

# FROM THE CHIEF EDITOR

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## The year of tough decisions

The third year of V.V. Putin's Presidency, his current third political cycle, is coming to an end.

It was a year of tough decisions, and this was what the President pointed out in his annual Address to the Federal Assembly of the Russian Federation on December 4.

Delivering his Address, V.V. Putin noted that in 2014 Russia faced trials that only a mature and united nation and a truly sovereign and strong state can withstand.

The historic reunification of the Crimea and Sevastopol with Russia, which was carried out in compliance with international law, and the efforts that Russia took in order to protect our compatriots in the south-eastern territories of Ukraine have caused massive economic and political pressure on Russia by the United States and its partners in Western Europe. This has been an attempt to talk with Russia from the position of strength. ***V.V. Putin said: "If for some European countries national pride is a long-forgotten concept and sovereignty is too much of a luxury, true sovereignty for Russia is absolutely necessary for survival"***. This approach expressed in the part of the Address devoted to foreign policy summarizes and streamlines Russia's foreign political course, which was pursued in 2012–2014. It is extremely important that this approach become a key factor increasing the consolidation of our society<sup>1</sup>.

The main focus of the Address was devoted to internal problems of Russia's development, and above all, to the execution of all the basic social obligations of the Government set out in the decrees of the President back in May 2012.

<sup>1</sup> According to the latest data provided by Russia's leading sociological centers, the level of support of V.V. Putin's performance as President of the Russian Federation at present is 85%. High approval of the President's performance is also registered in the dynamics of public opinion assessment carried out by ISEDT RAS in the Vologda Oblast.

Judging by many parameters of economic and social life, the situation at present cannot but arouse concern. According to many experts, Russia has entered a period of adverse economic conditions. Its resource-based economy causes high risks. These risks are increasing greatly under the external sanctions imposed on Russia, the ruble is falling and prices rising, which arouses continuing anxiety in the society. But for many years the Government of the Russian Federation has been doing virtually nothing to handle the problems connected with the structural and technological transformation of the economy. The Government does not pay attention to the experts and political parties that sharply criticize it for its commitment to liberal principles of organization of state administration<sup>2</sup>.

<sup>2</sup> See, for example: Grinberg R.S., Gorshkov M.K. Dvadsatiletie rossiiskikh reform v otsenkakh ekonomistov i sotsiologov (dvadsat' tezisov o glavnom) [Twenty Years of Reforms in the Assessments of Economists and Sociologists (Twenty Theses on Most Important)]. *Mir peremen* [The World of Transformations], 2012, no. 1; Amosov A. Kak preodolet' otstavanie v razvitii [How to Overcome the Lag in the Development]. *Ekonomist* [The Economist], 2013, no. 8; Gubanov S. Avtonomnaya retsessiya kak final'naya faza sistemnogo krizisa Rossii [Autonomous Recession as the Final Stage of the Systemic Crisis of Russia]. *Ekonomist* [The Economist], 2013, no. 9; *Na puti k sovershennoi dinamichnoi i effektivnoi ekonomike: doklad pod red. A.D. Nekipelova, V.V. Ivantera, S.Yu. Glaz'eva (v podgotovke doklada prinimali uchastie 25 deistvitel'nykh chlenov i chlenov-korrespondentov RAN)* [On the Way to a Perfect Dynamic and Efficient Economy: the Report, edited by A. D. Nekipelov, V.V. Ivanter, S.Yu. Glazyev (25 Full Members and Corresponding Members of the Russian Academy of Sciences participated in the preparation of the report)]. Moscow: RAN, 2013; Vinslav V. Proval'nye itogi—2013 — ocherednoi impul's k smene ekonomiko-upravlencheskikh reshenii [Disastrous Results of 2013 — Yet Another Push for Changing Economic and Managerial Strategies]. *Rossiiskii ekonomicheskii zhurnal* [Russian Economic Journal], 2014, no. 1, etc.

***“Fragmentarity and inconsistency of the national administration approach leads to the fact that instead of urgent change there is a continuous process of simulating transformations: change for the sake of process, and not for the sake of result. There is a widespread development of poorly coordinated pseudo-reforms. But most importantly, there is no effective independent public expert auditing institution, as well as no monitoring of the results of reforms implementation. This gives rise to a system in which the state apparatus acts in a totally irresponsible way toward the society. That is why instead of strategic foresight and design we observe only “forever immediate” response to immediate challenges”<sup>3</sup>.***

Instead of searching for ways to boost economic growth, the Ministry of Economic Development of the Russian Federation, in fact, only registers the recession and forecasts the decline of macroeconomic indicators; the data in *table 1* show it clearly.

According to the forecast that was made in May 2012, the gross domestic product growth rate in 2014 would be 104.4%, however, this rate was reduced to 100.5% in September 2014. The forecast rate of investment in fixed capital was 107.3 and 97.6%, respectively. In December 2013, the outflow of capital from the country was expected to be 25 billion U.S. dollars, and in September 2014 — 100 billion<sup>4</sup>.

<sup>3</sup> Gel'vanovkii M., Zakharov A. Obespechenie liderstva Rossii cherez rost konkurentosposobnosti [Ensuring Russia's Leadership through the Growth of Competitiveness]. *Ekonomist* [The Economist], 2014, no. 11.

<sup>4</sup> According to a recent statement by the Chairman of the Central Bank of Russia E. Nabiullina, the outflow of capital will reach 120 billion U.S. dollars this year.

Table 1. Forecast of the main macroeconomic indicators of the Russian Federation for 2014, as a percentage of the previous year, in comparable prices

Indicators	Date of provision of the forecast					
	11.05.12.	12.09.12.	12.04.13.	23.10.13.	27.12.13.	26.09.14
GDP	104.4	104.3	103.7	103.0	102.5	100.5
Industrial production index	104.1	103.7	103.4	102.2	102.2	101.7
Investment in fixed capital	107.3	107.3	106.6	103.9	103.9	97.6
Inflow (+), outflow (-) of capital, billion U.S. dollars	30.0	30.0	0	-25.0	-25.0	-100.0

Source: RF Ministry of Economic Development.

The developments of the Ministry of Finance of the Russian Federation have substantial deviations from the reference indicators and forecast parameters of the budget process.

This is particularly evident with regard to the consolidated budgets of the RF subjects (*tab. 2*).

The deficit of the consolidated regional budgets relative to their own revenues based on three years (2014–2016) was forecast to

be 212.3 billion and now it is expected to be 500.8 billion rubles, or almost twice as large. The amount of regional budgets' own revenues will be reduced by 7% in a comparable estimate.

The crisis of regional budgets is evidenced even more clearly in the dynamics of key indicators such as the amount of profit, profit taxes, and especially the growth of public and municipal debts of regions (*tab. 3*).

Table 2. Key forecast parameters of consolidated budgets of the subjects of the Russian Federation in 2014, billion rubles (in 2014 prices\*)

Parameters	Forecast			2014, estimation of expected parameters	Dynamics of estimate for 2014 in comparison with forecasts			
	2012–2014	2013–2015	2014–2016		2012–2014		2014–2016	
					billion rub.	%	billion rub.	%
Revenues	8384.5	9370.6	8485.4	8149.6	-234.9	-2.8	-335.8	-4.0
Own revenues	7413.3	8242.3	7186.8	6682.2	-731.1	-9.9	-504.6	-7.0
Deficit	-9.0	-81.9	-212.3	-500.8	+491.8	+55.6 p.	+288.5	+2.4 p.

\* Forecast level of inflation in 2014 was: in the forecast for 2012–2014 – 105%; in the forecast for 2013–2015 – 105%; in the forecast for 2014–2016 – 104.8%; expected level of inflation in 2014 – 107.5%.

Table 3. Key indicators of the budget process in the Russian Federation regions, billion rubles

Indicators	2011	2012	2013	2013 in % to 2011
Profit	8793.6	9213.0	8494.0	96.6
Profit tax	1927.9	1979.9	1719.7	89.2
Public and municipal debt	1387.3	1596.7	2026.4	146
Debt burden, %	23.8	25.0	30.8	+7 p.p.

Sources: RF Finance Ministry; Federal Treasury; Rosstat; ISED T RAS calculations.

The amount of this debt was 1387.3 billion rubles in 2011; but in 2013 it reached 2026.4 billion rubles, i.e. increased by almost 1.5 times. The debt burden on regional budgets increased from 23.8% in 2012 to 29.3% in 2014 (according to the data for 10 months). The debt load in a significant number of regions exceeds the annual amount of budget revenues.

Possible reserves for significant increase in tax revenues, and consequently, decrease in the public and municipal debt and strengthening budget security are not used<sup>5</sup>. Research and expert estimates<sup>6</sup> show that many private owners, especially oligarchic structures, use “loopholes” not regulated by the legislation and minimize their profit by formally increasing production costs, moving a significant part of created value added in the offshore, and by using other “profitable” tools, the origins of which are formed as a result of flaws in the public administration system in the country.

<sup>5</sup> See: Petrov Yu. Deofshorizatsiya ekonomiki, protivodeistvie “minimalizatsii nalogov” i presechenie utechki kapitala (vozmozhnosti sistemno-innovatsionnogo podkhoda k ekonomicheskoi politike) [Deoffshorization of Economy, Countering “Tax Mitigation” and Preventing Capital Flight (Opportunities for Systems and Innovative Approach to Economic Policy)]. *Rossiiskii ekonomicheskii zhurnal*, 2013, no. 6; Dmitrieva O. Ekonomicheskie krugooroty i finansovye pylesosy [Economic Turnovers and Financial Vacuum Cleaners]. *Voprosy ekonomiki* [Issues of Economy], 2013, no. 7.

<sup>6</sup> The studies include those conducted in recent years by ISEDT RAS and devoted to the analysis of the activities of the largest ferrous metallurgy corporations in Russia. See, for example: Ilyin V.A., Povarova A.I. *Problemy effektivnosti gosudarstvennogo upravleniya. Tendentsii rynochnykh transformatsii. Krizis byudzhethnoi sistemy. Rol' chastnogo kapitala. Strategiya 2020. Problemy realizatsii* [Public Administration Efficiency. Market Transformation Trends. Crisis of the Budget System. Role of Private Capital. Strategy-2020: Implementation Issues]. Vologda: ISERT RAN, 2014. 188 p.

The turmoil on the currency exchange that happened in December 15–16, 2014 showed the absence of coordinated actions between the Government and the Central Bank of Russia.

The journal “Expert” characterizes their level of mutual understanding as follows: “Not a week passes without the Government and its individual members, the Central Bank and some of its leaders making another forecast that “adjusts” all the previous ones. The outflow of capital from Russia will be so many billion this year; oh no, it will sooner be so and this much; no, it will rather be so and this much and a quarter of this much... Inflation this year will be so much per cent per annum; no, it will be a bit higher; no, it seems to be a double figure; no, a very double figure”<sup>7</sup>.

Under such a system of management, the Government, of course, finds dozens of reasons justifying its failure to execute the Presidential decrees of May 7, 2012.

The President expressed his dissatisfaction with the performance of the Government in his Address to the Federal Assembly of the Russian Federation of December 12, 2013. ***“A year and a half has passed since the executive orders were issued. You know what I’m seeing? Either things are being done in a way that elicits a negative reaction among the public, or nothing is done at all. Clearly, we will fail to achieve our stated goals with this kind of work”***<sup>8</sup>.

Unfortunately, by the end of 2014 the state of affairs in the financial and economic

<sup>7</sup> Privalov A. Ob uverenosti v zavtrashnem dne [About Confidence in the Future]. *Ekspert* [The Expert], 2014, no. 51 (928).

<sup>8</sup> *Address of President V.V. Putin to the Federal Assembly of the Russian Federation on December 12, 2013.*

sphere has deteriorated significantly. And the President, delivering his 2014 Address, again set a new range of economic objectives before the Government and federal and regional elites; these objectives take into account the actual external factors in the country's development.

Great concerns are raised with regard to the fact that these new guidelines set out by the President will be achieved if the current inefficient state administration system based on the extremely liberal financial-economic bloc of the Government is preserved, since *“the vulnerability of*

*Russia's finance was already evident during the crisis in 2008, and yet, five years after that, we continue to follow the same disastrous course”*<sup>9</sup>.

2015 will most likely be a year of tough decisions for the President, for the Russian citizens and for the country.

It is very important that the President's decisions be timely, coordinated, and supported by the voters, just like they supported the return of the Crimea to Russia – its “native harbor”.

<sup>9</sup> Redaktsionnaya stat'ya “Snova opyat'” [Editorial “Again and over Again”]. *Expert* [The Expert], 2014, no. 51.