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Sailing to Portugal's GDP Hits Some Turbulence

By Martin Gilman

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When traveling by boat, it is useful to check the navigation charts occasionally to ensure that it remains on course for its destination while avoiding any obstacles or turbulence. Hopefully, any deviations from the ideal route can be quickly corrected and progress can be made in getting to where the boat was intended to go.

This boating metaphor can be extended to an assessment of economic performance by countries, at least in those cases where a long-term economic objective has been articulated by its leaders. A long-term perspective is appropriate because, just like a boat, in the short term sudden storms and other unexpected external developments can blow a boat off course. It's only over a much longer period or journey that the correct policies, adapted to the prevailing conditions, can be assessed.

Understandably, most leaders refrain from such long-term speculation about their economies, especially in relation to other countries, for the simple reason that it is hard enough to have a clear idea of growth projections even just a year ahead. So it is either an audacious or foolhardy head of state who publicly sets an objective over a decade hence. But when the boat finally reaches its presumptive port, there are usually precious few still in power and accountable.

In Russia's case, however, a long-term goal was articulated, and the leader may still be in place when the time comes due for the final assessment.

Some will recall that then-Prime Minister Vladimir Putin on the eve of taking over from Boris Yeltsin, on December 30, 1999, presented his views on Russia at the turn of the millennium. In discussing an article chapter heading titled "Chance for a Worthy Future," Putin drew the main lessons of the outgoing century: "It is possible to outline the contours of a long-term strategy, which is to enable us, within a comparatively short time, by historic standards, to overcome the present protracted crisis and create conditions for our country's fast and stable economic and social headway. The paramount word is 'fast' since we don't have time for a slow start."

Putin then went on to elaborate the now-

famous comparison in setting the long-term (in 15 years) objectives for the country's economic policy. "It will take us approximately 15 years and an annual growth of our gross domestic product by 8 percent a year to reach the per capita GDP level of present-day Portugal or Spain, which are not among the world's industrialized leaders," Putin said. "If during the same 15 years, we manage to ensure the annual growth of our GDP by 10 percent, we will then catch up with Britain or France."

Of course, Putin was referring to real growth, abstracting from inflation. After all, in nominal dollar terms and using International Monetary Fund data, in the subsequent decade from 2000 to 2010 Russia's GDP per capita grew by 487 percent thanks mostly to inflation. In real terms, though, it grew by a much more modest, but still impressive, 60 percent. This is 6 percent growth per year on average, which includes the 2009 dip during the global financial crisis.

With 10 years down and 5 years left to go on the time scale set out by Putin, how is Russia doing?

By 2010, again using IMF data, Russia's per capita GDP was $10,522. In 2000, Portugal's per capita GDP was $11,511 and Spain's was $14,464. It would seem, at first glance, that Russia could easily by 2015 attain Portugal's 2000 standard of living and perhaps even that of Spain.

That is the good news. The bad news is that, even while Russia plays catch-up with the dollar-measured standards of living of Portugal and Spain in 2000, those countries also continue to grow modestly, despite the debt crisis in the euro zone. So while the IMF projects Russian per capita GDP to be $16,449 by 2015, Portugal is expected to grow to $21,887 and Spain to $32,051. Even adjusted for what is called "purchasing power parity," or PPP, which is used to better compare the actual costs of similar goods and services, Russia, at $20,074 in PPP terms, would still trail behind Portugal with $25,034 in 2015.

Perhaps somewhat more encouraging, though, is the table of country rankings based on per capita GDP. By 2010, Russia had climbed from 95th place in 2000 to 54th place by 2010, and still just ahead of Brazil, which had already been in 71st place in 2000, not to mention much poorer China and India.

Of course, this is all a rather mechanical exercise. The navigational skills of the authorities in all of these countries are being challenged as never before. There is no such thing as an inevitable outcome. And even a higher average per capita GDP number can still mask glaring inequality in countries like Brazil, even if improving.

For Russia, the challenges are particularly daunting since its population is declining. And, as Finance Minister Alexei Kudrin noted last week, Russia can no longer depend on the energy sector as a source for growth. At least there are no major constraints on the macroeconomic side that could hamper growth, but it does means that only rising productivity can drive the economy. Investment in human and physical capital holds the key.

This will be difficult to do. Kudrin also mentioned last week that with average monthly wages in Russia rising from $100 in 2000 to roughly $700 by 2010, wage increases have outstripped increases in labor productivity. While individual Russian firms can no doubt point to many investments that have produced tangible productivity gains, at the aggregate level the productivity dividend of the investments made over the past decade — especially in the state-owned sector — has been alarmingly low. This has to change.

Returning to the boating metaphor, perhaps it’s best not to state a predetermined destination that may lead to disappointment and frustration. Maybe it would be better to ensure the best boatmanship possible — that is, to worry less about the goal and focus more on the right policies to promote private, productive investment. Putin knows well what these are, and the foreign and domestic business community is waiting for clear and steady signals about smooth sailing ahead.

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