

Economic Slowdown and Putin's Promises Take Toll on Budget

By [The Moscow Times](#)

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The Russian budget's dependence on fickle oil and gas prices is set to remain high, as the country will be forced to borrow more in response to an unexpectedly severe economic slowdown.

Under a three-year budget plan, the Finance Ministry will raise borrowing to compensate for lower-than-expected tax revenues and to fund the rising cost of spending promises made by President Vladimir Putin.

Delivering on these promises, made before Putin's return to the Kremlin last year, has become much more challenging as a result of a worrying economic slowdown. The government now projects growth at little more than 3 percent over the coming years, down from previous projections of 4.3 to 4.5 percent.

"The government has to face reality, and the reality is that the economy is slowing," said

Vladimir Tikhomirov, chief economist at Otkritie brokerage. "Since the economy is slowing, revenues are going to be much lower than originally forecast."

Next year, the federal budget deficit is projected at 0.5 percent of gross domestic product up from a 0.2 percent forecast in the previous budget plan.

In 2015, Russia foresees a deficit of 1 percent of GDP, having previously projected no deficit. The deficit is projected to narrow to 0.6 percent of GDP in 2016.

Although small by the standards of debt-burdened western governments, Russia's rising borrowing needs will deal a blow to much-touted ambitions to lower the budget's worrying dependence on volatile energy prices.

The non-oil deficit, which measures the underlying fiscal stance by stripping out oil and gas taxes, will barely decline over the next two years. In 2015, it will amount to 9.6 percent of GDP — up from a previous projection of 8.4 percent and only fractionally below 10.3 percent in 2013.

A modest fall to 8.4 percent is projected in 2016, still almost double its level before the 2008-09 financial crisis.

"It's important to reduce the non-oil-and-gas deficit ... as this will ensure more stability in budget revenue," said Alexei Devyatov, chief economist at UralSib.

"So far Russia was pretty lucky because oil prices were quite high, but this may not last long. That's the problem."

Squaring the Circle

The rise in expected borrowing underscores the difficulty Finance Minister Anton Siluanov faces in squaring the budget circle, as he grapples with lower-than-expected tax revenues and the need to fund Putin's election giveaways.

His predecessor, Alexei Kudrin, quit in September 2011 in a row over a ramp-up in defense spending that he said would cause a massive fiscal headache from the middle of the current decade.

Under the revised budget plan, the Finance Ministry projects that revenues will be some 3.5 percent lower in 2014 and 7 percent lower in 2015 than had been expected.

The new budget plan also foresees cutbacks in expenditures, which will be 1.7 percent lower overall in 2014 and 2015, compared with previous projections.

Economy measures include a freeze in the pay of all military personnel next year, which will save 127.1 billion rubles (\$3.9 billion) a year by 2016.

The new plan also makes further cutbacks in the mandatory savings that Russians make toward their pensions. The freed-up cash — some 133.4 billion rubles per year by 2016 — will be used to fund current pensions instead.

The move is the latest blow to plans to create a funded pension system in Russia that would reduce long-term pressure on the budget from an ageing population.

"The key negative surprise ... is that in order to reduce transfers to the State Pension Fund, the government decided to cancel defined contributions for people who are not actively managing their pension savings," Alfa Bank economist Natalia Orlova commented.

Despite these savings, the fall in overall expenditures will be much more modest than the fall in revenues, as much of the projected savings are being poured into additional funding for Putin's spending commitments.

In a series of decrees last May, Putin committed the government to spend more on priority items such as public sector pay, social benefits and regional development, reiterating pledges made at the time of his re-election last March.

He has since upbraided ministers for not finding adequate amounts of finance for these spending plans.

Under the new three-year budget plan, the Finance Ministry proposes that 531.4 billion rubles will be spent on financing Putin's decrees next year, rising to 726 billion in 2015 and 849.9 billion in 2016.

Previously, Russia had budgeted 381 billion rubles for these programs in 2014 and 487 billion in 2015.

The new budget strategy is expected to be approved by the government's budget commission later on Wednesday. It still needs to be approved by parliament, although major changes are seen as unlikely.

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