Russian government to slash budget deficit

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In recent weeks the Russian government has announced plans to slash the country's federal deficit by half by 2013, a move requiring drastic cuts in government spending. While the Kremlin has yet to unveil a full package of austerity measures, in late June Finance Minister Alexei Kudrin proposed raising the retirement age by five years.

This would mean that the average Russian man would not receive a pension, as he would not live to the retirement age of 65 years. Russian male life expectancy is only 60 years.

President Dmitri Medvedev explained that the government's new fiscal policy means an end to the use of stimulus measures to boost the Russian economy. As a percentage of gross domestic product (GDP), Russia's "anti-crisis measures" were the biggest of any of the G20 countries.

The stimulus measures provided a bonanza for the corporate oligarchs that dominate the Russian economy. In 2009, by official estimates, the Kremlin spent nearly $40 billion bailing out large corporations with close ties to the state. Some experts put the real number at closer to $150 billion. News stories over the course of the last year have noted that Russia's oligarchs profited handsomely from the stimulus program.

A portion of the "anti-crisis" money was also used to subsidize employment, preventing a sharp upturn in wage arrears and mass layoffs. At the same time, at the instigation of Prime Minister Vladimir Putin, the government increased pensions in 2008 and 2009 by 18 and 11 percent respectively. This brought the average monthly retirement benefit in Russia up to the poverty level—approximately $250 a month.

As a result of the economic crisis and the bailout, the $600 billion fund built up by the Russian government with oil profits, known as the Reserve Fund, will run out by the end of this year.

In his June 29 message on the state budget, President Medvedev applauded the bailout measures for helping preserve "macroeconomic" and "social stability," but insisted that they were unsustainable.

In announcing the turn to budget cuts, Medvedev drew a direct link between Russia's actions and the pro-austerity policy statements of the June 26-27 G20 economic summit in Toronto. Slashing the deficit, he noted, is "the goal that all G20 nations, all developed economies, are setting for themselves."

Over the last several months, numerous European governments—Great Britain, Germany, Greece, Spain, Italy, Hungary, the Czech Republic, and others—have unveiled plans to dramatically cut state spending on social programs and public infrastructure. Russia has now made clear that it intends to move in the same direction, preparing an assault on the living standards of the working class under the guise of "modernizing" the economy and increasing "efficiency."

Efforts to rein in Russia's federal deficit, which currently stands at 5.9 percent of GDP, come alongside growing concerns about the country's level of indebtedness. This year the government intends to finance the budget by drawing $45 billion from what remains of the Reserve Fund and borrowing about $30 billion.

According to Sergei Aleksashenko, Russia's former deputy minister of finance and the former deputy governor of its central bank, even if the federal deficit is reduced to three percent of GDP by 2013, Russia will still be in a "debt hole."

Aleksashenko "expressed the opinion that even in the best case scenario, Russia will encounter budget deficit problems analogous to those of Greece and Spain," *RosBiznesKonsalting* reported on July 9.

He indicated skepticism towards the Russian government's official figures showing a return of industrial production to pre-crisis levels, which has been hailed as a sign that the economy is recovering. In this he is joined by other international investors who are wary of claims that the Russian economy has returned to health.

The Kremlin and other analysts blame much of Russia's worsening budget situation on exploding pension costs. According to Seija Lainela of the Bank of Finland, nearly half of the $80 billion 2010 federal deficit comes from the shortfall in the pension system, which has been underfunded for years. Out of a population of about 140 million, nearly 40 million draw a pension due to either old age or disability.

While Prime Minister Putin sought to boost his populist credentials by overseeing an increase in retirement benefits in 2008 and 2009, nothing was done to secure adequate funding for the pension system. The ultimate effect of his much-touted advocacy for the elderly was to set the stage for fiscal austerity.

Finance Minister Kudrin insists that the only possible way to continue financing pensions is to raise the pension age for men to 65 and for women to 60.

The average retirement age in Russia is currently 54 for men and 52 for women, however, as 30 percent of the work force falls into job categories eligible for early retirement. Some economists now advocate junking these special categories and increasing the number of years that a person must work before becoming pension-eligible.

They also propose making it illegal for a pensioner to work when he or she is receiving retirement benefits. Currently, 30 percent of Russia's pension-age population stays in the workforce because they cannot survive on what the government provides. Grandmothers begging on the streets are a common sight in Russian cities.

The aim of the proposed changes in the Russian pension system is to eliminate, once and for all, whatever remains of the Soviet-era welfare state. Kudrin's proposal has significant backing within the ruling elite. While Medvedev and Putin have failed to explicitly endorse the changes to the retirement system, both have embraced the finance minister's program of fiscal austerity.

"We need an extremely responsible and steadfast budget policy," Putin stated. "We cannot spend more than we earn."

The prime minister and the president's reticence on the issue of the retirement age is based on political calculations; in the lead-up to the 2012 presidential election, both are loathe to come out in open support of a policy that is widely opposed by the population.

Kudrin's proposal has elicited concern from layers of the government over its potentially explosive consequences. An increase in the retirement age in Russia would reverberate throughout the entire economy and expose the fragility of the social system.

After observing that 40 percent of the male population does not live to the current retirement age, the head of the Center of Social Policy at the Russian Academy of Sciences, Evgenii Gontmakher, told *Novie Izvestiia* on July 15, "Women, who currently retire at the age of 55 and do not work, take care of their grandchildren and elderly parents. This means that government pensions are effectively financing the lack of nursery schools and nursing homes."

In short, forcing these women back on to the labor market would create a crisis for working parents. Furthermore, increasing the pension age would also significantly raise the number of job seekers—driving unemployment up and wages down.

In addition to reforming the pension system, the Kremlin has also proposed to reduce the number of federal employees by 20 percent and sell off state property. During the economic crisis, the government took onto its books numerous failing enterprises. The aim is to now return these and other publicly-owned entities to big business.

In recent comments to the public, both Medvedev and Putin have insisted that the government will bring the federal deficit into line, while continuing to maintain, and even increase, spending on social entitlement and public services. However, as numerous economists have pointed out, this does not correspond with the government's stated budgetary goals.

Natalia Akindinova of the Higher School of Economics in Moscow told the online news site gzt.ru, that if the government tries to fulfill its "social obligations" (i.e., pensions and other welfare payments) while also bringing the federal deficit down to zero percent of GDP by 2015, "there will be no money for modernization or infrastructure projects," both goals of the Medvedev administration. "Moreoever," she added, "the share of expenditures on education and health care will fall two times."

She went on to note that in an alternate scenario in which the federal deficit was reduced to only three percent of GDP, the government would still have to "limit social policies."

The precise nature of the austerity measures in store is still being fought out within the highest circles of the Russian ruling elite. The Kremlin is divided over how to calculate the government's anticipated resources, with Prime Minister Putin insisting that the budget be based on a forecast oil price of $75 a barrel, while Kudrin—indentified as a fiscal hawk and a close ally of President Medvedev—maintains that it should be less than $70.

All sides of the Russian ruling elite, however, are committed to forcing through a significant lowering in the living standards of the population to shore up the economy and the federal budget. Furthermore, there is a universal understanding that in attempting to do so, the government will increasingly come into conflict with the sentiments of ordinary people. In the last two years, Russia has witnessed violent protests by miners and workers in decaying industrial towns, demonstrating against dangerous working conditions, low wages, and deplorable social conditions.

The recent passage of legislation in the Russian Duma expanding the powers of the FSB, the state security service, is significant in this regard. The FSB will soon be endowed with the right to issue warnings to anyone it suspects of being on the verge of committing a crime. Despite official claims that such measures are directed against terrorist extremists, they are directed against the working class in anticipation of mass social opposition.