



Russian Economic Policies after the Election

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The growth story of 2000-08 will not be repeated

- Preceding institutional change
- Low-hanging fruit of structural change
- Exceptional growth of the global economy
- Oil (and gas and minerals) price
- Low capacity utilisation
- Low labour costs
- Low domestic energy and utilities prices
- Undervalued ruble after 1998

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Preceding institutional change

- 2000-08
 - Liberalisation, privatisation since 1992
 - But stabilisation only since 2000
 - Monetisation: from barter to ruble
 - Signs of active, not only defensive restructuring in companies
- Now
 - Putin's second term was not a complete wasteland for reform
 - Financial sector
 - Power reform
 - Military
 - WTO
 - Hard challenges ahead
 - State: from grabbing to helping hand
 - Companies: growing from small to medium-sized
 - Financial system: from the dual system to long-term domestic funding
 - Public sector reform: pensions and much more

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3

Low-hanging fruit of structural change

- 2000-08
 - From planners' to consumer preferences
 - Opening up of the economy
 - Normalisation, not de-industrialisation
 - In different ways, both Putin and Zyuganov saw this as a problem: what might re-industrialisation policies be?
 - 1990s: entry of new companies
 - 2000s: monetisation and financial deepening
- Now
 - Between low-cost Asia and high-tech Europe: where is Russia's competitive advantage?
 - More value out of resources?
 - Does Schumpeter ever enter Russia?
 - Inherited military / dual use industries after the enemy has disappeared

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4

Exceptional growth of the global economy

- 2000-08
 - (Almost) unprecedented global boom
 - Learned: Resources are a blessing, not a curse
 - When adequately handled, as Russia did
 - Easy access to finance
 - Russia's debt remained under control
- Now
 - Lower growth generally expected
 - Access to finance a question mark
 - Russia's unfortunate dependence on European markets is difficult to remedy

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5

Export prices

- 2000-08
 - From trough in Spring 1998 to peak in Summer 2008 ten times increase in oil price
 - Gas and minerals prices followed
- Now
 - Similar will not be repeated
 - But neither will export prices collapse
 - Modest growth?
 - Market constraints in gas exports leading to underinvestment: a price/profitability cycle coming into supplies
 - Foreseen: no Shtokman, yes South Stream, perhaps Nord Stream 3-4

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6

Low capacity utilisation

- 2000-08
 - Statistical capacity utilisation rate increased from about 50 to some 80%
 - Cheap growth possible by increasing utilisation and some upgrading
 - Still, annual fixed investment growth clearly faster than GDP growth (2009 excluded)
 - Overheating with faster inflation in 2007-08
- Now
 - Putin: investment to GDP ratio should increase from current about 20 to 25 and then 30%
 - How, where, by whom?

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7

Low labour costs

- 2000-08
 - Average wage 180 USD in 2003 but increased to 1041 USD in 2011
 - Labour force grew due to high fertility in end-1980s
 - In-migration compensated for half of natural decline in population after 1992
 - Contrary to rumour, resident population has not decreased since 2005-06
- Now
 - Working age population will decrease for at least ten years unless pension age increased
 - 300'000 annually expected in medium term
 - Serious mismatches in regional distribution and skills continue
 - Most in-migration will continue to be with low skills
 - And at least some social tension expected

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8

Low energy and utilities prices

- Failure to liberalise energy prices in early 1990s, role of regional subsidies
- Key role of gas
 - Dual markets: Gazprom vs “independents”
 - Almost half of electricity produced from gas
 - Power sector reform: combined heat and power production with only partial (power) market liberalisation
 - In different ways both Putin and Zyuganov saw this as a problem
 - 2006: the net-back principle
 - Kind of followed, largely
 - Liberalisation soon becoming feasible

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9

These changes were foreseen

- Coincide in time with the crisis, are not caused by it. But
 - Dependence of the financial system on foreign funding
 - Further decreasing trust in the invisible hand
 - High-cost decisions to support stability and existing jobs plus pensions. Relative to Zyuganov, Mironov and Medvedev (?) Putin is no fiscal populist
- Putin's changing thinking: Is re-inventing VVP possible?
 - 2000-04
 - Key role of energy: production growth, increased state control, reserve funds
 - 2004-08
 - No growth in energy production foreseen; energy efficiency needed for maintaining export volumes; -> modernisation, diversification; Russia 2020 programme (2006-08)
 - 2009-10
 - firefighting
 - 2011->
 - January 2011: new Russia 2020 programme to be written as “economic programme of the May 2012 government”
 - 864 pages

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10

Undervaluation of ruble

- In 1998 ruble dropped from six to USD to about 20-25 to USD
 - No evidence that ruble was overvalued before August 1998
 - The force of stabilisation: Primakov – Maslyukov government declined to release a wage/price spiral -> the competitiveness edge could be maintained for years
- In the 2000s ruble was tied closely to a USD/euro basket
 - Due to differences in export/import invoicing currencies, this caused its problems
 - Peculiarly, the Ministry of Finance targetted inflation through export revenue taxation and the Central Bank exchange rate through market interventions
- Increased flexibility since 2010
 - But no serious test so far
- The problems of inflation targetting
 - Do you really wish exchange rate to fluctuate in a resource-based economy?
 - Do you really have a monetary policy channel?

A note on the side: role of experts

- Perestroika
 - Catastrophic outcomes, ignorant economists
 - Responsibility still not clear
- Early 1990s
 - Washington consensus was sane, but knowledge of Russia was minimal (also in Moscow)
- Gref programme
 - Most of authors remain in positions of authority
 - Estimated 40% implemented
- Benefits for cash
 - Sane idea, faulty cost estimates discredited non-governmental experts
- Original 2020 programme
 - Completely written by civil servants
- Revised 2020 programme
 - Non-governmental experts make comeback, asked by Putin
- And the next government...

But what does Putin think?

- Basically Putin's thinking has been consistent since late 1990s
 - 1997 dissertation, 1999 key articles
 - Processes need managing
 - Markets do not suffice
 - Impact of Soviet optimal planning school and US business management theory
 - In a changing environment, management needs to be adaptive
 - The problem of Soviet planning was inability to change
 - Hierarchy is the natural frame of management, but cannot be all-encompassing
 - Therefore, concentrate on commanding heights: energy, state corporations, state-controlled finance, industrial and technology policy
- But with twelve years of experience and frustration, also increasing cynicism
 - Which is not helped by the rise of the opposition
 - Whose future is however unclear

What has happened so far?

- Prior to elections Putin published several articles on key policy issues
 - No other candidate could produce anything similar
 - Still, as expected, these are vague and inconsistent manifestos
- With the exception of the Medvedev – Kudrin conflict, personnel changes have so far been inside the ruling circle
- The good news: Putin de facto did endorse the new 2020 programme, but key choices remain to be made
 - The key word: shift to investment-based growth
 - From 864 pages many choices can be made
 - But this is a unique document comparable with the Gref programme of 2001, with most leading experts contributing
 - WTO accession is a positive sign

What to look at next?

By May 2012

- Key appointments
 - Minister of Finance
 - Minister of Social Affairs
 - Minister of Defence
 - President's Economic Advisor
- First speeches of President and PM
 - Political reform
 - Military reform
 - Social reform

By October 2012

- Further changes in government?
- WTO ratification (June)
- 2013 budget
- Eurasian Union?

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15

Pro et contra: there is a chance

Pro change

- Putin is clever enough
 - And more liberal than 70% of population (Khodorkovsky)
- He has changed before
- There is need for change
- And better advice than before is available

Contra change

- In the face of emerging opposition, Putin cannot abandon his corrupt group
- Can one change the system one oversaw to evolve?
- Many of the needed changes are genuinely difficult

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16

ROUTLEDGE FRONTIERS OF POLITICAL ECONOMY

The Political Economy of
Putin's Russia

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17