# The failure of Russia’s free-market pension reform

Vladimir Volkov
17 August 2009

Since 2002, one of the main social policies associated with Russia’s former president and current prime minister, Vladimir Putin, has been pension reform. His policy has been directed towards the creation of a new social security system for the elderly based on capitalist market principles. It now stands on the edge of total failure. The mechanisms upon which the reform was founded have proven to be unviable. Even as the aggregate sum of pensioners’ contributions has grown, the average pension benefit has steadily fallen in comparison with average pay. The requirements of the State Pension Fund are colliding with an ever more ominous deficit. Moreover, the private funds and managing companies appointed to run the system have been discredited in the eyes of depositors by their irresponsible and risky speculative investments. The economic crisis, which in Russia has reached a scale comparable to the chaotic situation of the 1990s and the financial crash of 1998, has exacerbated the social conditions that the pension reform was supposed to address. The pension reform has three categories of benefits: basic, emergency and reserve. The basic pension, according to the government’s plan, provides a certain minimum safety net, independent of the participant’s pay or position. Such is the pension currently received by most of the elderly.

The emergency benefit is funded by an automatic deduction from pay and depends on the level of wages. Payment of this benefit is also guaranteed by the government.

The third benefit, the reserve, is funded by a voluntary deduction from pay that goes to privately managed funds. The most significant aspect of pension reform since 2004 was the provision allowing citizens to take money from their state pension accounts and invest it in privately managed funds. This change was launched during the heady years of high oil prices, large budget surpluses and a business boom. But only a few years later, pension management firms and the media have been compelled to admit that the reform has failed.

*Nezavisimaya Gazeta* (*Independent Journal*) wrote in its August 4 edition: “Since 2004, the succeeding pension reforms have resulted in losses on all fronts.” The Pension Fund of Russia (PFR) has registered a growing deficit, while only 13 percent of Russian citizens are paying into Non-State Pensioners’ Funds (NPFs). These funds are riddled with inefficiency and corruption. The Federal Service for Financial Markets (FSFR) published a list of 75 NPFs, nearly half the total number of such funds registered with the government, which are accused of breaking the law.

Since the reforms were initiated, the ratio of average pension payout to average pay has decreased. In 2000, this proportion was 33 percent, but fell to 24 percent in 2007 and 23 percent in 2008. According to the International Labour Organisation, the ratio should be not less than 40 percent. Established by the Soviet Union in 1980, the state pension system provided decent and guaranteed benefits to all retirees. The disintegration of the Soviet Union in 1991 and the subsequent introduction of capitalist market principles led to rampant inflation, approaching 2,500 percent in 1992. The savings of Russian workers, as well as the state pension fund, were wiped out. President Boris Yeltsin reacted to the impoverishment of wide swaths of society with cynical indifference, declaring that popular demands for state assistance expressed “a Soviet addiction.”

Putin came to power promising to overcome the worst features of the “terrible 1990s.” The public hoped for a progressive pension reform that would lift pensioners out of poverty. The ensuing burst of economic growth overwhelmingly benefited the post-Soviet oligarchs and the wealthy elite.

Now, under conditions of a deepening recession and financial crisis, the dismal failure of Putin's pension reform is having a profound impact on the social consciousness of the Russian working class.

Since the US financial crash of September 2008, consumer prices have risen in Russia by 30 percent, while the ranks of those officially registered as unemployed have swelled to 2 million. It is generally estimated that the real number of unemployed is 6-7 million. Russia's gross domestic product has fallen by more than 10 percent since the beginning of 2009.

Powerful sections of the Russian financial elite are demanding new austerity measures directed against workers and retirees. The August 4 issue of the journal *Vedomosti* carried an article, entitled "Pension or Default," which reproached the Kremlin leadership for excessively large expenditures on social benefits.

"The Russian budget for 2009 shows a transfer to the pensioners' fund of 35.7 percent of all expenses, whereas for anti-crisis measures, expenditures will be 9.3 percent," wrote *Vedomosti*, ignoring the fact that the Kremlin had already provided trillions of rubles in aid to the banks and large companies. "However cruel it may seem," the article continued, "a reduction in budget outlays is the preferable route. One mustn't increase taxes in a crisis...the better exit would be to decrease pension and social obligations...."

The acknowledgement by the government and the media of the failure of capitalist market-based pension "reform" symbolises the frailty of Russian capitalism and underscores its historically reactionary character. It portends the emergence of bitter social conflict.