Italy, which is Gazprom's second-biggest customer, relented for now in trying to renegotiate its contract.

If production in Algeria, a much bigger supplier than Libya, were to be disrupted, that would make Gazprom a power to be reckoned with again.

http://www.washingtonpost.com/world/oil-revenue-gives-russia-some-breathing-room/2011/03/04/ABbbW9P_print.html

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