

Russian Military Expenditures: What's Behind the Curtain?

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Abstract

This paper views the Russian defence budget as a representation of national strategic interests, priorities, and policies. Full achievement of these impressive goals is hindered by the budget's inherent properties as discussed in this paper. Although Russia conforms to the United Nations statistical standard for reporting military expenditures, several budgeting categories are hidden in other parts of the federal budget. Transparency in defence spending has been decreasing steadily. The budgeting process itself is cumbersome and opaque. Parliamentary control over the budgeting process and control over execution of defence appropriations are limited. Importantly, frequent changes in the system of national accounting impede valid historical comparisons. The study finds that the low quality of defence management dominated by military-industrial complex is a major problem locking the Russian defence policy in an institutional trap.

Key words: *budgeting, defence spending, institutional trap, military-industrial complex, military reform*

1. Introduction

Military budgets as “a visible manifestation of national strategic intentions, priorities, and policies” (Crane *et al*, 2005:91) are still worthy objects for study and monitoring them over time.

In the Cold War era Western economists devoted serious attention to Soviet economy in general and to Soviet military expenditures in particular. The validity of these efforts is quite obvious but their effect in the last case was mostly contradictory and some times disappointing (Rosefielde, 2005). There is still very little known about past military expenditures in terms of real statistics (Harrison,

2003). Contrary to that of Soviet's contemporary Russia's military expenditures can not boast of such attention with few exceptions (Fontanel, 2003). At the same time the United Nations (UN), the International Monetary Fund (IMF), the North Atlantic Treaty Organization (NATO), the Stockholm International Peace Research Institute (SIPRI), and the International Institute for Strategic Studies (IISS) continue to monitor this subject.

Inside Russia military expenditures are usually disregarded by economists and owing to the fact often do not receive close scrutiny. Trying to break this tradition the Moscow-based Institute for the Economy in Transition (IET) acting as an independent research body and a civil society organization has begun to publish each year since 2000 in its *Russian economy trends and outlooks* yearbook own estimates of Russian military expenditures.

This paper presents an analysis of Russia's current practice in this field based on the experience accumulated by IET. The paper focuses first on Russian military expenditures since 1999 with emphasis on current budget year. Then are considered underlying budgeting process, defence planning, and other institutional factors. Finally I review some prospects for the future announced by high-ranking Russian officials and propose own explanation of observed phenomena.

2. Russian Military Expenditures

2.1. Definition of military expenditures

The definition of military expenditures used by IET is based on a framework proposed in *United Nations Standardized Instrument for Reporting Military Expenditures* (United Nations, 2002) and resembles those developed for Argentina and Chile with UN support (CEPAL, 2005). Military expenditures are evaluated using as a base the functional classification of Russia's federal budget according to annual *Federal Budget Law* (budgetary allocation) and *Federal Budget Execution Law* (actual outlays).

The main part of military expenditures is concentrated in budgetary functional division *National Defence* and covers country's spending on its Armed Forces (military and civilian personnel less the retirement pensions; operations and maintenance; procurement; military construction; research and development) and military atomic program. This amount being formally linked to above-mentioned functional division is regarded as defence (or direct military) expenditures and labelled for further use as **DefEx**.

Then on this base is estimated the first aggregate of military expenditures labelled as **MilEx1** by means of addition indirect military spending from budgetary division *National Security and Law Enforcement Activity* on: Interior Troops of the Ministry of Interior, security bodies, and Border Service. From other divisions are included expenses on civil defence and Civil Defence Troops, special construction, and preparation for mobilization of the economy. As a result of that

the amount is close to G_1 measure (CEPAL, 2005). The second aggregate of military expenditure (**MilEx2**) is estimated by adding expenses connected with former military activity, namely on retirement pensions for military personnel and appropriate part of State's Housing Program, under which retired military are provided with dwelling. The **MilEx2** aggregate is an analog of G_2 measure (CEPAL, 2005).

2.2. Spending dynamics on short run

Defined by IET in that way Russia's military expenditures were used for generation of uniform time-series for years 1999–2004, which are shown in Table 1.

Table 1: Russia's Military Expenditures (allocations), billions current roubles

	1999	2000	2001	2002	2003	2004
DefEx	93.7	209.4	214.7	284.2	354.9	427.4
MilEx1	128.9	270.4	283.4	353.1	456.5	544.5
MilEx2	144.0	304.6	329.6	455.6	594.6	630.7

Notwithstanding well known limited value in comparing the military expenditures of different countries (Brzoska, 1981) the data of the Table 1 being converted in current US dollars using purchasing power parity (Rosstat, 2006) are shown in Table 2.

Table 2: Russia's Military Expenditures (allocations), current \$ billions

	1999	2000	2001	2002	2003	2004
DefEx	17.7	29.3	26.2	30.7	34.1	35.9
MilEx1	24.4	37.8	34.6	38.1	43.9	45.8
MilEx2	27.2	42.6	40.2	49.2	57.1	53.0

The same time-series as in Table 1 but in billions constant roubles (1999) applying GDP deflator (Rosstat, 2006) are presented in Table 3.

Table 3: Russia's Military Expenditures (allocations), billions constant roubles

	1999	2000	2001	2002	2003	2004
DefEx	93.7	152.2	133.9	153.5	168.6	171.2
MilEx1	128.9	196.5	176.8	190.7	216.9	218.1
MilEx2	144.0	221.4	205.6	246.1	282.5	252.6

Of course, what matters are not allocations but actual outlays. The task of estimating appropriate time-series was complicated by the fact that data about execution of federal budget by law are available in contemporary Russia only in 25 months after its passage. Therefore in Table 4 are shown only **DefEx**-connected data.

Table 4: Russia's Defence Expenditures (actual outlays)

	1999	2000	2001	2002	2003	2004
DefEx , bln current roubles	115.6	191.7	247.7	295.4	355.7	430.0
<i>DefEx outlays overrun</i>	23.4%	-8.5%	15.4%	4.0%	0.2%	0.6%
<i>Total federal outlays overrun</i>	16.0%	1.5%	10.8%	5.5%	-2.3%	-2.5%
DefEx , bln constant roubles	115.6	139.3	154.5	159.5	169.0	172.2
<i>DefEx growth (1999 = 100)</i>	100.0	120.5	133.7	138.0	146.2	149.0
<i>DefEx annual variation</i>	—	20.5%	10.9%	3.2%	5.9%	1.9%

The ratio of military expenditures to GDP forms an indicator known as defence burden, which permits a deeper analysis and understanding in defence management. Defence burden for corresponding time-series from Tables 1 is calculated using refined by Rosstat's GDP-data (Rosstat, 2006) and presented in Table 5. Here again actual outlays are more appropriate therefore as first line of the Table 5 are shown results from division of **DefEx** in billions current roubles from Table 4 by corresponding GDP values.

Table 5: Russia's Defence Burden, % GDP

	1999	2000	2001	2002	2003	2004
DefEx, actual	2.40	2.62	2.77	2.73	2.69	2.57
DefEx, allocations	1.94	2.87	2.40	2.62	2.68	2.55
MilEx1, allocations	2.67	3.70	3.17	3.26	3.45	3.25
MilEx2, allocations	2.99	4.17	3.69	4.21	4.49	3.76

2.3. Current military expenditures

Unfortunately, by changing its budgetary functional classification since 2005 according to the Classification of the Functions of Government (COFOG) from UN's System of National Accounts the government of Russian Federation has "spoiled" the uniformity of observed time-series. Now civilian-type expenditures of the Ministry of Defence are excluded from division *National Defence* and transferred to other ("peaceful") divisions, producing for them some unexpected (from the standpoint of economics) effect, which will be described further. Although this shifts the **MilEx2** definition used by IET closer to that used by NATO (Brauer, 2004).

Simultaneously with the switching to the new budget classification in the 2005 federal budget there was carried out a further consolidation of military expenditures in division *National Defence*, which included the expenditures for the implementation of the programs of international military technical cooperation and preparation for mobilization of the economy. Moreover, in the structure of expenditures pertaining to this division there were shown two new subdivisions:

Applied Research in the Area of National defence and Other Issues in the Area of National Defence.

The military expenditures time-series for years 2005–2006 and transferred civilian-type aggregate estimates are shown in Tables 6–7.

Table 6: Russia's Military Expenditures in 2005–2006

	2005	2006
1	2	3
DefEx , allocations, bln current roubles	578.4	666.0
MilEx1 , allocations, bln current roubles	752.2	880.0
MilEx2 , allocations, bln current roubles	909.2	1 037.7
DefEx , allocations, bln current \$	44.2	46.4
MilEx1 , allocations, bln current \$	57.5	61.4
MilEx2 , allocations, bln current \$	69.5	72.4
DefEx , allocations, bln constant (1999) roubles	193.5	184.5
MilEx1 , allocations, bln constant (1999) roubles	251.7	243.8
MilEx2 , allocations, bln constant (1999) roubles	304.2	287.4
DefEx , actual outlays, bln current roubles	581.1	—
<i>DefEx outlays overrun</i>	0.5%	—
<i>Total federal outlays overrun</i>	–0.8%	—

Table 6 continued

1	2	3
DefEx , actual outlays, bln constant (1999) roubles	194.5	—
<i>DefEx growth (1999 = 100)</i>	168.2	—
<i>DefEx annual variation</i>	12.9%	—
DefEx burden , actual outlays, % GDP	2.69%	—
DefEx burden , allocations, % GDP	2.68%	2.73%
MilEx1 burden , allocations, % GDP	3.48%	3.61%
MilEx2 burden , allocations, % GDP	4.21%	4.26%

Table 7: Estimates of Transferred Civilian-type Allocations in 2005–2006

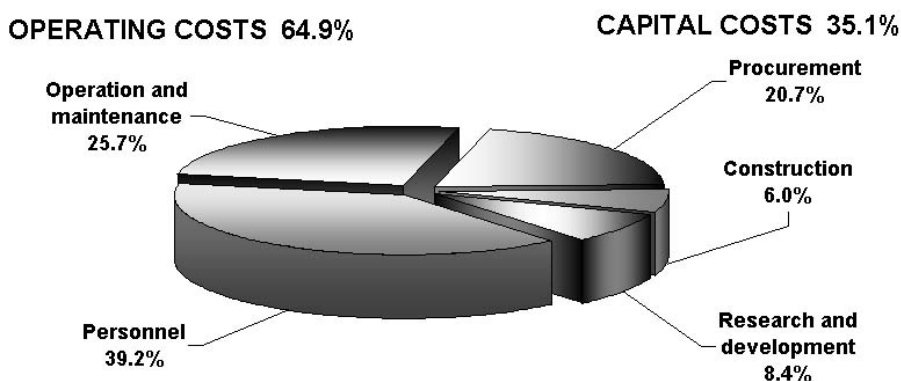
	2005	2006
Ministry of Defence ¹ , bln current roubles	37.6	42.7
Total for civilian-type ² , bln current roubles	52.5	63.7
Ministry of Defence, % GDP	0.17%	0.18%
Total for civilian-type, % GDP	0.24%	0.26%

Sources: 1 – The State Duma Defence Committee; 2 – own calculations.

Regarding the reliability of estimates in Table 7 I should note that the values given are all quite conservative and actually they can be substantially higher. In this connection it is worth to notice the statements made by Chairman of the Russian Federation State Duma Defence Committee Victor Zavarzin (Matveev, 2006) in which he has said that defence expenditures in current year amounted to 798 billions roubles with 132 billions roubles from them hidden in non-military budgetary divisions, what could increase our estimate of total defence burden shown in Table 6 for 2006 by 0.54%.

Due to high secrecy level of Russia's federal budget it is impossible now to estimate the structure of appropriate military expenditures according only to data supplied by annual budgetary laws. The only openly published official data about current structure of Russian military expenditures (UN, 2005) are presented on Figure 1.

Figure 1: The 2005 Structure of Russia's Military Expenditures Reported to UN



3. Behind the curtain there are...

3.1. Federal budget and budgeting process

The budgeting system of Russian Federation is still in the transition from that of the former Soviet Union although may be in one of the ultimate phases of it. And despite the fact that *Budget Code* came into force in 2000, the system is still a

subject to annual changes in the legal framework of budget management (Diamond, 2002).

The key feature of the federal budget preparation phase is a lack of formal and openly published budget request of the Ministry of Defence (and other governmental bodies, of course). Consequently the Ministry of Defence intentions and policy may be skewed by implicit bargaining process inside government thus increasing the level of irresponsibility in the former. The last advance in budget preparation is connected with adoption of three-year financial planning on rolling basis. Furthermore the goal is stated to shorten up to 15–16 months the time needed to approve by law executed federal budget thereby building its results and efficiency estimates in annual budgetary cycle.

In process of budget approval the main role belongs to members of Federal Assembly of Russian Federation. But they just can not effectively carry out the task of budgetary control because of well known prevalence in both Committees (in the Duma and the Federation Counsel) connected directly with defence matters of so called “soldier-politician” (Betz, 2002) who not only lacks both own skills and advanced analytical support in defence budgeting, economics or accounting, but “rather acts as a kind of lobby for the military circles than as a tool of democratic control of military and security agencies” (Fedorow, 2002) .

With federal budget execution itself there are problems too. Overall process of budget execution is remarkable for substantial delays. For example, governmental regulation of 2006 federal budget execution was issued only in the end of February 2006. No wonder that all budgetary payments get tendency to be skewed against the end of budgetary year with most ridiculous situations in the defence sector according to statements from the Chamber of Accounts of Russian Federation (Pulin, 2006).

The latest substantial changes in budgetary system include above-mentioned adjusting of its functional classification according to COFOG. After that classified expenditures emerge in the federal budget’s divisions, which are not directly related to defence and security—quite an unexpected effect from the standpoint of economics.

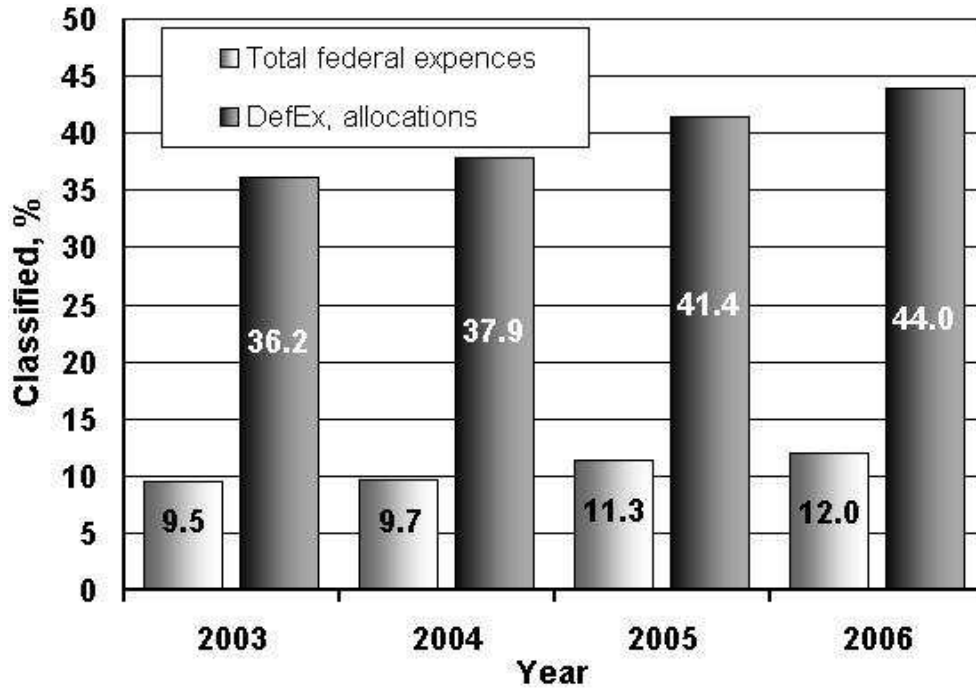
Of course, it should be understood that this effect of “spreading” of the classified expenditures over the whole budget is most likely caused not by the intention to conceal from domestic and foreign observers some of the rapidly growing expenditures on defence and security, but by the fact that in accordance with the recommendations of international standards the power structures expenditures on housing, education, health care, etc. were assigned to the corresponding divisions in new functional classification for budgetary expenses. Nevertheless the question arises: what were the actual motives of the federal budget developers when placing such expenditures on secret list and then leaving them classified?

3.2. Secrecy problem

The most prominent feature of Russia’s military expenditures is its potentially full secrecy according to the *Law on State Secrets*. Although the *Budget Code* limits secrecy only to budgetary item level but in practice there are many fully secret subdivisions in federal budget and secrecy level itself is regulated actually not by the Ministry of Defence but both of the Ministry of Finance and the Ministry for Economic Development and Trade.

Despite President Putin has stated before the Federal Assembly in May 2004 that “a transparent military economy is a necessary condition for reform”, the growth in secrecy level of federal expenditures continues as shown in Figure 2.

Figure 2: The Secrecy in Russia’s Federal Expenditures in 2003–2006



So far as there were no statements about the reasons for such growth, they remain hidden. It is only known that in the past two years there were no substantial changes in the official list of data considered as state secrets. In this connection attention should be given to the conjecture put forth by independent observers, that the main reason of the growth is opportunistic behaviour of the state machinery interested in remunerations for work with classified information, however this question still needs further exploration.

Now it is difficult to say what price in the percentage points of GDP growth Russia pays for one-percent rise in secrecy level of the federal budget, but existence of negative feedback between these two factors is beyond doubt.

3.3. Defence planning

The rational defence budgeting in contemporary Russia is seriously handicapped by situation in defence planning, which was inherited in general intact from Soviet times deteriorating contrary to intentions due to unlucky generation change. The federal *Defence Law* defines main components of the military planning system. The pillars of the system are *Armed Forces Employment Plan*, *Armed Forces Organization Plan*, and *State Armament Program*. The last and former constitute formal base for defence budgeting. Beside them by Russian General Staff for long-term planning are developed the *Conception of National Security and Armed Forces Organization* (currently till 2021) and the *Intention for Organization and Development of Army and Fleet* (currently till 2016). Since 2005 this planning system was extended by adoption of special *Armed Forces Units Provision Complex Program for 2006–2015*.

In 2001 Chief of the Russian General Staff (Kvashnin, 2001) has admitted that General Staff planning and *State Armament Program* were based on different principles, which made them simply incompatible. The planning system as a whole is incoherent and contradictory: are the *Conception* and the *Intention* all the same? Is the difference between 2016 and 2021 big enough to have two different long-term documents? What is the difference between the new *Armed Forces Units Provision Complex Program for 2006–2015* and the old *State Armament Program*?

3.4. Quasi PPBS

The beginning of the *State Armament Program* cherished by the Russian officials goes back to the late 1960s. It was initiated by the Soviet leadership, which had to react on successful PPBS implementation in the US Department of Defense. Despite the fact that USSR perished before the first Soviet *Armament Program* was completed, the Russian Federation continues to use it practically in the same form. The contemporary *State Armament Program* significantly differs from its obvious prototype what is shown in Table 8.

Table 8: Comparison of Two Military Programming Systems

	PPBES (USA)	State Armament Program (Russia)
Cycle duration, years	2 (was 1)	5
Depth *, years	4 (was 5)	10
Moving time horizon	Yes	No
Accountability	Transparent	Opaque
Secrecy	Minimal	Full

* *Note:* The contemporary Pentagon budgeting plan has the depth of 6 years.

From the Soviet time until today different interest groups participating in development of the *State Armament Program* could not negotiate and publish any rules and regulations for it (Burenok, 2004). No wonder that the program instead being a means of control over military-industrial complex became a tool of special interest groups for control over considerable share of federal military expenditures. Therefore the new *Armed Forces Units Provision Complex Program for 2006–2015* can be regarded as an evidence of intentions to discontinue development of *State Armament Program*.

3.5. Actors and goals

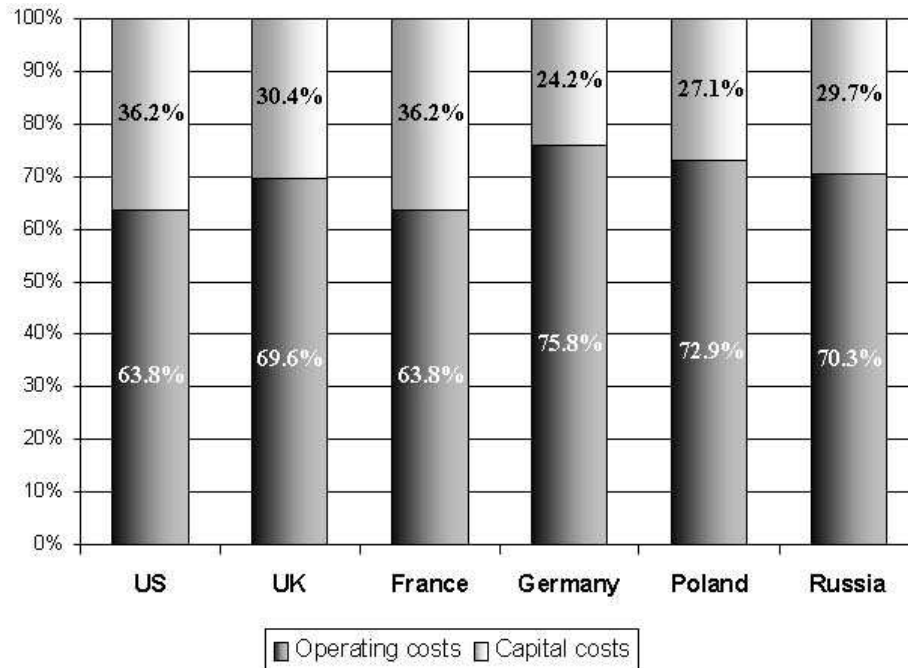
There are too many actors on the defence management stage in Russia. Not only size of the country's military expenditures but its structure are determined by the Ministry of Finance and the Ministry of Economic Development and Trade what actually decreases the Ministry of Defence responsibility. This virtual 'Grand Ministry of Defence' is another source of inefficiency on highest level of Russian public administration and vivid evidence of parliamentary control failure over security sector. And in this regard the latest changes connected with rising level of the Governmental Military-industrial Committee (Pulin, 2006) are questionable.

As an effect of such 'Grand Ministry of Defence' practice may be regarded current situation in Russian Armed Forces when due to economy consideration the spending on force training is kept at level 20–25% from demand hereby degrading overall Armed Forces capability and converting substantial part of its manpower into overhead.

Back in 2000 the Security Council of Russian Federation has set a perspective goal for the Ministry of Defence to achieve 50% share of capital costs in defence budget by 2010 following "best international practices". This perspective goal was intended to serve as a performance indicator for the Russian Armed Forces. The goal was confirmed again in July 2005. In late 2005 Chief of Russian General Staff stated (Cherhyak and Gavrilov, 2005): "All the world develops according to the outline: about 60 per cent is spent on procurement, research and development; and about 30–40 per cent—on salaries and matters, connected with logistics and combat training of forces". Unfortunately, the most superfluous analysis of the

international practices based on (United Nations, 2005) and shown on Figure 3 casts a serious doubt on the adequacy of goals pursued by Russian high-ranking officials, priorities they set forth, and quality of information they used in decision making for defence management.

Figure 3: The Operating/Capital Structure of Military Expenditures of a Number of Countries in 2004



According to the latest statement of the Chief of Defence Economic and Finance Service (Kudelina, 2006) the overall movement direction in Russian defence budgeting can be determined as ‘back to the future’ when unlucky former Soviet experience is regarded with envy, nostalgia, and short-sightedness as highly valuable classicism.

4. Conclusion

Russia’s defence management demonstrates now classical examples of government failures. These failures, connected with limited information and control over bureaucracy, were demonstrated by examples of secrecy and priorities setting in security sector. The failure imposed by political processes was not regarded but I agree that the whole situation after successful building so called ‘administrative vertical line’ in Russia gives us not much hope of democratic control on security sector and rational management in it. Russia gets in specific institutional trap with secrecy obsession of its high-ranking officials due to their occupational experience on the one hand, and vital necessity to be efficient and competitive on the other hand.

As regards the main theme itself, it will be very interesting to explore and dispute what factors raise the Russia's military expenditures in last years but that they are mainly of internal nature (Ovsienko, 2005) and not connected to external threat level seems obvious.

It is very hard art of prediction and especially of matters concerning the future. But unfortunately I can state with certainty that: in current year federal budget will be augmented more than one time; lack of fuel for combat training will be excused by 'unplanned' prices growth rather than by intentional budget policy; and most of procurement outlays will be again executed in last quarter of the year.

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