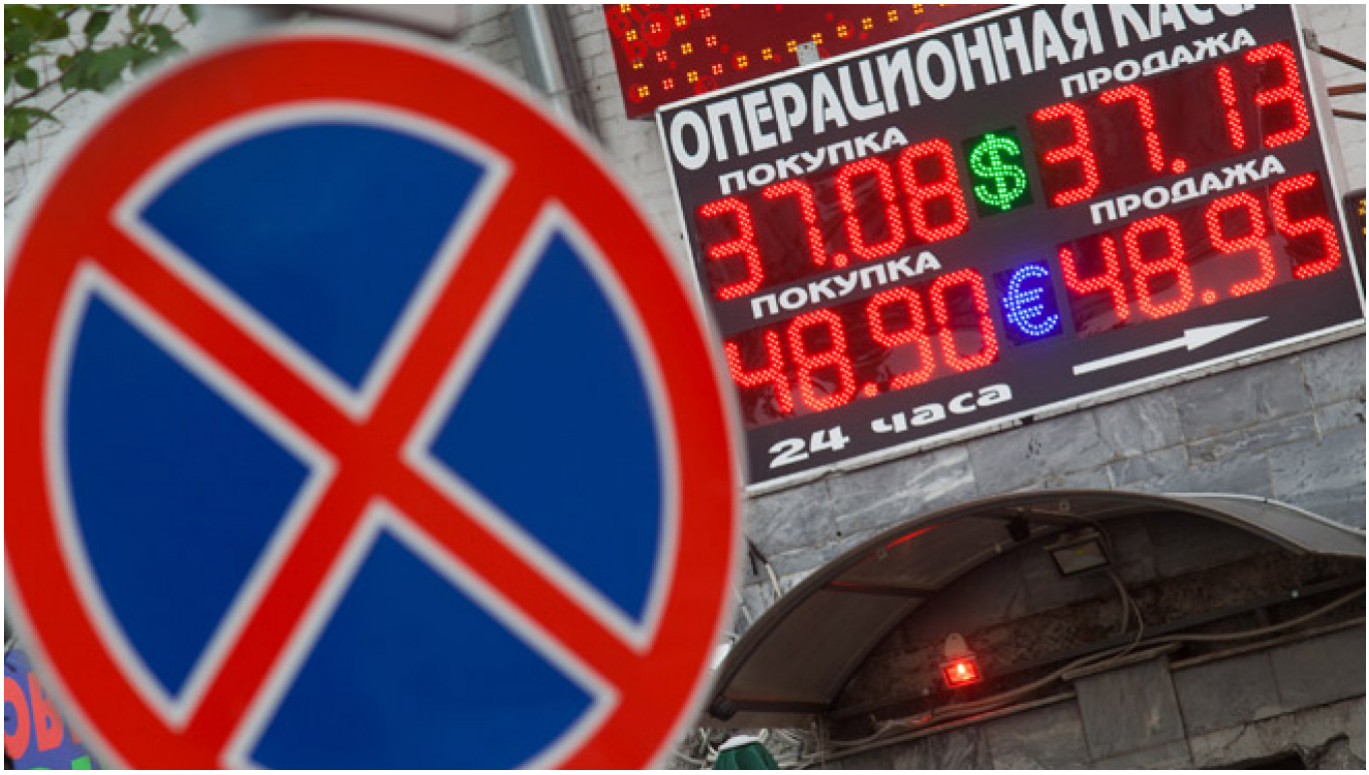
The Moscow Times
30 YEARS
INDEPENDENT NEWS FROM RUSSIA

Russia Shouldn't Expect a Prosperous Future

By Pekka Sutela

September 15, 2014



Russia's economic future is cloudy, at best.

There was a time, not long ago, when Russia was one of the fastest-growing economies globally. In constant dollar terms, Russia grew twice as fast as China in the 2000s. As an export market, Russia expanded by up to 30 percent annually, much faster than any other major economy.

But those times will not return. This is in part due to the world economy, and in part due to Russia's domestic issues.

The world economy is evidently entering a lower growth period, after decades of prosperity unique from a historical point of view. To a degree this is due to the financial crisis. Excessive debt levels have to be normalized and so finance will be tighter. More and more countries are also going through a demographic transition. The U.S. population is growing slowly, Europe's population is holding steady, and China will soon be facing not only an aging, but also

a declining population.

Europe's long-term expected growth is almost stagnant, while the U.S.'s is at best 2 percent annually. China will continue catching up with the rich countries, but Russia won't gain much as it produces little that the Chinese bourgeoisie demands.

But, even given the worsening global outlook, Russia has seriously damaged its potential for fast growth by failing to pursue meaningful economic reform, especially since 2011.

It's true, of course, that many existing policy challenges are complicated and lack obvious solutions. But the government's avoidance of reform is not due to lack of expert understanding. Rather, it is due to the Kremlin's weak hold on power, which forces it to make impossible promises of more money for everybody.

The military, pensioners, public sector employees and other worthy causes have all been promised more resources out of the same, limited pot. Even under normal circumstances, this is a highly risky tactic to adopt. The notorious prestige projects of the Winter Olympics and the World Cup are a highly visible consequence of this overly liberal spending.

And to make matters worse, some of the promises have even been extended abroad. Although Crimea is a relatively small place and therefore probably economically sustainable, eastern Ukraine's moribund industries are not. Even if Donbass remains within Ukraine, Russia has de facto promised to help it survive economically. The European Union has made a similar promise concerning Ukraine, but has hugely greater economic resources than Moscow.

Russia can rely on its natural resources to fund such outlays, but this may prove dangerous: In the foreseeable future energy will remain valuable, but the oil price will not increase by 10 times again, as it did between 1998 and 2008. Russia's energy production will basically stagnate.

And when budget expenditure is tied to a stagnant oil price, expenditure re-allocation becomes a zero-sum game. When one area, say the military, wins, someone else must lose.

Russia's demographics, at first glance, would appear to be a bright spot for the nation. Despite early predictions of steep decline, Russia's population has been stable for some 10 years, largely due to immigration from the rest of the former Soviet Union. Foreign temporary workers also help the labor markets, though statistics on this are unreliable. Life expectancy has increased, at long last also for men, but the pension age remains low, increasing the share of pensions in national income.

However, despite these good signs, the number of young adults has halved. Demographers debate whether this is due to the crisis of the 1990s, or even has roots in the early 1940s, when the birth rate dropped significantly. Total fertility has improved somewhat in recent years, but the next generation will only enter labor markets in 20 years' time. As the option of a higher pension age has been abandoned, labor markets are increasingly dependent on working pensioners or foreign temporary workers.

This is probably the principal reason why Russia overall has very low unemployment. In major economic centers, consequently, labor costs and inflation are increasing, even though

production is not growing.

But worryingly, the quality of the labor force is worsening. The pensioners most willing to work are often those with the lowest pensions, that is, people with the least qualifications. Immigrants have usually little education, low-level work experience and poor knowledge of the Russian language. They take the jobs Russians are unwilling to do.

What's more, a number of well-qualified Russians have left the country, perhaps permanently. Nobody knows how many, but the figure is probably in the low millions, similar to the size of the White Emigration after 1917.

Thus, in the long term, Russia faces adverse demography and slower global economic growth, in the medium term, the threat of a weak regime unable to pursue needed policies. And in the short term, international relations are steeply deteriorating, leading to adverse financial flows and sanctions.

It is difficult to predict what results these trends will bring. If the short- and the medium-term issues become long-term problems, baseline economic forecasts of 2 percent annual economic growth in Russia will prove to be utopian.

The consequences cannot be foreseen, but they will not be pleasant.

Pekka Sutela is professor at Lappeenranta University of Technology, Finland, and visiting professor at the Paris School of International Affairs, Sciences Po.

The views expressed in opinion pieces do not necessarily reflect the position of The Moscow Times.

Original url:
https://www.themoscowtimes.com/2014/09/15/russia-shouldnt-expect-a-prosperous-future-a39415