

Reuters

ANALYSIS

Welfare the big idea for Russia's Medvedev

By Douglas Busvine

MOSCOW, Jan 16 - After a decade of rapid economic growth fired by the animal spirits of unfettered capitalism, Russia isn't about to turn back into a Soviet-style cradle-to-grave welfare state.

But, judging by the rhetoric of president-in-waiting Dmitry Medvedev and his patron, Vladimir Putin, life may be about to get better for the millions of Russians still scraping a living 16 years after the demise of the Soviet Union.

Medvedev, who leads Kremlin initiatives to fix housing, healthcare, education and farming, is poised to win election by a landslide on March 2 after Putin -- barred by presidential term limits -- endorsed his 42-year-old protege.

In an already one-sided campaign, Medvedev is touring the country telling Russians they deserve a better deal. Visiting a naval base in the Arctic port of Murmansk, he vowed to shake up Russia's "extremely unsuccessful" pensions system this year.

Critics might dismiss Medvedev's pledge as cheap propaganda targeted at a voter constituency numbering nearly 30 million, out of Russia's population of over 140 million, that could rally to communist presidential challenger Gennady Zyuganov.

SERIOUS ACTION

But Russia would have to act to shore up living standards even if there weren't an election around the corner.

The incomes of working Russians are rising rapidly as export petrodollars trickle down into the economy. Pensions, however, average less than a quarter of the typical monthly wage of nearly \$600. Many old people still work or rely on their families for support.

"The gap between pay and pensions is growing and the most pressing need is to correct that," said Yevsei Gurvich, who heads the Economic Expert Group and advises the government.

Inflation, meanwhile, is on the rebound after ending last year at 11.9 percent. Without remedial action today's pensioners could suffer a fall in living standards.

And Russia's attempt to create an additional 'funded' pensions pillar, to enable people born after 1967 to save for their own retirement, has flopped.

Only a fraction have opted to take out a private pension. The rest still pay into the National Pension Fund, whose returns fail to keep up with inflation because it is only allowed to invest in highly-rated bonds.

GETTING IT RIGHT

Reforming pensions is the right thing to do because incomes and pensions have lagged growth in company profits during the Putin boom, argues Roland Nash, chief strategist at Renaissance Capital in Moscow.

Money is no object either, as Russia has a huge oil windfall from which it can draw. But get it wrong, and higher inflation and a further widening of the yawning gap between rich and poor could be the unintended results.

"If it's funding future pensions and setting up a decent system then that's wise," argues Nash. "If it's just going out and spending, that's a different issue."

One proposal already aired is to reform the main payroll tax, the Unified Social Tax, to make it a flat-rate 26 percent charge. The tax is now regressive, falling as earnings rise.

That, said Gurvich, would be enough to peg pensions to pay at current levels but not enough for them to catch up. He said the reform debate was unlikely to be wrapped up before the presidential vote.

STABLE TEAM

That makes the prospective line-up of a Medvedev government critical to Russia's reform prospects -- especially as he has already offered the job of prime minister to Putin, by far the more powerful and popular politician.

Putin has thrown his weight behind social reform, telling lawmakers on Tuesday that his goal of turning Russia into the world's No.5 economy by 2020 would facilitate a social development strategy worthy of the name.

A cabinet reshuffle last autumn has strengthened an economic team headed by Finance Minister Alexei Kudrin that could be ready to hit the ground running on social reforms as soon as the political transition is complete.

But with Kudrin's pivotal deputy, Sergei Storchak, in jail facing charges of fraud and embezzlement, one of Russia's periodic bouts of institutional paralysis could yet derail a fresh attempt to tackle social reforms.

"The fact that a deputy finance minister can be charged with those offences is not comforting," said Ed Parker, a sovereign analyst who follows Russia for Fitch Ratings in London.

After his re-election four years ago, Putin launched reforms to streamline poorly targeted Soviet-era benefits. Pensioners took to the streets and the Kremlin was forced to climb down.

Despite that patchy record, Ivailo Vesselinov, a Russia economist at Dresdner Kleinwort, takes the pledges to raise living standards seriously. "With Putin, we always believe it's best to take him at face value," he said.

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