Officials Balancing Fiscal Restraint and Growth

By The Moscow Times

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Russian government leaders concede that the focus on fiscal restraint, which includes freezing monopoly tariffs and bearing down hard on inflation, risks repressing the recovery of the country's $2 trillion economy, which until the 2008-09 crash relied on booming commodity prices to drive growth.

"Everything here is very stable; it is just the sort of stability we do not like," First Deputy Prime Minister Igor Shuvalov said during the Reuters Russia Investment Summit.

"If you look at other markets, even states in the Group of 20, the situation is much more unstable. We have it a lot better, but growth of 2 percent a year is just not enough for us to modernize."

The World Bank last week cut its Russia growth forecast for this year to 1.8 percent in line with the government, saying the economy was operating near full potential and a lack of structural reforms had become a "binding" constraint on growth.

While the U.S., Europe and Japan keep policy settings ultra-loose to sustain a fragile recovery, the policy consensus in Moscow is starting to look a lot more like a Bundesbank chairman of yesteryear dreamed it up.

Business does not like it, especially sectors that rely on investment by large state companies, such as gas export monopoly Gazprom or Russian Railways, who now face caps on the prices that they charge their customers.

"Why drive them into debt?" asked billionaire Andrey Filatov, a co-owner of infrastructure group N-Trans who has interests in rail freight, ports and construction.

"Freezing tariffs to fight a mythical inflation threat is the wrong decision — I am categorically against it," added Filatov, one of two dozen policymakers and entrepreneurs who shared their views at the summit.

New Austerity

By keeping the public finances tight while curbing regulated prices, the government believes it is helping keep inflation in check and hopes in return that the new team at the Central Bank will finally spur investment by cutting interest rates that have been on hold for a year.

Yet U.S.-educated economist Ksenia Yudayeva, who has just moved into the No. 2 role at the Central Bank, says "one should not exaggerate" the bank's ability to revive an economy already near capacity without losing control over inflation.

The government is ready to face down threats of large-scale job losses by the monopolies. Finance Minister Anton Siluanov says they can easily cut their bloated investment costs by 5 to 10 percent without resorting to slashing staffing levels.

"If before we sought to preserve jobs and were very cautious about layoffs, now our task is to boost labour productivity," Siluanov said. "We are ready as a state for job cuts and to help people find new work."

While Russia's economic recovery shows signs of stalling, a demographic squeeze on young people entering the workforce means that the unemployment rate has fallen to 5.5 percent, or almost full employment.

Labor shortages are being filled by as many as 10 million illegal immigrants, largely from Central Asia and the Caucasus. Yet casual jobs on building sites undercut Russia's tax and welfare systems, while rewarding employers who game the system.

Increasing legitimate employment could boost labor productivity by 70 percent, the government reckons.

Russia should actually be raising infrastructure investment and reviving a privatization process that has stalled since President Vladimir Putin's return to the Kremlin for a third presidential term last year, industry bosses argued.

Privatization "is a good source of fiscal revenues and to mobilize growth," said Mikhail Shamolin, CEO of telecom-to-oil conglomerate Sistema, adding he would be interested in snapping up assets should they come up for sale.

A Question Of Confidence

Russian consumers used to be free spenders but, even though household borrowing is a paltry 12 percent of gross domestic product, their confidence has yet to recover from the crisis.

The balance of risk and reward has in the meantime tilted against investors, said Boris Titov, a wine merchant appointed business ombudsman last year by Putin.

"Anti-crisis management is like building a chair: you can sit too comfortably," Titov told the Summit.

"But if you want to develop, you have to forget about the chair. Because if you have a too comfortable chair you will never stand up — and you have to run!"

Sovereign debts are just 11 percent of GDP, less than half the level of 25 percent that Siluanov considers safe given Russia's dependence on oil and gas taxes to cover half of its revenues.

But instead of eyeing fiscal stimulus, he is already fretting that state spending may run away before the 2018 presidential vote. Russia has painful memories of earlier crises: It suffered hyperinflation after the Soviet Union collapsed and was bailed out by the International Monetary Fund in 1998.

Sergei Guriyev, a leading economist and former government adviser, is confident there will be no repeat of that under the current administration.

"Putin remains a fiscal conservative," he said.

"He always said it is a humiliation to go to external creditors — and especially to the IMF. It is a loss of sovereignty."