



DISCOVERING RUSSIA

Padma Desai

BEYOND RESENTMENT

Mykola Riabchuk

COMMERCIAL CONTACT AND
CONFLICT PREVENTION:

THE GEORGIA-ABKHAZ CASE

David L. Phillips

HARRIMAN REVIEW

Volume 18, Number 1

June 2011

Padma Desai
DISCOVERING RUSSIA 1

Mykola Riabchuk
BEYOND RESENTMENT 12

David L. Phillips
COMMERCIAL CONTACT AND
CONFLICT PREVENTION:
THE GEORGIA-ABKHAZ CASE 17

The Harriman Review
is published quarterly by the Harriman Institute, Columbia University.
Copyright © 2011 by the Trustees of Columbia University in the City of New York.
All rights reserved.

Harriman Institute
420 West 118th Street, MC 3345
Columbia University
New York, New York 10027
<http://www.harrimaninstitute.org>

THE HARRIMAN REVIEW

Harriman Institute
Columbia University
1216 International Affairs Building
420 West 118th Street
Mail Code 3345
New York, NY 10027
USA

Non-Profit Org.
U.S. Postage
PAID
New York, NY
Permit No. 3593

DISCOVERING RUSSIA

Padma Desai

How can one discover a country which is in the process of discovering itself?

My complicated journey to unravel this riddle started with a fitful adolescent resolve of wanting to read Dostoevsky in Russian. That rash impulse, however, seemed to disqualify me for the larger undertaking of understanding Russia in the view of most Russians I have known over the years. “Why Russia?” asked the young secretary of Oleg Vyugin, the former Deputy Chairman of the Central Bank of Russia, as she accompanied me in a Mercedes to the imposing office of her boss whom I interviewed for a book project in 2003. “Because of Dostoevsky,” I ventured. “But he is so disturbing,” she said, raising her voice. “That is exactly why,” I remember saying. What was the point of venturing into a scholarly endeavor devoid of challenges?

Adam Ulam, the distinguished Harvard historian of the former Soviet Union, once remarked that he chose to study the Soviet Union rather than the British Empire because he wanted to deal with an expanding scene rather than a declining one, Britain having already lost India. History can occasionally prove tricky when it comes to choosing one’s area of expertise. Both Adam and I lost the Soviet Union along the way but Russia has continued to engage me.

Having trained as an economist, I opted to study the Soviet Union by deliberately dropping India as an academic pursuit. My teenage fascination with the English translations of Russian literature had also led me to study the language from my Harvard days as a graduate student in the Economics Department in the late 1950s. Besides, Wassily Leontief’s input-output model was one of the pioneering empirical exercises of those days. I chose to apply it to Indian data by separating consumption spending from the final bill of goods and introducing it endogenously in the application. The article “A Short-Term Planning Model for the Indian Economy” was published in the *Review of Economics and Statistics* (June 1961) in what turned out to be my earliest publication in a professional journal, and I felt adequately prepared to deal with the challenges of the Soviet planned system.

I visited the Soviet Union for the first time in the summer of 1964, lived for the most part in the Indian consulate in Odessa, traveled, and gathered firsthand impressions of Soviet arrangements. In the tsarist days, Odessa was known as the “Pearl of Russia” and as “Little Paris.” During my stay under Soviet rule, it appeared morose and preoccupied as if it was in permanent

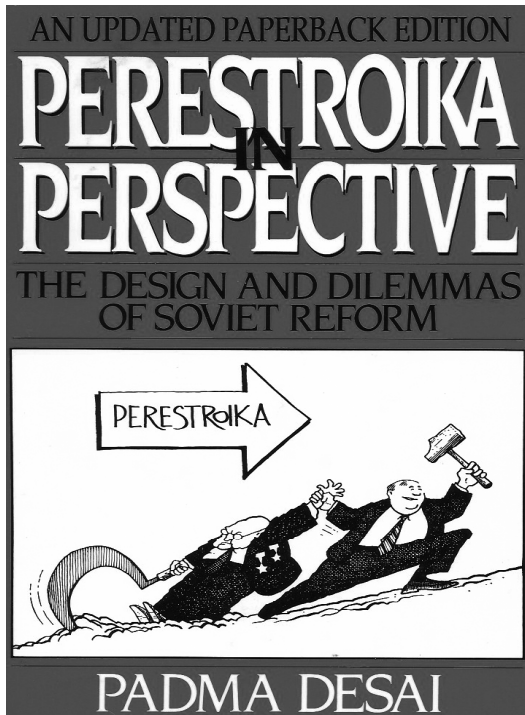
mourning. The French and Italian cafes of its cultural heyday, which I imagined Pushkin and Tolstoy had visited during their stay, had disappeared. When Mark Twain passed through Odessa in 1869, he wrote: “We saw only America. There was not one thing to remind us that we were in Russia.”

I, on the other hand, realized that I was in the Soviet Union. I remember the perennial lines in front of the stores, combined with exquisite orderliness. Beyond orderliness, I noticed pervasive fear. I also sampled from visiting Indian students to the consulate that exceptional brand of Russian humor which imparts an impeccable intellectual touch to a current event or some aspect of the country’s political reality. During my stay, Khrushchev was still the leader and Valentina Tereshkova, the first woman astronaut, happened to return from outer space. This most exciting event in early Soviet space history brought momentary jubilation on Soviet TV and creative fervor among humorists of the day. In one joke, titled Khrushchev’s Dilemma, the Soviet leader discovers that Valentina returns home pregnant. He had to either accept the Biblical notion of Immaculate Conception or the alternative that an American astronaut had encountered Valentina in outer space.

While I began my discovery of Russia with love for Russian literature and humor, I have deliberately avoided converting it into a sentimental journey. From early on, I had decided to handle Soviet and Russian policy issues rigorously and empirically by applying appropriate models to the available data and tracking the model results with the help of the fast advancing computational procedures.

Four Decades of Empirical Modeling: From the Post-War Economic Growth Retardation to the Current Financial Crisis

From the perspective of more than four decades, the problems I posed, the empirical models I adopted, and the computer packages I employed may appear primitive, but they were the exciting scholarly endeavors of the moment calling for answers. Which production function specification would accurately capture Soviet growth retardation which began from 1950? What contribution, if any, did total factor productivity make to the growth process? These inquiries, which were being sorted out for the U.S. economy, awaited the models and the empirical exercises which were applied for the very first time to the Soviet case. And I wanted to move further. Suppose the Soviet planned economy had worked according to



the rules of the American free market system, how much more productive would it have been? If the gains turned out to be significant, one could make a solid case against Stalin's adoption of the Marxist-Leninist system.

With Mikhail Gorbachev's appearance in March 1985 as Soviet leader, the changing Soviet scene created new research opportunities for me. I analyzed the design and dilemmas of his perestroika reforms even as they were unfolding in *Perestroika in Perspective* (Princeton University Press, 1989). I also sought to figure out the impact of Gorbachev's very limited liberalization policies in Soviet agriculture. Would the opportunity which he gave to collective farm households for retaining their

earnings raise farm productivity in terms of per acre grain yield? Would the new contract system, which assigned a piece of land to the farm household and linked its earnings to its contribution to the collective farm output, create incentives in Soviet agriculture? But then it would be necessary to separate the impact of weather from yield variability. That was a formidable challenge. The arable land constituted only 7.17 percent of Russia's enormous territory of 6,387,319 square miles. However, the high latitude and the extreme continentality of an eleven time zone land mass with severe winters, short growing seasons and fluctuating temperatures complicated my task of selecting a representative sample and constructing appropriate weather variables.

When Boris Yeltsin and his band of reformers, led by his young prime minister, the late Yegor Gaidar, began liberalizing prices and privatizing assets in early 1992, the process unsettled enterprise prices, costs and revenues on a massive scale. Millions of workers in privatized industry and the state sector (which failed to receive tax revenues from failing businesses) were deprived of wages and pensions from 1994 to 1998. My coauthor Todd Idson and I employed the multivariate maximum likelihood probit estimation for assessing the partial impact of specific attributes which affected the likelihood of the sample employee's experience of wage denial. Among these attributes were the respondent's residence, occupation, education, and gender. We used a substantial household data set for answering these questions.

But the Russian economy was set to revive. Under Vladimir Putin's two-term presidency from 2000 to mid-2008, it registered an annual real GDP growth of 7 percent, the result of high oil prices which hit an eye-popping \$147 a barrel in July 2008. The impressive growth did collapse toward the end of 2008 when the global financial crisis hit Russia as oil prices tumbled to \$30 a barrel. Foreign portfolio investors fled from



Russia. The ruble declined sharply. Rather than restrict my analysis to the crisis impact on the Russian economy, I began formulating a computable model with data for about 60 countries. The model will estimate the impact of the crisis in 2009 and the recovery prospects in 2010 for the sample, both in terms of GDP growth rates. The explanatory variables will consist of sample country export dependence; banking sector balance sheet health; pre-crisis budget situation; and inflation rate during crisis onset which would inhibit policy makers' stimulus adoption capability. Russia, it would seem, had everything going against it in terms of these variables.

During the Soviet investigative phase, I encountered massive data problems. "Where do you get your data from?" was the routine question I faced.

Where Was the Data?

Official data began to be available in a sustained fashion only after the Second World War—more precisely, after Stalin's death in 1953. The first Soviet statistical yearbook was published in 1956, an event of momentous excitement. Indeed, some of the most valuable work in the field consisted in generating data. While Soviet data were of recent origin, they were also plagued with gaps here and there. The size of the statistical yearbook waxed and waned with the state of U.S.-Soviet relations. The detente-phase yearbooks were opulent in contrast to their lean condition during bilateral tensions. Information was arbitrarily held back with the result that obtaining a 30-year time series was an improbable event. And in the view of diehard practitioners, 30 observations are not enough for rigorous econometric application.

Even when long time series were available as with Soviet weather data for my grain yield project, one had only the basic information on monthly temperature and precipitation for use as weather variables in the weather-yield models. "The author should use soil moisture indexes instead because they are more appropriate" was the journal referee's blunt response. But where could I get the detailed information on soil types, their moisture retention capacities at various depths and the like for this purpose?

In short, micro data on outputs and inputs at the firm or farm level were absent. This contrasted sharply with the ready-to-use availability of time series and cross section information, quite often on computer discs, to researchers who worked on problems of the American economy.

Equally serious were the methodological problems associated with the information that was available. These went beyond the familiar distinction between the Marxist Net Material Product (which omitted the contribution of the service sector) and the market-economy Gross National Product. Again, Soviet output data were reported in official sources by sectors of the economy in annual growth rates only. They were also known to include raw material usage by a sector to the exclusion of the market economy value added procedure. Nor were they estimated in constant prices. In my production function estimation

project, the methodological soundness of the output and input data was critical. Of immense value for this purpose were the Central Intelligence Agency's successive rounds of estimates of outputs at the economy, industry and industrial branch levels in terms of the standard market economy practice. I developed alternative output series in two articles published in the *Bulletin of the Oxford Institute of Economics and Statistics* (summer 1973, February 1978) with the intention of correcting the inadequacy. It was not possible to convert Soviet capital stock data, which were inflated, despite official claims to the contrary, into a constant price series. A suitable price deflator did not exist. Nor was it possible to derive a measure of capacity utilization.

Given these problems, I could discard the econometric box of tools, tell stories, and become a free-wheeling policy wonk or apply these tools with a mixture of optimism, curiosity and caution, optimism regarding the applicability of these tools to Soviet problems, curiosity about the results that emerged, and caution about how sound they were. I chose the latter route in my scientific work.

So I began studying the Soviet planned economy in depth in 1968 when I returned to Harvard as a Research Associate at the Russian Research Center, continuing it after I had moved to Columbia University in 1980 as Professor in the Economics Department. My earliest research focused on using the detailed production function estimates for measuring the loss experienced by the Soviet planned economy from 1955 to 1975 as a result of its departure from market economy practices.



How Costly Was the Marxist-Leninist System? : Measurement Issues

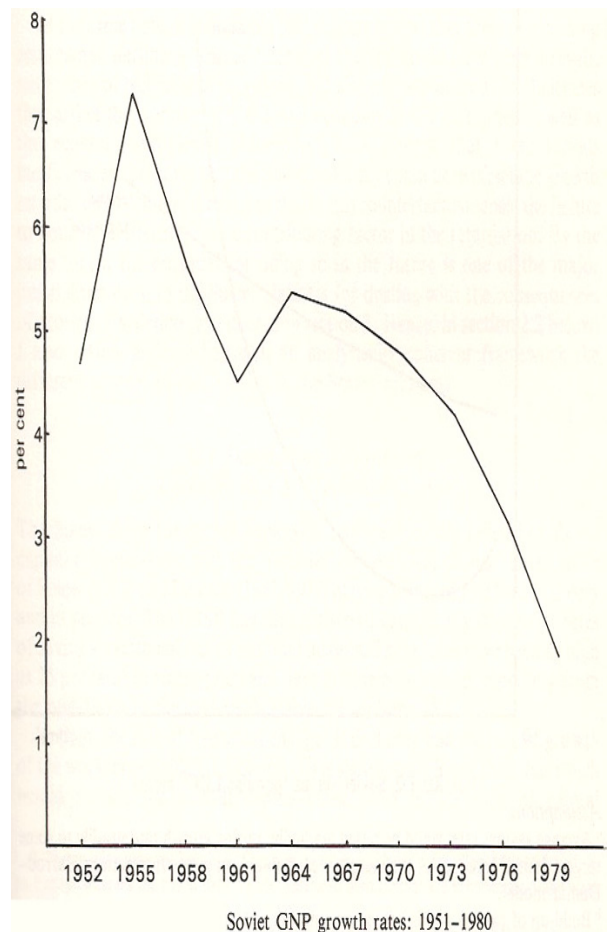
The features of the planned system were implanted via a succession of five-year plans which began with Stalin's massive industrialization drive of the 1930s. Labor was sucked in at a dizzying speed from the countryside and employed in factories at fixed wages. Managers sought to fulfill output targets (handed down by the planners) and sold their products at fixed prices. They also lacked the Schumpeterian drive to innovate. Except in the military and isolated industries, the Brezhnev-era (1965-82) record was devoid of innovative breakthroughs. The inevitable consequences of the rigid institutional setup were shortages and bottlenecks, retarded innovation and faltering growth. The pervasive shortages gave a bizarre flavor to the daily life of the people. "The whole country is covered with blast furnaces," an exasperated Russian friend told David Shieler of the *New York Times*, "but I can't get a table knife." In sum, the overpowering signs and signals of the drab, regimented Orwellian reality were everywhere prompting me to recall a wry witticism: Religion comforts the masses by assuring them that there is life after death, whereas Communism does so by assuring them that there is death after life.

The Soviet output growth record during the immediate postwar period until 1955 for the economy and for specific sectors such as industry and agriculture was solid. However, output growth began to decline from the mid-fifties in comparison with that in most



other countries. The growth was fueled primarily by high saving and investment rates. As labor shortages developed, the strategy of massive substitution of capital for labor could not be relied for long to propel vigorous future growth. Instead, the Soviet planners would be increasingly forced to rely on technological progress that had propelled growth in several capitalist economies with a lower saving rate. One would assume that the switch from an intensive growth regime marked by diminishing returns associated with a high capital to labor ratio did not come soon. The system was much better at amassing resources for large-scale accumulation than at the risk taking and innovative, decentralized, rate-of-return approach that was required.

These subjects such as technical change and allocative efficiency in the Soviet economy represented a new trend in Soviet economics. I was keen to depart from the institutional thrust of much of the preceding work and bring the discipline of Sovietology into the fold of mainstream economics. Why not estimate different specifications of the production function, also with alternative definitions of technical change, and pick up one which "best" defined Soviet production activity? My earliest paper dealing with alternative production function formulations, titled "The Production Function and Technical Change in Postwar Soviet Industry: A Reexamination," was published in the *American Economic Review* (June 1976). By the mid-1970s, foreign capital had begun trickling in the Soviet economy. Could it give a much needed push for easing the growth retardation under Brezhnev? My paper on "The Productivity of Foreign Resource Inflow to



the Soviet Economy” was published in the *American Economic Review (Papers and Proceedings, May 1979)*.

When econometric estimates of production functions and the observed allocation of labor and capital in different sectors of the Soviet economy suggested that resources were misallocated among sectors, how should one measure the implied loss? What could be the appropriate measures of such misallocation losses? I assumed that the actual situation was characterized by the absence of equality between the marginal rates of substitution of factors of production in different industrial branches. When marginal rates were equalized, the reallocation of factors led to more output from the same factor use or less factor use for the same output. I then analyzed the measurement issues first with reference to the output loss resulting for the suboptimal utilization of given factors and then extended the analysis to include measures of factor saving when the same basket of outputs was produced with less factor utilization. I used econometric estimates of production functions in industry branches to reach estimates of the loss arising from inter-branch misallocation of capital and labor deployed in Soviet industry. This loss turned out to be non-negligible, ranging from a low of about 3 to 4 percent to a high of 10 percent of efficient factor use and rising over time. The result suggested a measure of recent decline in Soviet industrial and overall growth from 1955 to 1975. My paper (jointly with Ricardo Martin) titled “The Efficiency Loss from Resource Misallocation in Soviet Industry,” covering the analytical approach and the empirical results, was published in the *Quarterly Journal of Economics* (August 1983). The research project was financed by a two-year grant from the National Science Foundation.

My next exercise related to the importance of weather and input contribution in Soviet per acre grain yield performance.

Weather Variables versus Input Use, Grain Yield, and Grain Imports

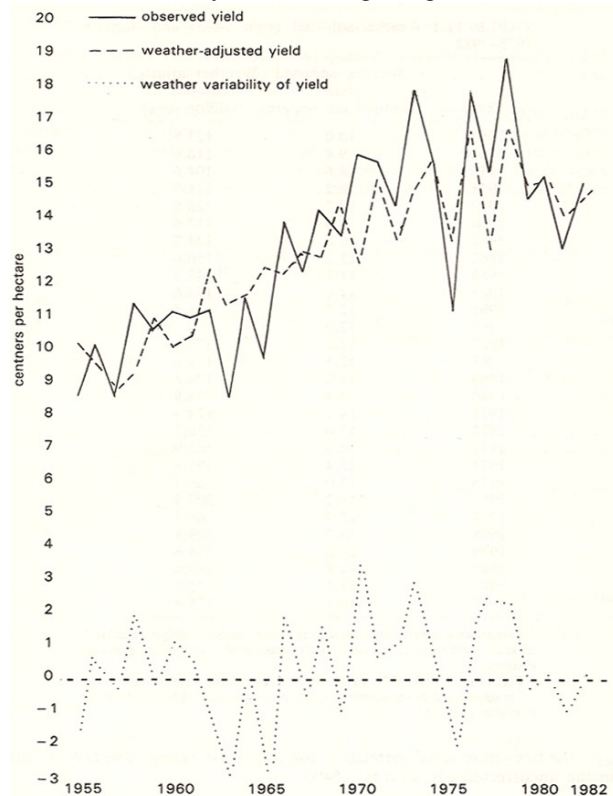
Prevailing opinion on the subject was divided with some experts underlining the role of weather and others emphasizing the impact of “systemic” factors. Among the latter were the lack of market type incentives and decentralized decision making that pervaded the Soviet economy, including farming. Policy factors such as the decision to promote fertilizer use by increasing its supplies and application or raising the relative spring grain acreage would also influence yield. It was clear that the impact of “systemic” and policy factors on yield could not be assessed unless the weather component was separated from yield.

I selected 14 oblasts (provinces) which represented the climate, soil and vegetation of the Soviet grain belt. The oblast was the basic unit of analysis because it was the smallest unit for which sustained time series data of grain yield were available. (Indeed, although they were small, the oblast sizes in the East European grain

growing region varied from 21,350 sq. miles for Pskov oblast to 2,18,040 sq. miles for Samara oblast. Even after the collective farm reorganization under Putin, Russian farm size averages 12,500 acres, much larger than a U.S. farm on average.) I regressed per acre grain yield in each oblast from 1950 to 1975 on an input component and a weather variability component. The input component measured the contribution to yield of the time trend and average weather variables of the oblast crop cycle (The time trend was assumed to represent input use.) The weather variability component measured the variability of oblast yield attributable to the deviation of actual weather from mean weather. I then derived an aggregate equation by regressing actual Soviet grain yield from 1958 to 1975 on the oblast yields derived from the weather yield models and weighted by the relative oblast acreage. As with oblast yields, I defined weather variability for aggregate Soviet yield as the variability of yield attributable to the deviation of actual weather in a year from average weather.

The contribution of weather fluctuations to aggregate Soviet yield variance (explained by the covariance ratio) was 52 percent with input variation accounting for the remaining 48 percent. It turned out that the contribution of weather fluctuations to per acre yield variance (explained by the aggregate model) was only slightly larger than that of input variation.

In the meantime, I noticed that Soviet grain imports had become substantial in relation to world grain trade in the early 1980s. They also tended to vary from year to year depending on Soviet grain and wheat outputs in below average and above average weather. The size and variability of these imports presented serious

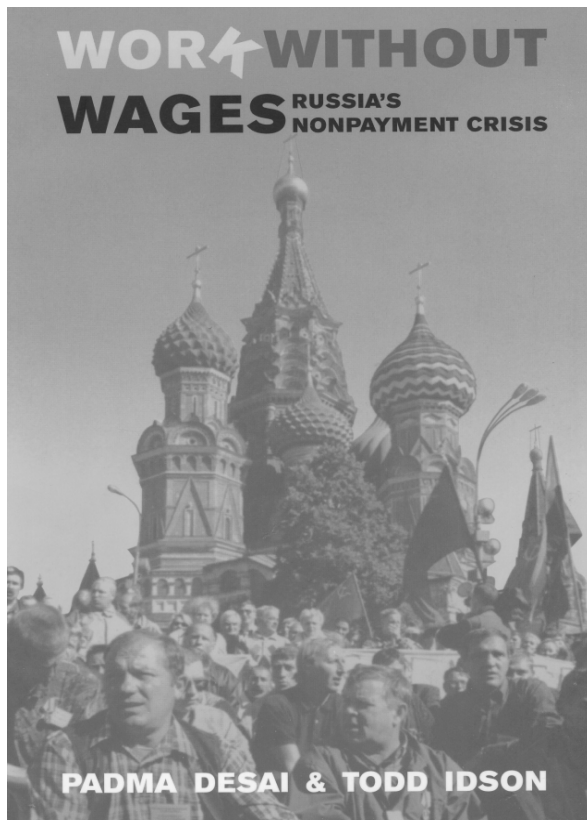


Observed and weather-adjusted grain yield, and weather variability of Soviet grain yield, 1955–1982

implications for grain exporting and grain deficit countries. I employed some of my research results on weather related grain yield variability for predicting Soviet grain and wheat imports in each year in the early eighties. These results were published in “Soviet Grain and Wheat Import Demands in 1992-1985” in the *American Journal of Agricultural Economics* (May 1982). Another paper, “Reforming the Soviet Grain Economy: Performance, Problems and Solutions,” was published in the *American Economic Review (Papers and Proceedings)*, May 1992). The research on the Soviet grain economy during the early eighties was financed by two grants from the International Food Policy Research Institute in Washington, D.C. and by the UN Food and Agriculture Organization.

The articles relating to my continuing research on the allocative efficiency of the Soviet planned economy along with several others on Soviet trade and aid connections with Soviet bloc and developing countries were brought out by Basil Blackwell in 1987 in a volume titled *The Soviet Economy: Problems and Prospects*.

My next project (jointly with my former Columbia colleague Todd Idson) related to an analysis of the exceptional and extensive wage nonpayment from 1994 to 1998 under Yeltsin during which wage and pension payments were either withheld or reduced for millions of Russians.



From “Wages without Work” to “Work without Wages”

The seventy-year old Soviet tradition of “wages without work” turned all too soon into “work without wages” as the Stalinist planned economy began switching to a market system in 1992. The lack of budget discipline surrounding unrealistic budgets, combined with the breakdown of contractual obligations at all levels, and the failure of state agencies to enforce business laws led to pervasive wage nonpayment to workers in the budget sector and in privatized industry. Outright worker layoffs associated with cash flow problems as during the current U.S. recession were avoided. Bankruptcy enforcement was slowed.

Our data originated from the Russian Longitudinal Monitoring Survey (RLMS) project of the Carolina Population Center (CPC) at the University of North Carolina at Chapel Hill, financed by the United States Agency for International Development. The data contained detailed information on demographic and employment characteristics by occupation and job location of working men and women which helped us analyze their labor market experience. The surveys covering 2,000 to 4,000 households at a time helped us answer a variety of questions from the interviewees’ responses. For example, how did employers decide which workers to deny wages? To what extent? How frequently? Were women denied wages more frequently than men? Did workers fall below the poverty line as a result? What were their survival strategies? For example, did they borrow from family members? Did increasing wage arrears lead to widespread strikes? On the other hand, did strikes lead to lower wage arrears? Which way did the causation run?

We analyzed nonpayment patterns across demographic groups defined by gender, age, and education, and in various occupations, industries, and regions of Russia. Having avoided bankruptcies and substantial worker layoffs, Russia’s Soviet-era managers resorted to wage nonpayment and barter as survival mechanisms. We concluded that, having opted for wage withholding rather than explicit contract renegotiations, managers withheld wages more frequently and in larger amounts and for longer periods for the relatively low-paid workers. We also found that women with similar demographic and job market attributes as men were more likely to be subjected to wage nonpayment. The prevalence of barter among enterprises and among employers and workers, seemed to have been exaggerated. Despite mounting anecdotal evidence, although employers did pay workers in goods, the payments, according to our analysis, were insufficient to counter the adverse impact of accumulated wage nonpayment.

Did wage denial push people below the poverty line, defined in terms of a minimum living standard? How did families survive when they were denied wages for months at a time? Indeed, wage denial increased the likelihood of families falling into poverty. Russian

families engaged in a variety of survival strategies to compensate for nonpayment by undertaking informal paid activity, selling family assets, engaging in home production for consumption and sale, and receiving cash from relatives.

Did strikes lead to reduced wage arrears? Workers' recourse to laws for extracting back wages was ineffective, and strikes were largely uncoordinated over time and territory. Our statistical results showed that although wage arrears led to increased strike activity, strikes did not result in a lowering of wage arrears.

Our research was supported by partial funding from the Harriman Institute of Columbia University, and the results were published in *Work without Wages: Russia's Nonpayment Crisis* by the MIT Press in 2000.

The Russian economy, however, began reviving from 2000, its GDP registering an annual real growth rate of 7 percent until mid-2008. The high growth, which resulted from rising oil prices during the period, raised the issue of the possible occurrence of the Dutch Disease in Russia.

Did the Economy Experience a Dutch Disease from 2000 to 2007?

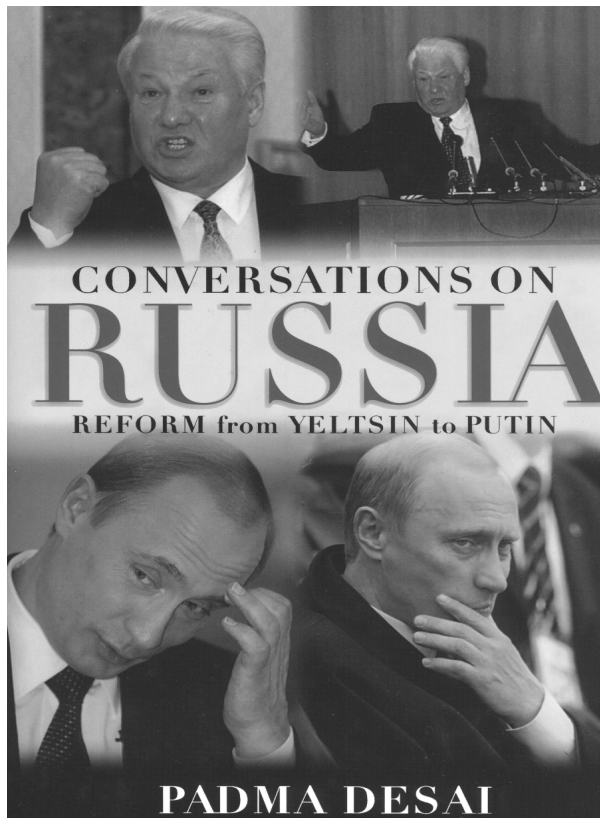
Did the real appreciation of the ruble, brought on by a strong economy and growing investment flows into Russia, damage its manufacturing sector exports as a symptom of the Dutch Disease? Next, did the escalating taxation of the booming oil sector profits create a disincentive for investment in the economy and its growth? Was this impact negative suggesting a

fiscal drag? I applied the Vector Auto-Regression models to the available quarterly data from 1999 to 2005 for analyzing these two issues. My result was inconclusive with respect to the impact of the Dutch-Disease-related ruble appreciation on Russia's manufacturing sector. Its performance was evidently troubled by problems within the sector itself reflecting its rigid, limited pro-market environment. The answer to the second question suggested a fiscal drag resulting from the government sucking investment resources from private oil companies. In other words, the escalating taxation of the oil sector had adverse effects on investment and growth in the economy. The results were published in my paper titled "Why Is Russian GDP Growth Slowing?" in the *American Economic Review (Papers and Proceedings, May 2006)*.

My continuing research relating to various aspects of Russia's transformation from its Communist past required frequent visits to Moscow and close contacts with policymakers at the highest level. In 2000, I started a project of interviews with leading Russian and American policymakers and with prominent analysts who commented on that process as it transpired with unprecedented consequences under Yeltsin's leadership. The project, partially funded by the Harriman Institute, turned out to be a challenging enterprise requiring a firm grasp on my part of the unfolding scene in Russia and of its complicated past. Fortunately, my scholarly engagement of over three decades with the Soviet experience and subsequently with the tumultuous events in Russia under Gorbachev and Yeltsin provided me with the necessary background. My book-length studies, articles in professional journals, and frequent commentaries in the press and the media came in handy for the task at hand. Overall my conversations went beyond economic issues to discuss Russian foreign policy, history, society, and demography. The interviewees livened up their responses with interesting anecdotes, historical and literary references, and revealing stories. The resulting book *Conversations on Russia: Reform from Yeltsin to Putin* (Oxford University Press, 2006) was selected by the *Financial Times* as a "pick of 2006."

Conversations on Reform from Yeltsin to Putin

The evolution of Russian reform started with Yeltsin's colorful and remarkable appearance on the Russian scene as president in 1992 and ended with Putin's orderly but disquieting consolidation of federal authority starting in 2000. In his interview, published in *Conversations*, Yeltsin referred to his young reformist collaborators as his "kamikaze crew." It is incontestable that the group planted the liberal idea in the land of Lenin and Stalin. They dismantled the Communist planned economy and the authoritarian political arrangements that had prevailed over seven decades. Besides, their destructive agenda had a full nod of approval from the U.S. leadership. In a revelatory gem, Strobe Talbott, former Deputy Secretary





of State under Bill Clinton said that the two presidents, Bill and Boris, had bonded. Both wanted the Communist planned economy and the authoritarian regime to go. Clinton's policy imperative was: "Yeltsin drunk is to be preferred to any alternative sober."

However, while the reformers' "demolition project" was successful, their success did not extend to what might be called a balancing "creative project": the establishment of institutions necessary to support a market-oriented economy. In my view, the reformers paid insufficient attention to the consequences of the reform process they unveiled. Their absolutist stance underemphasized both the need to work at getting public acceptance of their program and the need to countervail the adverse distributional implications of some of the key reforms. In particular, while one can understand the rationale for hastening privatization, their agenda of selling Russia's state-owned assets in the natural resources sector to the oligarchs was widely seen as inequitable and even as "outright robbery."

As the reform team stepped into uncharted territory, they not only encountered Communist opposition but also massive difficulties in implementing their program. The process, involving price decontrol and cutback of budgetary subsidies for a variety of entitlement programs, imposed severe hardships on ordinary Russians. At the same time, Russian oligarchs captured significant assets in leading Russian sectors, among them oil, aluminum, steel and nickel. When Yeltsin abruptly resigned on December 25, 1999, his public approval rating had slumped to less than five percent. The political situation across the land was marked by widespread dissatisfaction, increased corruption and weakened federal authority.

Perhaps anticipating his resignation, Yeltsin had already appointed Putin as prime minister. In hindsight, he affirmed his choice of Putin as his successor because, he declares in his interview, Putin was not a "maximalist," and could act as a stabilizer by reining in

the post-Yeltsin political disorder and public discontent. Four years later in the December 2003 parliamentary elections, the Russian electorate voted decisively against the Yeltsin-era reforms and the liberal reformist groups. After eight years of authoritarian governance under Putin, who was elected president in the spring of 2000, Russians continued stating their approbation of Putin in repeated polls by substantial majorities. They were ready to settle for a mild dose of authoritarianism that promised a return to stability, control of terrorism, and economic gains that they felt had eluded them for so long. The implicit contract with an authoritarian leader did not imply that the underlying situation was similar to the arrangements which Russians had willy-nilly undertaken with their leaders throughout history. At the start of the new millennium, Russians in large numbers had ended their involuntary employment with their Communist masters and instead found jobs of their choosing. In their interviews, former prime minister Mikhail Kasyanov (who was fired from his job by President Putin in 2004) and former central bank chairman Sergei Dubinin argued that Russia and Russians had changed in several respects. Yegor Gaidar, who launched the reforms in 1992, remained wary of Putin's democratic credentials but did not "believe in the emergence of nondemocratic regimes in countries with educated, urban populations" such as Russia's.

But the widespread betterment of living standards stretching over eight years was threatened when the global financial turmoil hit Russia toward the end of 2008. That raised new questions about the global impact of the crisis in 2009 and the recovery prospects for 2010 which would differ from country to country. I analyze these issues at length in my new book *From Financial Crisis to Global Recovery* (Columbia University Press, 2011), published with partial funding from the Harriman Institute.

The Financial Crisis and Russia's Recovery Prospects

In my analysis, a crisis-afflicted country's downturn in 2009 and its recovery outlook in 2010 would depend on its continuing export dependence; its pre-crisis budget situation; its inflation rate at crisis onset which would limit its policymakers' ability to mount a government financed stimulus; and finally, the presence of toxic assets in its banking sector.

As I argue in my book, Russia was among the worst hit economies. Its export earnings slumped as demand for oil and commodities, its major exports, declined drastically in global markets. The positive growth rate of the pre-crisis years suddenly became negative in 2009. Government budget surplus turned negative in 2009 when revenue inflows from taxes on the energy sector faltered. The double-digit inflation running into 10 percent a year in 2009 constrained the government's ability to mount a significant stimulus. Finally, Russian banks found it difficult to pay back the loans they had acquired from hard currency creditors during the pre-crisis years. Failing Russian businesses added to the load of nonperforming assets in some banks.

Indeed, this was not the first time Russian banks had damaged their balance sheets by reckless borrowing from outside. Back in 1998, the Russian economy was equally vulnerable to macroeconomic and financial imbalances as in 2008-2009, but for a different reason. On August 17, 1998, Yeltsin's government declared a unilateral default on the government's ruble debt, prohibited commercial banks from clearing their foreign liabilities, and devalued the ruble from 6 rubles to a dollar to 26 rubles. The 1997-98 financial crisis, which had spread from Bangkok to Brazil via Moscow, had arisen from massive short-term capital inflows into emerging market economies which were pushed by determined Washington policy makers, among them the IMF, and supported by Wall Street financiers. These inflows were short-term, speculative, and destabilizing. In my *Financial Crisis, Contagion and Containment: From Asia to Argentina* (Princeton University Press, 2003), I argued that the premature financial opening up by the risk-prone, return-savvy investors from developed market economies with global electronic reach had collided with the weak financial institutions, traditional corporate practices, and vulnerable political arrangements of emerging market economies, among them Russia. The book was noted by Paul Krugman as "the best book yet" on financial crisis.

How effectively has the Russian government managed the recent financial crisis that unfolded toward the end of 2008? Which policies were implemented by decision makers in the Ministry of Finance and the Central Bank of Russia for minimizing its impact? In my article titled "Russia's Financial Crisis: Economic Setbacks and Policy Responses," published in the *Journal of International Relations* (February 2010), I argued that Prime Minister Putin's government managed the options with a noteworthy technocratic policy orientation. The

ruble was allowed to decline gradually in early 2009 as foreign holders switched to other currencies. The inflation rate was brought down from a low, double-digit to a single-digit 6 percent by early 2010. While Russian banks continued to battle nonperforming loans in their balance sheets, the overall situation sent improving signals. The unemployment rate by mid-2010 had settled at 7 percent of the workforce. The accumulated foreign exchange reserves of \$600 billion as well as the budget surpluses of the pre-crisis years provided the bailout resources. Even the oligarchs, who faced margin calls from their foreign, hard-currency creditors, were rescued with funds from a state bank which, however, acquired their stock in exchange. By a strange irony of circumstances, the Russian state (via the state-owned Vneshekonombank) regained stocks which it had given away to the oligarchs who had provided cash support to the Russian budget in 1996 and 1997.

The initial Russian bailout however was a top down, speedy process involving a few decision makers without it being subjected to independent scrutiny or legislative oversight or systematic winnowing of the turmoil victims. One looked in vain for the likes of Representative Barney Frank who insisted on a vigilante role for the U.S. lawmakers.

Beyond 2010, the Russian leadership faces the formidable challenge of modernizing and diversifying the Russian economy from excessive reliance on volatile exports of energy and commodities.

How Can the Russian Economy Be Modernized and Diversified?

Apart from excessive energy export dependence, the Russian economy's diversification dilemmas arise also from the interlocking of the massive industrial companies in the commodities sector with large service, technology and trading enterprises. For example, Gazprom, the world's largest natural gas monopoly, not only supplies gas to customers inside and outside the country but also effectively controls the entire natural gas transport network. Both, in turn, with majority ownership of the Russian state, are effectively controlled in their production and pricing decisions by state-appointed executives. The interlocked structure not only prevents the emergence of robust corporate governance and market-based competitive decision making but also fosters an attitude of "legal nihilism." In a striking display of forthrightness, Russian President Dmitry Medvedev remarked on September 10, 2009: "Can a primitive economy, based on raw materials and economic corruption, lead us into the future?"

Clearly, the adoption of market-based budgetary, monetary and exchange rate policies by technocrats in the Ministry of Finance and the Central Bank of Russia helped them steer the economy through the initial impact of the financial crisis. But the tail of these policy instruments cannot wag the sprawling dog of the entrenched, state-controlled big business in Russia. The

flow of foreign investment, even in a minority role, can help initiate the process, but venturing in Russian big business is an unmitigated risk. Russia's forthcoming entry in the World Trade Organization can also promote rule-based procedures in pricing and trading activities. But foreign investors and WTO rules can only play a marginal role. Ultimately, the Russian economy's overhaul from top down will depend on "destructive creation" initiatives from the leadership in Moscow.

Can the reset button announced by Secretary of State Hillary Clinton on March 6, 2009, provide an external stimulus via a cooperative management of bilateral American-Russian relations on issues ranging from NATO's eastward expansion and arms control to nuclear nonproliferation and terrorism control? Will the handshake between presidents Obama and Medvedev on April 8, 2010, over their signing of the renewed START Treaty, which pledged to reduce U.S.-Russian stockpiles of deployed nuclear weapons, ease bilateral tensions further? Can a continued easing of bilateral tensions on foreign policy and security issues provide a modicum of confidence to Prime Minister Putin to begin liberalizing the economy if not the authoritarian political arrangements? From a limited perspective, can the process initiate investment flows from American business which Russia needs?

The Implications of the Reset Button

A careful review of the two-year tenure of the joint Putin-Medvedev governance suggests guidelines in this regard. Following the severe impact of the financial crisis on the energy-dependent Russian economy, both leaders have discovered a common mission for modernizing and diversifying the Russian economy. Indeed, they both

want a significant role for foreign direct investment for the purpose.

There is, however, a difference in their philosophy and approach. President Medvedev is a staunch believer in free enterprise, and talks unabashedly about what is wrong with Russia. On June 18, 2009, at the St. Petersburg International Economic Forum, he articulated his vision of a future Russia with total clarity: "A modern economy cannot be built through decrees from the top." He frankly states the handicaps that Russian policy makers face: In his view, they battle poor governance, ineffective law enforcement, corruption, white collar crime, administrative barriers and monopolies. Prime Minister Putin, who is equally committed to modernizing Russia in measured steps, would not express either of these views although he is fully aware of the massive hurdles facing foreign investors.

The Russian economy in the view of both leaders needs foreign direct investment desperately. The flow of \$70 billion in 2008 had dropped to \$15.9 billion in 2009. Even the lawmakers have recognized the need for safeguarding the property rights of investors. On June 16, 2010, the lower house of the Russian parliament, the Duma, passed a law prescribing punishment for individuals who falsify official charters of legal businesses or results of shareholder meetings. The penalties are severe for those who use violence for this purpose. Bureaucrats who facilitate these activities will face a fine or lose their jobs or go to prison.

The reset button initiated by the Obama-Clinton team provides a solid underpinning for U.S. investors to step actively into Russia. They will not only provide the necessary technology and corporate management expertise but also the legal underpinning which Russian big business needs. The interactive relationship can



gather speed if Prime Minister Putin reduces the number of strategic sectors in which foreign investment participation is restricted.

I am not suggesting that U.S.-led investment participation will initiate a process of political liberalization in Russia. It is difficult to predict the timing and manner of the demise of authoritarian regimes. The current signals from Moscow lack positive indications in that regard. Russia will hold parliamentary elections in 2011, followed by the presidential election in 2012. The reformist groups in Russia have decided to combine their ranks and fight the parliamentary election as a single bloc. Will United Russia, the party which is led by Prime Minister Putin and which controls the Russian Duma, break into two groups? In a recent statement, Gorbachev described United Russia as “a bad copy of the Soviet Communist Party.” Will Putin contest the presidency in 2012 and remain in charge of Russia’s destiny for 12 years as the constitution allows him? That can mark a repeat of the economic stagnation which the Soviet Union experienced under Brezhnev from 1965 to 1982. There is, however, a difference. Brezhnev had to deal with the military and economic burden of the Cold War. The reset button will afford Putin the choice of initiating mini-steps of political liberalization starting with the election of regional governors.

The decade-long authoritarianism under Putin portends an uncertain political future. Given Russia’s long history of authoritarian rule, “the poisoned chalice of history,” the evolution of a liberal political order will be haphazard, perhaps even hazardous at times.

However, the Clinton announcement of the reset button and the Obama-Medvedev handshake at the signing of the Start Treaty were moments of immense professional fulfillment for me. From early on, I had

been arguing against the Bush-Cheney confrontational decision-making on several issues ranging from NATO’s eastward expansion to include Ukraine and Georgia in NATO and the placing of nuclear units in Poland and the Czech Republic to ward off an enemy missile attack. The Russian leadership regarded the former as placing western military outposts in Russia’s backyard and the latter as a revival of cold war confrontation. These initiatives have now gone into moratorium.

Starting in 1968, I began analyzing the policy twists and turns in the former Soviet Union by sifting the evidence and applying the analytical tools of the economics discipline rather than letting myself be swayed by ideological preconceptions or emotional predisposition. This approach clearly violates the stricture laid down by the nineteenth-century Russian poet Fyodor Tyutchev in his four-line lyric which has become a celebrated invocation about how one might understand Russia.

Умом Россию не понять...
В Россию можно только верить.

“Russia cannot be grasped with the mind.... One can only believe in Russia.” On my part, I have sought to understand Russia on the basis of a challenging and rewarding intellectual engagement.

Padma Desai is the Gladys and Roland Harriman Professor of Comparative Economic Systems and Director of the Center for Transition Economies at Columbia University. Her new book *From Financial Crisis to Global Recovery* has just been published by Columbia University Press.

BEYOND RESENTMENT

Mykola Riabchuk

Vasyl Kuchabsky, *Western Ukraine in Conflict with Poland and Bolshevism, 1918-1923*. Translated from the German by Gus Fagan. Edmondton and Toronto: Canadian Institute of Ukrainian Studies Press, 2009. 361 pp. + 6 maps.

It might be a risky enterprise to publish a historical monograph written some eighty years ago, which at the time addressed the very recent developments of 1918-1923—this would seem to be much more suited to lively memoirs than a cool-blooded analysis and archival research. Indeed, since 1934 when Vasyl Kuchabsky's *Die Westukraine im Kampfe mit Polen und dem Bolschewismus in den Jahren 1918-1923* was published in Germany in a small seminar series, a great number of books and articles on the relevant topics have appeared, and even a greater number of archival documents, letters and memoirs have become accessible to scholars.

Still, as Frank Sysyn rightly points out in his short foreword to the English translation of Kuchabsky's book, "it remains critical to the study of the topics [outlined in its title]. It is also essential to understanding the views of a leading Western Ukrainian political activist and thinker, himself a participant in that struggle, and, through him, the generation that shaped Ukrainian politics in the first half of the twentieth century" (ix).

Oleksandr Pavlyuk, who penned an informative introduction to the book that provides readers with a sketch of the author's life and writing and places everything in a comprehensive historical and social context, emphasizes the importance of Kuchabsky's eyewitness accounts. Yet, of even greater value, he argues, is the high professional quality of the monograph—"a study by a scholar with a good education, a sharp analytical mind, and fluency in several European languages" (xiv).

Kuchabsky's account of the events is certainly not impartial. World War I found him a nineteen-year-old student at Lviv University; he joined as a volunteer in the Ukrainian Sich Riflemen—the first Ukrainian military legion created within the Austrian army. The experience of the war, of Russian captivity and escape, of the revolution and further fighting for Ukraine's liberation as the head of the Riflemen, a short stint in diplomatic service for the West Ukrainian National Republic, and the bitter fate of political emigration undoubtedly influenced the way in which he perceived and interpreted events.

His sympathy for the Riflemen as superior fighters is unreserved, his mistrust of the duplicitous Poles is unbalanced, his disdain for the leaders of the Ukrainian revolution sometimes appears extreme, and his repeated accusations of betrayal at the hands of Western governments, however warranted, sound obsessed.

Nevertheless, the book provides a comprehensive account of the political, military and diplomatic efforts

of Western Ukrainians to establish their independent republic on the ruins of the Habsburg empire—in full line with the prevailing Wilsonian principle of national self-determination, the right presumably granted by the victorious Entente to all East European nations. Western Ukraine is in the center of both the title and the narrative, and this makes both the book and its translation rather important, since there are still very few "Ukrainocentric" accounts of these events, which though not necessarily opposing the dominant Polish and Russian perspectives, at least provide some check on the myths and biases and challenge or supplement the dominant views with neglected facts and alternative interpretations.

Ukrainians lost their battle for independence and, as Kuchabsky bitterly remarks, proved to be the only East European nation which failed to benefit from the "Wilsonian" right to self-determination or, rather, which under strong Polish pressure was denied this right by the Entente and its Supreme Council. Resentment reigns supreme in the book, and the author is not sparing with his indignation of Western ignorance, hypocrisy and cynicism, as well as Polish arrogance, pathological chauvinism and perfidy. Yet, despite some excessive emotionality, he avoids propagandistic demonization and the essentialization of opponents. He aptly notes important nuances and internal differences within both the Polish and Entente camps that could have been effectively used by Ukrainians to their advantage.

Within the Polish camp, he distinguishes the "fanatical nationalism" and profound Ukrainophobia of Dmowski's National Democrats, on the one hand, and the more pragmatic approach of Pilsudski and the Polish socialists who flirted briefly with the idea of a Polish-Lithuanian or even Polish-Lithuanian-Ukrainian federation, on the other hand. Moreover, he recognizes that in late 1918 and early 1919 the newborn Polish state was in a much worse internal and external situation than the Western Ukrainian National Republic. Internally, as a result of divisions caused by the Partitions, it was completely disorganized and chaotically ruled by different governing bodies. Externally, it faced actual or potential border disputes with all its neighbors. This was a short window of opportunity for WUNR, when independence could have been secured by military means—if Ukrainians had better prepared their takeover of Lviv and Eastern Galicia or, at least, blocked effectively their border with Poland, primarily the bridge across the San river at Peremyshl and the railway to Lviv, rather than waging

a protracted and unsuccessful battle with Poles for Lviv, which ultimately was a battle of high symbolic but little strategic importance.

After the opportunity was lost and the Polish state had gradually consolidated under Pilsudski's leadership, the fate of Western Ukrainian independence depended primarily on the political and diplomatic skills of its leaders. And here, again, despite all his disgust for the "Western traitors" who sacrificed WUNR to the Poles for particular gains (oil fields for the Brits, an anti-German alliance for French), Vasyl Kuchabsky recognizes that the Westerners who negotiated a political settlement for Galicia were neither a homogeneous group nor were they immutable. Here the interplay of various views and interests was even more complicated than within the Polish camp. And this, again, provided Ukrainians with some window of opportunity—despite the huge advantages the Poles gained from their historical visibility versus the virtual absence of Ukrainians on the Westerners' mental maps. The Poles, indeed, had a much stronger and larger intellectual elite, much better contacts in Western capitals and, of course, they represented their cause more effectively by depicting Ukrainians as an Austrian invention and German intrigue, as wild Bolsheviks and/or unruly, uncultured aborigines unable to govern themselves and requiring assiduous Polish guardianship. Yet, as Kuchabsky argues, there were a number of opportunities to strike a deal with the Poles and the Entente and secure the independence of Western Ukraine—without Lviv and probably without the Boryslav-Drohobych oil fields but with due international recognition that was far more important for the "nowhere nation" than anything else.

It might have been a difficult choice—it ran counter to the popular mood and the inevitable mass protests. But "given Ukraine's internal and external situation at the time, it was in no position to achieve more. It was a major step forward for a stateless people to be able to set up a rump state if the choice was between this and complete subjection. In order to accept [this] kind of peace, a nation would have to be free of all ethnic conceptions in the realm of politics. International politics would have to be seen as the interplay of real national forces, not as a conflict involving just abstract national rights" (206).

In fact, Kuchabsky blames the Entente powers not so much for the cynicism, since Realpolitik, in his view, is a norm on the international scene: all the players are driven primarily by their particular interests, not universal values. He blames the Entente primarily for hypocrisy—the false proclamation of the Wilsonian principle that had not been honestly implemented, but which instead confused and misled Western Ukrainians, evoked expectations that were too high; moreover, a naïve trust in the Entente and the sacred right of national self-determination distracted them from more decisive activity in the battlefield and more rational and pragmatic political decisions. To his credit, he blames not so much the Westerners as his countrymen, especially from

Eastern Ukraine, who discredited and undermined their cause rather than promoted it. At several points, he recognizes that the leaders of the Ukrainian revolution were mediocre persons, inferior in many regards to their Polish counterparts and unable to negotiate effectively with the Entente. None of them "had a comprehensive view of what was happening"; "isolated events were not seen as a part of a general context" (42).

Dr. Yevhen Petrushevych, the head of the West Ukrainian state and a former member of the Vienna parliament, is described as a "provincial lawyer," a person of "strong moral principles" and "inner discipline," whose "complete honesty and respectability" made him a "model notary and keeper of the seal"; but still he was not a statesman. All these features, Kuchabsky argues, were of little help since they only "restricted his political intellect, which operated only in the narrow realm of a puritanical simplicity" (255). The entire Western Ukrainian leadership is viewed in a similar way:

In the atmosphere of legality and security in which the Ukrainian parliamentarians in Austria had carried on their conflict with the Poles, they had never really learned that war is an instrument – in fact, the most refined instrument – of politics, and now that the Poles were no longer a negotiating partner equally subject to the verdict of Vienna, but an independent warring power, they were at a loss as to what to do in such an unusual situation... In the leading Ukrainian political circles there was not a single relatively prominent personality who was capable, in this difficult situation, of taking the reins in his own hands and directing events. (41)

East Ukrainian leaders evoke in him even greater disdain. Volodymyr Vynnychenko is mentioned briefly as a "baleful man of letters" whose politics "had done a good deal of damage to Eastern Ukraine in 1917-18, just as in the decade before 1917 his clever pen had poisoned the intellectual atmosphere" (158-59). General Mykhailo Omelianovych-Pavlenko is described as a "serviceman through and through, very modest in ideas and general cultural interests," skilful in "training troops" but not in "leading them in warfare." "He was unable to grasp a broader totality, be it political or strategic, consider it from different viewpoints, and chart a way forward" (186). Even Symon Petliura, "a brilliant orator with a winning personality, witty, modest and gentle," a great patriot of Ukraine ("no one had greater love for the fatherland than he"), whose name "became practically synonymous with the whole enterprise of the Ukrainian People's Republic," was, in Kuchabsky's view, merely a "tribune of the people, not a statesman" (92-93):

He had no understanding of what constituted the underlying strength of a state or of what moral and intellectual preparation

was necessary for a position in the service of that state. He considered a national sentiment an adequate basis on which to found a state. He sought without scruple to arouse national enthusiasm among the people and was prepared to use any means to that end, whether socialist demagoguery to whip up the masses or an appeal to defend civil order in Ukraine against the threat of Bolshevism... [National independence] became for him a fanatical religion for which he would live and die. But this was only a fanatical emotion, without insight, without understanding... He distrusted the senior officers of the former Russian army, looking instead for the kind of carelessness that, in his mind, went with a proper warlike spirit... He failed to recognize that the army is better fitted to the task of building a modern nation-state if it is strongly disciplined in its military behavior and in its dealings with the civilian population and has a strong sense of honor. (93)

In sum, “Petliura was not a man of any great political talent, and he never really understood the need for proper organization of the army and the country” (286).

These assessments, however harsh and at times imbalanced, deserve our attention since Vasyl Kuchabsky had firsthand knowledge of many Western and Eastern Ukrainian leaders. The Westerners, in his view, deserved less censure, since under peaceful conditions they were well qualified to manage the country lawfully and efficiently. Their problem was rather external. As “small-minded pacifist philistines” (190), with poor statesmanship qualities and strategic vision, they could not withstand effectively the Polish invasion and Entente betrayal. The Easterners, in Kuchabsky’s view, were crude products of the “radical democratic, revolutionary socialist and internationalist development” (93)—not gentrified by liberal notions of constitutionalism, rule of law, separation of powers, and institutional efficacy. Hence, their problem was first and foremost internal. They proved to be absolutely dysfunctional in governing and state-building. “Such a task greatly exceeded intellectual, political and material strength of the Eastern Ukrainian national movement... The national leadership would perhaps have measured up to the task of building an independent state in a country the size of Lithuania. But Eastern Ukraine... had a population of thirty million” (71).

The bitter truth, according to Kuchabsky, is that the Ukrainian People’s Republic “was no more a state than any of the other counterrevolutionary enterprises in Eastern Europe in 1919, such as those of Aleksandr Kolchak or Anton Denikin. It was merely a military organization. Just as in the case of the reactionary armies in Russia, the masses of the people did not take part in this organization. In some areas they approved of it;

in others, they rebelled against it. But that was the full extent of their relations to this organization” (92).

National leadership, in Kuchabsky’s political philosophy, plays the paramount historical role—far more important than the common folk. Nonetheless, at certain points, the author comes to recognize a connection between the quality of elite and the population at large. Great statesmen and military leaders, indeed, can do miracles even with an immature population—as seemed to happen, for a brief time, with the Western Ukrainian army under General Aleksandr Grekov’s lead. But one can barely build a full-fledged nation-state upon miracles, especially if these “miracles,” as Kuchabsky implies, are also products of some path-dependency: “[Grekov] was one of the few Russians who linked his fate to that of Ukraine... In his thinking and his actions he was a statesman of a great political nation, Russia. He had what the Western Ukrainians lacked – a mature political culture that had developed out of the manifold experience of the Russian Empire” (230-31).

Whatever miracles might have happened, the path-dependency is unavoidable in the long run. And Kuchabsky, despite all his profound elitism, comes to recognize a bitter egalitarian truth about the Ukrainian revolution: “The internal state of the Ukrainian nation itself, with its sociopolitical divisions, made it unfit for the task of establishing an Eastern Ukrainian state. In the art of politics it showed itself too weak to build any kind of state, whether democratic or conservative” (71).

Besides the Poles and Bolsheviks who presented the main challenge to Ukraine’s independence and who are rightly featured in the title of Kuchabsky’s book, there was one more force that contributed to Ukraine’s ordeal. The author defines it as the “all-Russian counterrevolution” represented in the southwestern part of the former Russian Empire, including the territory of Ukraine, by the “White Guard” of General Anton Denikin. In September 1919, they threw Petliura’s government out of Kyiv—just a few days after the Ukrainian troops took it over from the Bolsheviks. This left Ukrainians with little choice but to declare war on Denikin, even though they tried to avoid military confrontation with Russian monarchists and were ready for negotiations and some sort of compromise. The Russians, however, preferred the language of ultimatums demanding from Ukrainians unconditional submission to “Russia, one and indivisible.”

“For Denikin’s army, this was madness” [292], since it not only severely hampered the Ukrainian struggle for independence but also dramatically undermined Denikin’s own chances to defeat Bolsheviks in his rather successful march to Moscow. Nevertheless, as Kuchabsky aptly remarks, “this was a typical result of the situation created by the senseless divisions in the counterrevolution... Once again the superiority of the Bolshevik strategy over that of the Russian counterrevolution was demonstrated with a great clarity. The Bolsheviks could have easily advanced from the north to occupy Ukrainian-held territory... But they preferred to postpone the occupation

of Ukraine until Denikin's forces had been finally defeated by the Ukrainians" (293). Remarkably, in 25 years, the Bolsheviks once again demonstrated the same superior strategy—postponing their advance on Warsaw until the Nazis fully extinguished the Polish uprising.

"In overestimating its own potential, the all-Russian counterrevolution completely failed to realize that the driving force that could be turned against the Bolsheviks was not its own desire for restoration but the regional desire to separate" (283). The extreme stupidity of the Russian monarchists who were dogmatically attached to the idea of "one and indivisible Russia" and idiosyncratically rejected any demands of imperial nationalities for a broader self-rule, is a rather well-documented and broadly recognized fact. Vasyl Kuchabsky, however, goes beyond this recognition. He tries to explain the reasons for such a dramatic, unbelievable blindness on the part of an otherwise rational, well-educated imperial elite.

He concludes that Russia was not perceived by the ruling elite as a multiethnic state because, unlike most European countries, it had not undergone the process of democratization throughout the nineteenth century. The Russian nation, for them, was limited to the upper stratum. As long as this stratum (with the remarkable exception of Poland and Finland) was Russian or Russified, rather indifferent to cultural, let alone political particularism, all ethnic differences among the passive popular masses within the empire were irrelevant. "This numerous all-Russian upper stratum, consisting of a bureaucracy in constant flux, as well as of long-established large landowners and bourgeois, gave the empire a unified character... It cemented the bond between St. Petersburg and the ethnically non-Russian periphery and knit together the non-Russian masses, with their real but politically inconsequential ethnic differences, into a more or less organic union with the Russian Empire as if this empire were an ethnic unit, an ethnic Russian entity" (270).

So, Kuchabsky insightfully writes, "when the all-Russian representatives of the Russian empire expressed their contempt for the insignificant separatist activities among the ethnically non-Russian peoples; or when they proclaimed the national unity of the Russians, Ukrainians and Belarusians and described the Ukrainian movement in Dnipro Ukraine as a fantasy; even when they rejected with indignation the term 'multiethnic state' with reference to Russia and preferred to think of it as a united nation-state, then, given the overwhelming dominance of the 'all-Russian' idea, they were correct for the time being" (270).

The Revolution of 1917 destroyed this pre-modern quasi-national unity but the "all-Russian" elite failed to recognize its meaning – exactly as they had never actually recognized the real meaning of the French Revolution and all the eventual democratizing-nationalizing developments in Europe, America, and worldwide. "Russia as an all-Russian national state, the state of the Russians and the Russified upper strata,

was now irretrievably lost. What emerged in 1917 was a multiethnic state in which the democratized and nationally conscious non-Russian peoples regarded themselves as equals of the Russians... There was no reason why a democratic sovereign people, in ethnically non-Russian territories such as Ukraine, should allow their state to go on having this all-Russian character..." (271).

The process of the empire's disintegration looked inevitable but, all of a sudden, "the old Muscovite-Russian conception of imperial unity emerged again in a new and unexpected form: Bolshevism" (272). Long before 1917, Kuchabsky writes, the Bolsheviks understood that not only tsarism but also the idea of all-Russian unity had irrevocably played out its historical role. Any social emancipation inevitably entailed an awakening and national emancipation of non-Russian nationalities. Nationalism was a force to be reckoned with. The Bolsheviks as egalitarians understood what the elitist counterrevolutionaries could not grasp. If you cannot contain the process, you'd better try to lead it. They employed, with the highest skill, their favorite tactics of "give away – take back" to dismantle the old empire and re-establish the new.

First, to mobilize allies in their struggle against the Provisional Government and weaken the imperial apparatus, they proclaimed the "right of self-determination for the nationalities of Russia, including their right to separate." Then, when the ancien régime collapsed with the substantial help of peripheral nationalists, they began reconstruction of the empire under the slogans "proletarian internationalism" and "world revolution." To some extent, they offered the non-Russian nationalities a share in the global social-revolutionary joint-venture called the "USSR" that appeared ultimately to be just a cover-sheet for the same old-new Russian Empire.

In order to stem the centrifugal tendencies of [imperial] nationalities and weld them together once more into a unified political nation, the Bolsheviks advanced not a political but a social program. Unlike in the old regime, the all-Russian idea would now penetrate to the lower strata. While leaving their ethnic, regional and linguistic particularities untouched, as was the practice under tsarism, the Bolsheviks spoke to the political aspirations of the nationalities, calling on them to create the closest possible bond with the Russian state and, in the name of the international social-revolutionary solidarity of the non-Russian and Russian peoples, to defend Soviet Russia against the whole capitalist world. These nationalities would then be restricted in the process of their development toward nationhood and kept politically at the level of their "Little Russian" regional particularity not by power

of the Russified upper strata but by means of the free will of the non-Russified lower strata. (274)

However brilliant the idea, the Bolsheviks largely overestimated the ability of social categories to substitute for national categories. The “free will” of the non-Russian masses did not prove to be a sufficient bond to hold the multiethnic empire together vis-à-vis the centrifugal tendencies of ethnic nationalisms. The new regime had to rely not only on the power of the Russified upper strata but also on the secret police and mass terror to keep the democratically emancipated masses at bay. It turned out exactly as Kuchabsky predicted: “with the decline of the democratic revolution, an even greater despotism than the tsarist one would emerge: world-revolutionary Soviet Russia” (274).

In 1918-23, both Western and Eastern Ukrainians lost their struggle for independence but the Ukrainian question had not disappeared from the agenda either in interwar Poland or in the Soviet Union, but instead continued to poison the organism of both states, ultimately contributing to their decline. In the early 1930s, when Kuchabsky was completing his book, he could certainly not predict the timing of pending processes or their specific ends. But he felt perspicaciously that all the parties “caught up in a wild and vicious conflict” are ultimate losers, “sliding toward dissolution and internal collapse” (327).

Despite all its misapprehensions and limitations, Vasyl Kuchabsky’s insightful book remains important reading for any student of the history of the region as well as its still complicated present.

Mykola Riabchuk is a Senior Research Fellow at the Ukrainian Center for Cultural Studies in Kyiv, and currently (March-July 2011) a Reagan-Fascell Research Fellow at the National Endowment for Democracy in Washington, D.C. His last book is a volume co-edited with Andrej Lushnycky: *Ukraine on Its Meandering Path between West and East* (Bern: Peter Lang, 2009).

Commercial Contact and Conflict Prevention: The Georgia-Abkhaz Case

David L. Phillips

Introduction

This article explores opportunities for interaction between Georgians and Abkhaz. Recommendations are based on the belief that private sector representatives are well suited to take a cooperative approach to engagement and that, even in the most intractable conflicts, the private sector is primarily interested in market access and a stable environment for doing business. The article does not address questions regarding the political status of Abkhazia nor does it explore security arrangements. Politics and security are considered only to the extent that they impact economic issues.

History/Context

Abkhazia, a territory located on the Black Sea in the northwest corner of Georgia, broke away from Tbilisi's control after the conflict of 1992-93. More than 250,000 ethnic Georgians were driven from their homes in violence that the international community characterized as "ethnic cleansing." The conflict remained frozen until the war between Georgia and Russia in 2008.

After the 2003 "Revolution of Roses" brought President Mikheil Saakashvili to power, the Government of Georgia (GoG) initiated dramatic political and economic reforms. Development and democratization were aimed in part at advancing the reintegration of Abkhazia and South Ossetia. Georgia became an economic success story. In 2007, Georgia's economy grew 12% from a boom in the telecom, construction, transport, financial and tourism sectors. Trade increased 39.9% between 2006 and 2007. Exports increased 32.5% and imports by 41% during the same period. Georgia saw an overall improvement in its GDP, fiscal balance, current account balance, and real exchange rate. Positive structural changes included improvements in the banking system, position of the central bank and increasing rates of tax collection. Foreign direct investment was \$1.8 billion in 2007, a 40% increase from the previous year and 19.8% of GDP.¹ Georgia also benefited from its membership in

the World Trade Organization, as well as its location on the Eurasia Silk Road.

Russia resented Saakashvili's pro-Western positions and launched a propaganda and harassment campaign aimed at undermining the GoG. It also took steps against Georgia's statehood by providing Abkhaz separatists with diplomatic and military support. In March 2008, Russia withdrew from the CIS declaration banning military assistance and imposing sanctions on Abkhazia. It also established legal connections between its ministries and their counterparts in Abkhazia, opening fifteen new checkpoints along the cease-fire line between Georgia and Abkhazia.

War between Georgia and Russia erupted on August 7, 2008. In response to Russian and South Ossetian provocations, Saakashvili ordered the shelling and deployment of Georgian troops into Tskhinvali, South Ossetia's capital. By August 9, Russia's disproportionate land, air, and sea assault overwhelmed Georgia's armed forces. Operations extended from the port of Poti in the west to Gori just 40 km from Tbilisi. Russian forces occupied the Kodori Gorge, to the northeast of Abkhazia. Ossetian militias, often in collusion with the Russian military, burned and looted Georgian villages around Tskhinvali.² Civilian economic costs are estimated at \$1.2 billion.

Acting on behalf of the EU Presidency, France's President Nicolas Sarkozy negotiated a ceasefire on August 12, 2008. The agreement required a withdrawal of forces to pre-war positions and access by humanitarian and monitoring missions to the conflict areas. Russia has repeatedly violated the ceasefire by, for example, refusing to withdraw troops or dismantle checkpoints and unilaterally creating a 12 km buffer zone around South Ossetia. Citing "new realities," Russia established diplomatic relations with Abkhazia on August 26, 2010. Only Russia, Venezuela, Nicaragua, and Nauru have recognized Abkhazia and South Ossetia. Every other

1. Interview by the author with U.S. Ambassador John Tefft in Tbilisi, June 18, 2008.

2. Tavernise, Sabrina. "Survivors in Georgia Tell of Ethnic Killings," *New York Times*. August 19, 2008; C. J. Chivers, "In Battered Villages, Georgians Speak, if They Dare." *New York Times*. August 18, 2008.

country views Abkhazia and South Ossetia as part of Georgia.

More than \$4.5 billion over three years was pledged to the GoG at a conference of donors on October 22, 2008. The package consisted of \$2 billion in aid and \$2.5 billion in loans, including an 18-month stand-by agreement with the IMF worth \$750 million.³ Making Georgia one of the largest per capita recipients of foreign aid, the U.S. pledged \$1.06 billion. Assistance helped bolster investor confidence, sustain private capital flows, and provide sufficient liquidity to the banking system. It also helped the GoG maintain a stable exchange rate and adequate level of international reserves.⁴

Engagement Strategy

The GoG published its “State Strategy on Occupied Territories” on January 27, 2010. The State Strategy rejects violence as a tool for resolving conflict with Abkhazia and South Ossetia, or addressing status issues. It seeks instead to promote interaction aimed at improving the socio-economic conditions on all sides.

The State Strategy and Action Plan provide a roadmap for implementing Georgia’s “Law on Occupied Territories.” Adopted on October 15, 2008, the Law is the primary bulwark supporting the GoG’s policy of non-recognition towards Abkhazia and South Ossetia. The Law regulates diplomatic contact, commercial activity, travel to the territories, and travel by Abkhaz and South Ossetians who do not use Georgian passports. It condemns Russia’s violation of the ceasefire agreement, its refusal to extend the UN Mission Observer in Georgia, and the deployment of the Federal Security Service along administrative dividing lines, which prevents the EU Monitoring Mission from fulfilling its mandate.

By mentioning “Occupied Territories” in its title, the State Strategy gives no ground on recognition. Its preamble states that the goal of the State Strategy is to “reverse the process of annexation by the Russian Federation.”⁵ The State Strategy is a political text prepared for multiple audiences including hardliners in Georgia, directly affected parties in Abkhazia and South Ossetia, and the international community. While text of the State Strategy mirrors the legislative intent of the Law on Occupied Territories, the documents have different objectives. The State Strategy seeks to engage Abkhaz and South Ossetians, while the Law is punitive in seeking to isolate them.

Archil Gegeshidze, Senior Fellow of the Georgian Foundation for Strategic and International Studies, commends the State Strategy for “denying coercion and offering opportunities to engage in mutually beneficial projects.” But he believes “[i]t is badly packaged.” Gegeshidze notes, “The Strategy may impress the outside world but not the Abkhaz. Georgia needs to openly refrain from making claims on territory if it wants the Abkhaz to go along.” The State Strategy and subsequent Action Plan were rolled out with much fanfare.⁶

Abkhazia’s Economy

Abkhazia covers an area of 8,700 square kilometers.² According to the 1989 census, Abkhazia’s population was 525,000 people, of which Georgians represented 45.7% and ethnic Abkhaz 17.8%. Other groups included Armenians and Russians. After the 1992-93 conflict, however, Abkhazia’s current population decreased to about 180,000.⁷

In the 1980s, Abkhazia’s economy included 500 industrial enterprises, primarily power engineering and machine manufacturing.⁸ Gagra, with its beautiful white sand beaches, was a celebrated tourist destination. Other tourist spots included Sukhumi, Gudauta, Pitsunda, Lake Ritsa, and Novyi Afon, home to one of the world’s most beautiful and historic monasteries. After the 1992-93 conflict, Sukhumi’s hospitality industry virtually disappeared. Its storied seaside grew dilapidated, its coastline polluted, and infrastructure neglected.

Mild and sub-tropical, Abkhazia’s economy is seasonal with more than 200 sunny days each year. These conditions are ideal for citrus, tea, and tobacco, which occupy 40% of the land under cultivation. After the 1992-93 conflict, Abkhazia grew dependent on humanitarian assistance and subsistence farming. Accelerated by the CIS embargo (1996-2008), Abkhazia’s productive capacity collapsed. Industrial production decreased tenfold; underinvestment and neglect undermined Abkhazia’s transport and energy infrastructure. The Gali district and other parts of Eastern Abkhazia were deserted as ethnic Georgians were driven from their homes. Tea, citrus and tobacco production plummeted, and poaching depleted Abkhazia’s rich forests of its chestnut, oak, box, and yew stock.⁹ According to Abkhaz authorities, Abkhazia lost \$13 billion as a result of the conflict.

6. Interview by the author with Archil Gegeshidze at the Georgia Foundation for International Studies in Tbilisi, May 11, 2010.

7. *From War Economies to Peace Economies in the South Caucasus*. International Alert. 2004. Chapter 4: David Chkhartishvili, Roman Gotsiridze and Bessarion Kirsmarishvili, p. 123.

8. Butuzova, Lyudmila, and Roman Mukhametzhonov, “Abkhazia Revisited,” *Moscow News*, no. 36 (September 13, 2007).

9. Feyzba, Y. and O. Shamba. “National Economy of Abkhazia” (Alashara Publishers 2000).

3. “Cheney calls on west to rally behind Georgia,” *Financial Times*, September 5, 2008.

4. “IMF Mission Reaches Agreement in Principle on a US\$750 Million Stand-By Arrangement with Georgia,” *IMF*, September 3, 2008.

5. State Strategy on Occupied Territories: Engagement through Cooperation, 2010, p. 49.

Abkhazia's economy is currently rebounding. Russia is building roads, expanding the utility grid, and developing a water supply system. A new highway was recently completed between Sukhumi and southern Russia. Abkhazia has functioning ports: Sukhumi, Gagra, Gudauta and Ochamchira. Abkhazia's hospitality industry is expanding. Abkhazia is also developing natural resources, including coal from Tkvarchel. It is working with Rosneft to explore oil reserves. Logging and agro-industries involving hazelnuts, persimmons and viticulture, kiwi also have growth potential.¹⁰

Economic Cooperation

The GoG's State Strategy and Action Plan can potentially boost Abkhazia's economic recovery. Commercial contact can also serve as a tool for conflict mitigation, while laying the ground for long-term rapprochement between Georgians and Abkhazi. Russia would also benefit from regional economic development.

Current and historical examples exist of mutually beneficial economic activities for Georgians and Abkhaz including the Enguri Hydroelectric Power Station, which generates 1.3 million kw from the Inguri River and marks the administrative border of the conflict zone. The reservoir is located in Georgia while the plant and distribution transformer is in Abkhazia. 60% of the electricity goes to Georgia with the balance transmitted to Abkhazia.

The Khudoni Dam and Hydro Station is located 40 km upriver from the Inguri Dam. Started in the 1980s by the Soviets, construction is about 30% complete. Finishing construction will cost \$2 billion. Given the site location and the development of Georgia's high voltage transmission system, generated electricity could be transmitted to Krasnodarsky Krai, a region in Russia with Sochi as its largest city, or to Turkey.

Black Sea Infrastructure Development proposes the Enguri Sand and Gravel Export Project, which will dredge the dry-bed of the Inguri River 62 km from Anaklia and 40 km upstream from the Khudoni site. Up to 500 million cubic meters of product will be immediately loaded onto barges and transported downriver, bound for markets across the Black Sea where gravel for cement is urgently required.

Suitcase trade of commodities and agricultural goods is conducted by many of the 1,800 persons who cross the Enguri River each day. Medical equipment and pharmaceuticals are also procured in Georgia for sale in Abkhazia. As a member of the World Trade Organization

(WTO), Georgian imports goods at a much lower cost than Russia does making Georgian-origin products less costly. Agro-enterprise activities have involved tea, tomatoes, citrus and apple products, and hazelnuts.

There are many examples of commercial contact as a tool for conflict mitigation: the Southeast Europe Economic Cooperation Initiative promoted stability after Yugoslavia's breakup. The Greek-Turkish Business Forum catalyzed bilateral agreements on trade, tourism, maritime and environmental issues. And trade between China and Taiwan has helped reduce tension across the Taiwan Straits.

Sochi Olympics

The 2014 Sochi Olympics, just 35 km from Abkhazia, represent another opportunity for economic cooperation benefiting Georgians and Abkhaz, as well as Russia. The Games are in serious trouble due to construction delays and cost overruns. Originally budgeted at \$8-13 billion, the current cost is estimated at \$37 billion.

There are serious obstacles to building facilities for the Games. Since the Sochi area lacks raw materials, barges are bringing sand and gravel from Turkey. Russia has tried to build a port at Sochi, but has encountered engineering difficulties. Even when raw materials are available, laborers are in short supply. Abkhaz are concerned about the surge of up to 50,000 foreign workers, who will be employed to build the Olympic Village and related facilities. They are also worried about the ecological impact of a huge Russian cement plant under consideration for Abkhazia at a cost of \$170 million.¹¹

Transport and hospitality infrastructure are also major problems. Sochi also lacks a major airport. Russia hopes to use Sukhumi's Babushera Airport as a transport hub. However, the GoG has protested to the International Civil Aviation Organization. Facing a crisis in hotel capacity, Russia wrote the International Olympic Committee to propose that athletes stay on boats in the Black Sea.

Civic Initiatives

People-to-people activities – also called “track two activities” – represent a form of cooperation engaging business representatives and other non-governmental actors. People-to-people activities create space for civic engagement while building bridges through practical forms of cooperation that, based on dialogue and joint analysis, derive mutual benefit. They can also help transform conflict conditions through confidence building

10. Beslan Baratelia. “Economic Development of Disadvantaged Areas of Abkhazia.” *Georgian and Abkhaz Perspectives on Human Security and Development in Conflict Related Areas*. CIPax. Toledo International Center for Peace. May 2009. pp. 77-82.

11. International Crisis Group. “Abkhazia: Deepening Dependence.” February 26, 2010, p. 8.

by reducing misperceptions and combating negative stereotypes that undermine mutual understanding. People-to-people activities are not a substitute for official diplomacy, but they can change the climate in which diplomatic efforts occur. They can also add value by developing innovative policy initiatives based on common approaches to shared problems.¹²

Track two activities involving Georgians and Abkhaz are constrained by bitterness and distrust. They also suffer from inadequate resources, as well as failures by both the Georgian and Abkhaz sides to create a permissive environment for interaction. Abkhaz especially oppose activities that can be manipulated to advance Georgia's goal of reintegration. Abkhaz civil society representatives believe that the GoG's current engagement strategy is too politicized and has little chance of occurring. They prefer regional frameworks for cooperation on business and environmental issues such as the Caucasian Forum on Provincial Cities in the South Caucasus.¹³

Going forward, the GoG is exploring innovative ways to facilitate freedom of movement. It plans to offer laissez-passer travel documents and identification cards to Abkhaz. That could make travel easier and allow Abkhaz to benefit from social services available in Georgia, such as health care and education, which are of higher quality and lower cost than in Abkhazia. The GoG also hopes that social interaction will help reduce tensions and set the stage for rapprochement over the long-term.

Abkhaz Perspective

This section of the article describes Abkhaz perspectives. It is based on the author's meetings in Sukhumi with Abkhaz authorities, members of parliament, and civil society. While the author does not necessarily associate himself with the statements in this section, they are provided so that the reader may have a fuller understanding of the divergent views of Georgians and Abkhaz.

Abkhaz authorities, including Prime Minister Sergei Shamba, have many grievances. Most of all, they deeply resent Georgia's Law on Occupied Territories. Shamba maintains that the GoG rejects "new realities." He complains about Georgia's efforts to block air, land, and sea access, and its lobbying of Western countries to prevent visas from being issued to Abkhaz with Russian passports. Abkhaz are also upset by the GoG's efforts to

disrupt commercial contacts citing its undermining of deals with Nokia and Benetton.

In addition to the Law on Occupied Territories, Abkhaz authorities criticize the State Strategy for referring to "occupied territories, de-occupation and non-recognition." According to Shamba, the State Strategy is "a device to bring Abkhazia back to Georgia." Nadir Bitieff, the National Security Adviser, maintains: "If Abkhazia is built and then decides to rejoin Georgia, so be it. But that won't happen. It's too late."

They dismiss confidence-building measures as "unrealistic." Deep distrust between Georgians and Abkhaz is rooted in historical memory. According to Shamba, "We barely survived. Georgians stole everything – cars, factory equipment, furniture in houses – after attacking us in 1992." Abkhaz authorities want an agreement with the GoG on the non-use of force as a first step to restoring trust. The GoG rejects Abkhaz overtures; it believes that entering into an agreement with the Abkhaz authorities would imply recognition. Instead, the GoG offers to sign a non-aggression pact with Russia, but only after Russian troops withdraw from occupied territories.

Regarding Russia's role, Shamba adds: "Why engage [with Georgia] when we have a strategic partnership with great and huge Russia? We are ready for relations with all countries except Georgia."¹⁴ He points out, "By isolating us, the international community creates the situation where we are dependent on Russia and then criticizes us for being a puppet regime."

Shamba welcomes the "breathing space" provided by Russian troops. "The constant threat of war forced us to spend all our resources on security. Now people have confidence for the future. They know aggression will be prevented." He describes the Russian presence as an economic opportunity. "Help, tourists, television all come from Russia." Regarding "bilateral agreements" allowing Russian bases in Abkhazia, "We had very tough arguments with Russia and always tried to defend our national interests." He adds wryly, "We have a long history of fighting foreign domination. Maybe that is why there are only 100,000 of us."

Batal Tabagua, head of the Central Election Commission, represents Abkhaz hardliners with deep antipathy towards the West. "The United States is our main enemy," he says; "Everybody is afraid of the U.S., so it thinks it can do what it wants. It threatens countries that want to recognize us." Shamba tries to temper

12. This paragraph draws on "Confidence building and the role of civil society as a key element for conflict resolution" by Jonathan Cohen. Conciliation Resources. January 2010.

13. Interview by the author with Liana Kerchiela in Sukhumi, May 11, 2010.

14. Abkhaz perspectives are drawn primarily from interviews with Prime Minister Sergei Shamba in Sukhumi on May 11 and 12, 2010. Other persons interviewed include Nadir Bitieff (Adviser to the President), Maxim Gunjia (Deputy Foreign Minister), Batal Tabagua (Head, Central Election Commission), the Chairman of the Abkhaz Parliament's Defense Committee, and NGO representatives associated with the Center on Humanitarian Issues.

Tabagua's comments adding, "There is no hatred at the societal level. We have very good attitudes towards the American people and culture."

Turkey is seen as both an alternative and additional partner to Russia. Turks currently come to Abkhazia via Sochi. Abkhaz authorities want direct ferry service between Trabzon and Sukhumi. Shamba plans to set up a special ministry to encourage repatriation of the Abkhaz Diaspora from Turkey. He wants to replicate Israel's "Aliyah" policy. Abkhaz authorities also plan to study how other non-recognized states have gained credibility by opening trade and cultural liaison offices.

Abkhaz feel that time is on their side; they believe that international recognition is inevitable. Bitieff acknowledges that communications are the key to better understanding. "We want Georgia to recognize us. That would allow refugees to come home or get compensated." He also believes that normalizing relations with Georgia would be a boon for business. "The more money comes, the stronger our civil society." With pride he adds, "It's more free here [than in Georgia]. Abkhazia is an open society that wants to interact with the world. Georgian society is more like Russia's — Bolshevik and imperial."

Stakeholders

Opportunities for cooperation between Georgians and Abkhaz require the encouragement of major stakeholders whose interests are affected by developments in Georgia and the South Caucasus.

The United States

Affinity between Georgia and the United States goes back to the period when Eduard Shevardnadze served as the Soviet Union's foreign minister. Shevardnadze attained iconic status in the West for his pivotal role managing the dissolution of the USSR, as well as negotiating German reunification. Shevardnadze served as head of state from 1995 to 2003. Under his leadership, Georgia steered a pro-Western course, becoming both ally and friend of the United States.

Georgia's location makes it an important trans-Eurasia energy transit country. The East-West Corridor transports vital oil and natural gas supplies from the Caspian via Georgia to Western markets. The Baku-Tbilisi-Ceyhan pipeline cost \$3.5 billion and now delivers a million barrels of oil each day to Western markets. The South Caucasus gas pipeline, which follows the same route, and the smaller Baku-Tbilisi-Supsa line are other Caspian pipelines not under Russia's control. Estimated to cost \$12 billion, the Nabucco pipeline will expand trans-Caspian projects by transporting natural gas from Azerbaijan and Turkmenistan through Georgia to Turkey. These supply routes are essential to diversifying energy sources for consumers in the West.

Georgia emerged as a high-value ally after the events of September 11, 2001. President George W. Bush and Saakashvili developed a close personal relationship based on shared values and Georgia's support of Bush's war on terror. Saakashvili embraced liberal democracy after the "Rose Revolution of 2003." Representing the possibility of a democratic post-Soviet state outside of the Baltics, Bush heralded Georgia as a beacon of democracy.

Since 2007, however, Georgia has struggled to consolidate its democratic development. Addressing Georgia's parliament, Vice President Joseph R. Biden, Jr. called for "significant, concrete steps that need to be taken to deepen democracy." He added, "Your Rose Revolution will only be complete when government is transparent, accountable, and fully participatory; when issues are debated within this chamber, not on the streets; when you fully address constitutional issues regarding the balance of power between the parliament and the executive branch, and leveling your electoral playing field; when the media is totally independent and professional, provide people with the information to make informed decisions, and to hold their government accountable for the decisions it makes; [and] when the courts are free from outside influence and the rule of law is firmly established."¹⁵

Regarding security cooperation, the Pentagon launched a Train and Equip Program to enhance Georgia's counter-terrorism capabilities in April 2002. Georgia was one of the first countries to join the multinational force in Iraq. The United States led efforts to establish the Partnership for Peace Program between NATO and Georgia. The Bush administration also championed Georgia's NATO membership. A decision on MAP for Georgia was deferred at NATO's Bucharest Summit on April 4, 2008. However, the final communiqué affirmed, "We agreed today that these countries [Georgia and Ukraine] will become members of NATO."

Though the Obama administration continues security cooperation with the GoG, it declined Georgia's request for assistance in rearming after the 2008 War. Instead, it is working with the GoG to modernize its military, focusing on training, planning, and organization of Georgian forces to be deployed in Afghanistan.¹⁶ In response to President Barack Obama's appeal for more forces in Afghanistan, Georgia pledged approximately 1,000 troops. The southern line of the Northern Distribution Network supplying troops in Afghanistan runs through Georgia. The GoG also provides over-flight rights to NATO. Adopted in 2009, the "U.S.-Georgia

15. Remarks by Vice President Joseph Biden to the Georgian Parliament, July 23, 2009.

16. Cory Welt. "How Strategic is the US-Georgia Strategic Partnership?" Presented at the Harriman Institute, Columbia University. March 11, 2010, p. 2.

Charter on Strategic Partnership” affirms support for Georgia’s “legitimate security and defense needs” as well as “regional peace and stability.” It does not, however, provide a U.S. security guarantee.¹⁷

U.S.-Russia relations have rebounded since their low point during the Bush administration. Pressing the “reset button” has enabled the U.S. and Russia to work more effectively together on a range of issues, including non-proliferation as well as multilateral initiatives before the UN Security Council. The Strategic Arms Reduction Treaty was signed on April 8, 2010. A new cooperative approach to Russia was announced at NATO’s Lisbon meeting in November 2010. To assuage the GoG’s concerns, U.S. officials affirm that rapprochement with Russia does not come at Georgia’s expense. According to Biden, “We stand against the 19th century notion of spheres of influence ... We will not recognize Abkhazia and South Ossetia as independent states. And we urge the world not to recognize them as independent states. We call upon Russia to honor its international commitments clearly specified in the August 12 ceasefire agreement, including withdrawal of forces to their pre-conflict positions, and ultimately out of Georgia.”¹⁸

While the strategic partnership between Georgia and the U.S. endures, today’s relations are more straightforward and based on strategic objectives. These include preventing conflict between Russia and Georgia that would put the U.S. in a position of having to take sides.

Russia

After recognizing Abkhazia, Russia signed a “bilateral military cooperation agreement” with Abkhazia formalizing the deployment of 3,800 Russian troops and 1,000 FSB members on the administrative border.¹⁹ In addition, Russia and the Abkhaz authorities signed a 49-year lease for the naval base at Ochamchira, where naval/coast guard forces will be stationed, and for the Bombora Air Base near Gudauta where 1,700 troops will be posted. Beginning in August 2009, the Sevastopol-based Russian Navy started patrolling the Black Sea to prevent Georgian Coast Guard vessels from interdicting Turkish ships. Russia deployed sophisticated S-300 missiles to Abkhazia on the two-year anniversary of the war, which further heightened tensions.

On his first post-war trip to Abkhazia, Putin pledged \$470 million to support the Russian armed forces in Abkhazia and reinforce the administrative dividing line at the Enguri River. Putin also announced \$340 million for

social support and as stimulus for the Abkhaz economy, including \$65 million in direct budgetary support in 2009 and a slightly higher amount in 2010. In addition, Russia agreed to pay \$17 million in pensions to Abkhaz holding Russian passports.²⁰ Russia’s assistance came at a time when its economy is adversely affected by the global economic crisis and declining energy prices.

Russia is a dominant force in Abkhazia’s economy. Approximately 80% of all goods consumed in Abkhazia come from Russia.²¹ Russia is financing the set-up of Abkhazia’s banking system.

Russia’s state railway is leasing the Abkhaz railroad. Negotiations are underway for Russia to assume operation of the airport and a port near Sukhumi.²² Major Russian television stations are broadcast in Abkhazia and Internet access in Abkhazia is provided via Russian Internet service providers. Prominent Russians have acquired properties on the Black Sea coast, including the oligarch Oleg Deripaska and Moscow’s Mayor Yuri Luzhkov, who built a mansion on a spectacular bluff in Gagra.

Though Abkhaz welcome their strategic partnership with Russia, they also have a long history of resisting Russian imperialism. Abkhaz want independence. They do not want to be assimilated or annexed by Russia. The Russian State Duma passed a resolution on February 17, 2010 heralding “the 200th anniversary of Russia’s patronage over Abkhazia.”²³

Russia’s relations with Georgia remain tense and acrimonious. Though Georgia and Russia severed diplomatic relations after the 2008 War, each maintains an interests section at the Swiss embassies in Moscow and Tbilisi. The GoG maintains it cannot resume relations until Russia abides by ceasefire commitments. Russia’s disparaging of Saakashvili further impedes resuming relations. The GoG adamantly insists that it will not agree to restore full diplomatic or consular relations until Russia rescinds its recognition of Abkhazia and South Ossetia and withdraws troops from these territories. The GoG believes that normalizing relations would send the wrong signal to countries it is lobbying to hold the line on non-recognition. According to Medvedev, Russia will eventually restore relations with Georgia, but not until Saakashvili leaves office.²⁴ Georgia and Russia are at loggerheads; Moscow has no intention to compromise.

17. Ibid.

18. Remarks by Vice President Joe Biden to the Georgian Parliament, July 23, 2009.

19. Ibid.

20. International Crisis Group. “Abkhazia: Deepening Dependence.” February 26, 2010, p. 6.

21. Ibid.

22. Isabel Gorst. “Moscow Tightens Grip on Abkhazia.” FT.com. February 17, 2010.

23. Radio Free Europe/Radio Liberty. February 17, 2010, www.rferl.org/content/Russia_Gains_Military_Base_In_Abkhazia/196545.html.

24. Isabel Gorst. “Moscow Tightens Grip on Abkhazia.” FT.com. February 17, 2010.

Despite acrimony, Russia remains a major investor in Georgia. Most Georgians want the GoG to take a more business-like approach towards Russia. A public opinion poll on April 11-26, 2010 found that 52% of those surveyed disapprove of Georgia's current policy towards Russia; 82% support a resumption of direct flights between Tbilisi and Moscow.²⁵

Turkey

Turkey has extensive ties to both Russia and Georgia. As part of Turkey's "Zero Problems with Neighbors Policy," President Abdullah Gül visited Moscow and Tbilisi several times in 2010 to mediate a rapprochement. Though Turkey's proposal for a South Caucasus Stability Pact floundered, Turkey believes it is well positioned to act as mediator given its close ties with each.

Medvedev and Gül signed 17 cooperation agreements including an agreement on nuclear power on May 12, 2010. As a result, bilateral trade volume currently valued at \$30 billion is expected to surpass \$100 billion. Most of the increase will come from the energy sector via a pipeline from Samsun on the Black Sea to Ceyhan on the Mediterranean. "South Stream" further consolidates Russia's energy influence in Eurasia advancing one of Moscow's strategic objectives: an outlet to the Mediterranean via Turkey.

Turkish construction workers are employed across Russia, and Turkish construction companies were contracted to build Russia's military bases in Abkhazia. The Trabzon-Sochi maritime link is important commercially. About 5.5 million Russian tourists visit Turkey each year; tourism will increase with plans to lift visa requirements for visits of less than a month.²⁶

Georgia is Turkey's window to the Caucasus and the Caspian countries. Turkish hubs on the Black Sea coast are linked to Batumi in Ajara, a former Ottoman province now serving as the primary East-West route from Turkey to Central Asia. Turkey is one of Georgia's top trading partners. Trade volume was \$1 billion in 2009. Turkey ranks second in Foreign Direct Investment valued at \$165 million in 2008. Turkey is Georgia's largest export market, accounting for 17.6% of exports in 2008. The value of goods imported from Turkey by Georgia is 14.9% of total imports.²⁷ The two countries signed a Free Trade Agreement and cooperate militarily via weapons sales from Turkey to Georgia and training of Georgian military personnel.

In addition, Turkish freighters supplied Sukhumi despite efforts by Georgia's Coast Guard to impose

a maritime blockage. Under the Law on Occupied Territories, the Georgian Coast Guard arrested three ships by mid-2009 carrying goods between Turkey and Abkhazia.²⁸ At least 300,000 ethnic Abkhaz, even more ethnic Georgians, and untold numbers of North Caucasians (mostly Circassians) live in Turkey.²⁹ As a result of this diaspora, Turkey is Abkhazia's second largest trading partner behind Russia.

European Union

Georgia currently participates in the EU's Eastern Partnership Initiative (as does Ukraine, Armenia, Azerbaijan, Moldova and Belarus). Georgian passport holders benefit from a Visa Facilitation Regime with the EU. A Visa Liberalization Dialogue is also underway. Georgia also enjoys GSP+ (General System of Preferences), allowing it to export without tax or quota to EU Member States.

Additionally, Georgia is negotiating a Comprehensive Free Trade Agreement with the EU. Its advantages are mostly political, sending a positive signal to international financial institutions and private investors. In May, the EC issued a directive allowing the start of negotiations on a Stabilization and Association Agreement (SAA) for all countries in the South Caucasus "when conditions are correct." Georgia is at the head of the queue.

Russia resents the EU's involvement in Georgia and its staunch non-recognition policy towards Abkhazia and South Ossetia. Russia impeded deployment of the EU Monitoring Mission with FSB forces. The EU also participates diplomatically as a co-chair of the Geneva process. Russia is suspicious of the EU. It sees the Eastern Partnership Initiative as a way of weaning countries from its influence. If Georgia gets an SAA, then Russia's efforts to assert control over its near abroad will be further undermined.

Recommendations

This article presents a hopeful, yet steely-eyed view of the situation. Collaborative activities can only go forward with concurrence by the GoG and Abkhaz authorities. Commercial contact will not occur in the current climate unless both sides make a strategic decision that it is in their interests to allow it.

Georgia's State Strategy and Action Plan embody the right approach. Engagement addresses immediate basic human needs, while potentially reducing tensions. It can also potentially diminish the distrust and acrimony that pervades relations between Georgians and Abkhaz, thereby setting the stage for long-term rapprochement.

25. "Poll Shows Decrease in Support for NATO Membership." *The Georgian Times*. May 10, 2010, p. 4.

26. Sebnem Arsu, "Turkey's Pact With Russia Will Give It Nuclear Plant," *The New York Times*, May 13, 2010, p. A12.

27. CIA Factbook 2008.

28. "Turkey May Help Abkhazia Reintegrate With Georgia Through Direct Trade," *The Georgian Times*, May 10, 2010, p. 6.

29. *Milliyet* "Unlu Portreler," January 18, 1996.

Practical benefits of the State Strategy can be maximized by depoliticizing it and by emphasizing regional cooperation.

Engagement must take into account intractable, core positions on all sides. Georgia wants to engage without legitimizing the Abkhaz authorities or seeming to support Abkhazia's goal of independence. Abkhaz will only engage if engagement does not undermine their goal to gain greater global recognition as an independent and sovereign State. Progress requires a flexible, long-term and realistic approach. It must be based on the GoG's recognition that Georgia's interests are best served when Abkhaz prosper via commercial contact with Georgians as well as through regional links in the Caucasus and with littoral states of the Black Sea. The GoG is adamant about non-recognition. Therefore, it will only pursue this course if it believes that infrastructure and regional economic development do not advance recognition efforts by the Abkhaz authorities.

Russia is indispensable to Abkhazia. It provides security, funds, and access. While Abkhaz recognize Russia's indispensable role, they are wary of being annexed by Russia or having their identity overwhelmed by Russians. It is in the interest of both Georgia and Abkhaz to strengthen Abkhazia, thereby reducing the possibility of absorption by Russia. A self-confident and empowered Abkhazia may be more willing to discuss some kind of association with Georgia in the future.

There is not a lot of common ground. The delicate balance between Georgian and Abkhaz interests could easily be upset without gradual and carefully calibrated steps that benefit all parties, including Russia. Even when everyone benefits, there is a question that hangs over cooperation between Georgians and Abkhaz: does Russia have incentive to allow it?

Business proposals

Business is the common language. There are several opportunities with the potential to derive mutual benefit. Most noteworthy is the Inguri Sand and Gravel Export Project (and related activities). This private sector initiative can be launched immediately as a win-win for Georgia, Abkhazia, and Russia.

Pending negotiations and agreement with affected parties, the Project will produce raw material urgently needed by Russia for construction of the Olympic facilities. Abkhaz will receive royalties in exchange for guaranteeing security and safe passage of barges down the Inguri to the Black Sea. Georgia will benefit from the upgrading of roads, railways, and nearby bridges by the developer. In addition to creating 250 jobs, the Project also presents an opportunity for tourism and agro-industries.

This article proposes an enterprise called "Black Sea Resorts," which would build and operate a hotel, gaming and recreational facility at the site. As part of its cruise and tourism package, Black Sea Resorts would also develop facilities in Western Georgia and Russia, including locations that could be used for the Sochi Olympics.

Bridges and infrastructure at the dredging site will facilitate commercial contact between Georgians and Abkhaz. Restoring tea plantations in Gali and setting up a tea collection and processing center on the east side of the Inguri would facilitate interaction. The same model could be explored for other agro-industries linking Georgians and Abkhaz (e.g. hazelnuts, tomatoes, citrus, and apple products). In addition, it would be desirable to establish the equivalent of a free trade zone near the project site where other commodities, machinery, and equipment could be sold.

The Project's realization would be a cause for celebration. On this occasion, Yevgeny Yevtushenko could participate in a collaborative cultural event such as a "poetry concert" for an audience of Georgians and Abkhaz. Yevtushenko is revered as an artist and moral icon by Georgians and Abkhaz alike. Now 80 years old, he has ties to Abkhazia, where he kept a home that was destroyed during the 1992-93 conflict.

Policy Proposals

The following policy proposals promote contact between Abkhazia and the international community, including Georgia.

- Upgrade the Action Plan: The donor community can assist by establishing an "Action Plan Affinity Group" offering resources to private sector initiatives in the form of project financing, loan guarantees, risk insurance, and grants for worker training and other benefits. The Action Plan can best be achieved through a more relaxed regulatory environment which calibrates modifications in the Law on Occupied Territories with Sukhumi's cooperation. Without a quid pro quo, the United States could provide Georgia with a Free Trade Agreement as incentive to modify the Law on Occupied Territories.
- Empower the Coordinating Commission: A reliable communications and liaison channel exchanging information and assisting project development is essential to implementing the Action Plan. Led by a Special Representative on Shared Interests, the Coordinating Commission should have the tacit approval of both the GoG and Abkhaz authorities. However, it must not accept funds from either side lest financing

from one compromise its credibility with the other. The cost of staff and facilities should be fully covered by a member of the international donor community, such as the EU, that has experience funding activities in Abkhazia. To ensure the Commission's independence, it could be established under UN auspices.

- Enhance freedom of movement: It would be best if the Abkhaz authorities had “no objection” when Abkhaz travel in Georgia or internationally using laissez-passer documents issued by the GoG. If they do object, the GoG needs a fallback position: allow mutual recognition of civil documents, such as birth certificates, driving licenses, and professional degrees, to allow freedom of movement and facilitate commercial contact between Abkhaz and Georgians, including those displaced by the conflict.
- Reduce the isolation of Abkhaz: Civil society interaction can identify practical areas for cooperation, thereby building confidence. Donor funds should be allocated to dialogue initiatives engaging Georgians and Abkhaz. In addition, the U.S. can help connect Abkhaz civil society with the international community via existing Fulbright scholarships, IREX university exchanges, and participation in the State Department's International Visitors Program. Abkhazia's isolation would be further reduced through the participation of civil society representatives in the “Forum on Provincial Cities in the South Caucasus.”
- Expand Turkey's role: The GoG should waive customs requirements for Turkish cargo ships putting into Abkhaz ports. Rather than requiring them to dock first in Poti or Batumi, a notification protocol could be developed informing the GoG of their cargo and route. Links between Turks and Abkhaz would also be enhanced by developing a direct land route from Turkey to the Gali region, as well as via restoration of the Vesyloloye-Sukhumi railway linking Russia, Abkhazia, and other parts of Georgia. Opening commercial ferry service between Sukhumi and Trabzon would stimulate trade and tourism. Ankara should assure the GoG that direct contact between Turks and Abkhaz does not represent a process of “creeping recognition.”

Conclusion

It would be wrong to underestimate Russia's role in fomenting conflict and sustaining divisions. But just as Russia is a source of the problem, it can also contribute to progress. Improved Georgia-Abkhaz relations can be

achieved by improving relations between Georgia and Russia.

The GoG currently rejects cooperation until Russia rescinds recognition of Abkhazia and South Ossetia, and withdraws forces from occupied territories. The GoG would be best served through a non-confrontational approach. It should not let its national pride interfere with its national interests. When Russia lifts its boycott of Georgian water, wine and other goods, Georgia should support Russia's membership in the WTO. Russia's membership is also in Georgia's interest as it will require Russia to abide by WTO regulations and provide a forum to redress trade embargos. Resuming direct flights between Tbilisi and Moscow would be a step towards normal travel and trade relations between Georgia and Russia.

As Georgia's strong supporter, the United States is best placed to counsel Georgia on ways to mitigate conflict and move forward. More than “strategic patience,” the United States should proactively promote peace and progress in Georgia and the region. Anything less could be interpreted as abandoning Georgia to Russia's sphere of influence, which would be detrimental to both Georgia and the United States.

David L. Phillips serves a member of the Harriman Institute's National Advisory Board and was co-director of Harriman's Study group on U.S.-Russia and Georgian Relations from 2008 to 2009. Currently he is Director of the Program on Peace-building and Human Rights at Columbia University's Institute for the Study of Human Rights and a Fellow at Harvard University's Future of Diplomacy Project. Phillips has worked as a senior adviser to the United Nations Secretariat and as a foreign affairs expert and senior adviser to the U.S. Department of State. Phillips has been extensively engaged in the Southern Caucasus for almost 20 years. This article draws from a recent report by the author for the National Committee on American Foreign Policy – “Peacebuilding and Business: Fostering Commercial Interaction between Georgians and Abkhaz.”