

**ASSESSMENT OF POLICY MEASURES TO SUPPORT RUSSIA'S REAL ECONOMY**

Moscow, April 2009

## **Abstract**

This paper presents the results of an analytical project on the design and approval of methodology for assessing and monitoring the anti-crisis measures taken by the government of the RF. The paper is based on an analysis of about 100 measures for support of Russia's real economy, which were initiated in October 2008 – March 2009. Within the scope of this analysis, we singled out the main beneficiaries by industry and enterprise scale, and estimated the effects of the measures underway in the crisis phase and in the phase of a return to economic growth. The paper also gives an account of the major risks the Russian government will face in putting into practice the measures supporting the real economy, and reveals the key problems and inconsistencies of the anti-crisis program.

**Key words:** anti-crisis measures; methodology of assessment; Russia; real economy; beneficiaries of the state support.

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## Foreword

The global economic crisis has challenged every government throughout the world. Although huge financial resources have been utilized to combat this crisis, so far no country has managed to find a prescription for a way out. The search for effective solutions that could minimize and overcome its aftermath is closely related to working out new ideas and recommendations for anti-crisis measures. This was the very task the government of the Russian Federation has been focused on in recent months, along with the fast implementation of a package of emergency measures. However, we believe that today, when scores of anti-crisis measures have entered their practical stage, the time has come on the one hand, to launch more sophisticated *mechanisms for monitoring these measures, and, on the other hand, to include procedures for special preliminary evaluation into the creation and inter-agency endorsement of new anti-crisis measures.*

The reason for taking such a step is our awareness that the resources and reserves available for the support of the economy are limited, particularly in a situation where the quickest way out of the crisis is becoming less and less likely. This change will be a necessary precondition for yet another shift in economic policy away from ‘theatre-of-war weapons’ that are supposed to alleviate the immediate consequences of the crisis and repair the damage done to the most vulnerable sectors, towards ways of overcoming the crisis, creating incentives for entering new markets, expanding output and creating new jobs. A shorter horizon of economic policy was inevitable in the acute phase of the crisis. A regular overview of adopted measures and a better-structured preliminary assessment of new measures will help make this horizon longer and combine current policies with strategic priorities that were announced earlier by our government. The present report is the result of a joint project launched by the SU-HSE and the Interdepartmental Analytic Center for the creation and approbation of procedures for evaluating and monitoring the anti-crisis program. This study is already launched in developed countries. Moreover, international organisations have already launched a comparative analysis of fiscal policy response to the crisis in a number of countries (OECD 2009, chapter 3). However, Russia is not yet included into these studies. The only exception we are aware of is the World Bank Russian Economic Report published in March 2009. This report gives the first description of anti-crisis measures in Russia in comparison with the programs that are being implemented in other countries. However, the World Bank Report is focused on general overview of economic situation in Russia and contains a very brief analysis of anti-crisis measures. On the contrary, in our study we centered our attention on the measures for support of the real economy and tried to single out beneficiaries by industry and enterprise size, and to give a comprehensive assessment of the outcomes that the measures under way will produce during the recession and at the time of recovery from the recession. We also defined the main risks the Russian Government will face in

practical implementation of support of the real economy and revealed the key problems and inconsistencies of the anti-crisis policy.

This project was carried out in a very short time span in February-March 2009, and it imposed a number of limitations and bifurcation points on the authors. Firstly, we had to choose between detailed procedures and a swift achievement of practical results. Being aware that the proposed approaches to an assessment of anti-crisis measures are far from being ideal, we chose to test this set of tools right away on a relatively wide range of measures, instead of honing the procedures to an evaluation of several examples of concrete measures. Secondly, we faced a choice between a detailed, all-inclusive assessment of the measures announced by the government (taking several months and involving drawing in a larger number of experts), and a swift evaluation of a set of interrelated measures on a unified schedule and unified and simplified range of characteristics. We took the second option as the more reasonable one, making “express diagnostics” of about 100 measures designed to support the real economy. Meanwhile, measures to support the financial sector, some actions in support of people’s livelihood and other measures fell outside our attention, mainly because our time and human resources were so limited. We used only public data although in this we could evaluate some measures less correctly than our much better informed colleagues in economic agencies could do. Finally, one of the limitations we faced was that each measure was evaluated by a single expert, so that the obtained results may include some subjective opinions.

Therefore, this was essentially a pilot project. Our major task was to offer and test a possible set of instruments for an evaluation of anti-crisis measures. At the same time, we believe that we have successfully achieved positive practical results even at this pilot stage. Our approach has enabled us to analyze a wide spectrum of policy tools, to evaluate their relative pluses and minuses, and to define the risks related to their application. Reliance on this analysis has enabled us to identify a number of problems that are typical of the anti-crisis program, and to formulate recommendations for their removal or alleviation.

We accept that some of our conclusions will be met with criticisms, and we recognize the targets for possible criticisms. At the same time, we hope that the proposed approach will meet a constructive response, both from the expert community and from our colleagues in the government. Today, a competent public discussion of the anti-crisis program and an evaluation of its expediency is highly important. In this context, it is noteworthy that on March 19, the federal government itself offered its Program of Anti-Crisis Measures for 2009 for discussion. We sincerely hope that our project will be the first step towards the organization, in the framework of our government, of a regular system for an evaluation of anti-crisis measures, and will therefore, help upgrade the effectiveness of economic policy.

## **Impact of the Financial Crisis on the Russian Economy**

For a better understanding of the context in which the anti-crisis measures are being implemented in Russia, we must give a brief account of the general economic situation in Russia in 2008-2009. The global crisis affected Russia later than other countries, and till the mid-2008, Russia's economic growth rates stayed high, following the trend of the preceding nine years (the average annual GDP growth rate in 1999-2007 was 7%; in 2007 the rate was 8.1%). The crisis first manifested itself when in August, stock indexes went sharply down, coming to a market crash in September. As a result, the leading RTS stock market indicator fell by a quarter (from almost 2,500 points in the beginning of May to less than 600 points in the late October, 2008). This steep decline posed problems for the financial sector because banks extensively borrowed foreign money on share packages. A number of big banks hovered on the brink of bankruptcy, and a panic started among their depositors.

Nevertheless, prompt assistance from the Government and the Central Bank helped stabilize the situation in the financial sector by November, despite increasing inflationary pressure on the rouble. As a result, by the end of autumn 2008, the probable economic slowdown and the need to settle the external debts of Russian corporations, along with rising inflation, were believed to be the major challenges for the Russian economy.<sup>1</sup> Meanwhile, economic growth forecasts for 2009 were generally positive. For instance, Sergei Aleksashenko, a well-known Russian expert, former Deputy Governor of the Bank of Russia, believed in November that the GDP growth in 2009 would be no higher than 2.5 per cent (Aleksashenko 2008, p.34); the World Bank saw GDP growth at 3 per cent based on unchanged oil prices around US\$75 a barrel (World Bank 2008, p.17), and the November outlook by the European Commission for Russia gave growth at 6 per cent in 2009 and 6.5 per cent in 2010 (DG ECFIN 2008, p.137).

However, in reality, the outcome of the crisis was much more severe. As stated in the Russia Economic Report released by the World Bank in March 2009, the decline in global demand, the fall in commodity prices, and the tightening of credit have accelerated Russia's economic slowdown since the fourth quarter of 2008 (see the table 1). Estimated real GDP growth in the fourth quarter of 2008 was about 1.1 percent, down from 9.5 percent during the same period in 2007. With few exceptions, all sectors reported lower growth rates in 2008, but tradables are slowing faster, in line with collapsing global demand. These sectors grew by only 1.8 percent in 2008, compared with 3.9 percent in 2007, with growth in manufacturing turning negative in late 2008. Nontradables — driven mainly by retail and construction—sustained growth of 7.4 percent for 2008, compared with 10.3 percent growth in 2007.

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<sup>1</sup> As mentioned by Aleksashenko (2008), the total external debt of Russian companies and banks, as of September 30, 2008, was over \$510 billion, of which about \$200 billion were due before the end of 2009.

**Table 1. Main indicators of Russian economic development, 2006-09**

	2006	2007	2008	Q4 2008	Jan- 09	Feb- 09
GDP growth, %	7.7	8.1	5.6	1.1***	-8.8*	-7.3*
Industrial production growth, year on year, %	6.3	6.3	2.1	-6.1	-16.0	-13.2
Fixed capital investment growth, %, year on year	16.7	21.1	9.8	-2.3	-15.5	-14.1
Federal government balance, % GDP	7.4	5.5	4.0	4.0	15.0	2.6
Inflation (CPI), % change, end of period	9.0	11.9	13.3	13.3	2.4**	4.1**
Current account, billion USD	95.6	76.6	98.9	8.1	n/a	n/a
Unemployment, % (ILO definition)	7.2	6.1	6.3	7.1	8.1	8.5
Memo: Oil prices, Urals (USD/barrel)	61.2	69.5	95.1	54.9	44.2	43.1
Reserves (including gold) billion USD, end of period	303.7	478.8	427.1	427.1	386.9	384.1

*Source:* (World Bank 2009) on the base of Rosstat, CBR, Ministry of Finance, Bloomberg data.

\* Preliminary estimate by Ministry of Economic Development.

\*\* Cumulative from end-2008.

\*\*\* Preliminary estimate by the WB staff.

The economy deteriorated dramatically in early 2009. Demand- and finance-sensitive construction reported a 18.8 percent decline in January-February relative to the same period in 2008, while transport contracted by 18.2 percent. Retail trade reported modest growth of only 3.1 percent in January, but then registered a decline of 2.4 percent in February. Industrial production fell 10.3 percent in December 2008 relative to December 2007. It then dropped 16 percent year-on-year in January and 13 percent in February 2009.

Five of 14 major manufacturing industries reported output declines in 2008, with electronics, electrical, and optical equipment hardest hit (-7.9 percent), followed by textile and sewing (-4.5 percent) and by chemicals (-4.2 percent). Most of this dislocation took place in November and December 2008, when total manufacturing output respectively fell 10.3 and 13.2 percent (year-on-year). As credit continues to tighten and demand to fall, manufacturing is likely to contract further this year. According to recent statistics, manufacturing output dropped 24.1 percent in January 2009, compared with January 2008, and 18.3 percent in February 2009, compared with February 2008.

Although average unemployment in 2008 remained relatively unchanged (6.3 percent in 2008 and 6.1 percent in 2007), it shot up to 8.5 percent in February 2009 (ILO definition), from 8.1 percent in January 2009 (and from a record low of 5.4 percent in May 2008). Real incomes also declined substantially at the end of 2008 and the beginning of 2009. In the fourth quarter of 2008 alone, real disposable income dropped 5.8 percent, compared with the same period in 2007, and 10.2 percent in January 2009 (year-on-year).

It appears that a large share of additional liquidity, initially provided to the financial system was immediately converted into foreign currency, putting more pressure on the rouble. In November the Central Bank of Russia started to allow increasingly frequent step depreciations resulting in a 28% decline in the rouble against the US dollar-euro basket in late January. The CBR tightened monetary conditions in early February 2009 to prevent further loss of foreign exchange reserves. However foreign exchange reserves fell to about USD 380 billion in mid-March 2009, from its record of more than USD 580 billion in September.

The fiscal position of Russia has worsened considerably, and the Ministry of Finance in early 2009 has released the main parameters of its revised federal budget for 2009. It is prudently based on the low oil prices (US \$41 a barrel, Urals) and a drop in budget revenues from the original 21.2 percent of GDP (under the old assumption of US \$95 a barrel) to 16.6 percent, or RUB 6.72 trillion. At the same time, expenditures will be increased by RUB 667.3 billion to RUB 9.69 trillion, to produce a deficit of RUB 2.98 trillion (about 7.4 percent of GDP), a massive reversal of the fiscal position from the 4.1 percent surplus in 2008. The consolidated general government deficit is expected to be 8 percent in 2009 deficit and will be financed largely from the Reserve Fund (7 percent of GDP) with modest domestic borrowing (up to 1 percent of GDP).

As a result, according World Bank estimations, due to much worse global financial outlook and oil prices in the USD 45 a barrel range the Russian economy is likely to contract by 4.5 percent in 2009 (World Bank 2009, p.6-7). However, the OECD refrains from making precise forecasts for Russia (OECD 2009, p.101-103), and the Ministry of Economic Development of the RF predicts a GDP decline by 2.2 per cent in 2009.

At the same time, the Ministry, in its report on the current economic situation released in May has pointed out that, according to the January-to-April data, the scale of GDP decline is getting smaller (Ministry of Economic Development 2009). The data from current surveys of industrial enterprises show that the situation has already stabilised since January-February 2009 (IET 2009), and a more detailed analysis of output by commodity shows that in a number of sub-industries, economic growth has already resumed (Ekspert 2009).

## Some Results of Expert Assessments of Anti-crisis Measures

1. The total volume of additional RESOURCES that were appropriated to support the real economy is estimated at 2.1-2.5 trillion roubles for October 2008 – December 2009 (about 100 policy steps were announced by the Federal Government along this line)<sup>2</sup>:

- 1.1-1.2 trillion roubles for widening access of entities in the real economy to financial resources (including the volumes of injections in the capital of public development institutions for financing of the real economy and the volume of government loan guarantees);
- 500-700 billion roubles for the reduction of burden on businesses
- 250-300 billion roubles for the alleviation of negative social effects and development of labor market;
- 180-230 billion roubles for the expansion of domestic demand;
- 60-90 billion roubles to support small and middle-sized enterprises.

The main emphasis of the anti-crisis program is given to incentives for lending to the real economy – the share of relevant measures is about a half of total resources in the anti-crisis package. Another quarter of the resources are given to reducing tax burden. Measures for support of domestic demand (no more than 10% of total resources in the anti-crisis package) look quite scanty against this background.

2. Judging by the composition of these measures, the industry-wise priorities of the Anti-crisis Program are automobiles, agricultural machines, the defense-industrial sector, agribusiness, housing construction, and, taking into account reallocated resources, oil and gas. So far, chemicals, logging and woodworking, light and food and some other industries have been left outside the Anti-Crisis Program.

3. The Anti-Crisis Program focuses on supporting large-scale companies and micro-businesses, while MIDDLE-SIZED enterprises are left out of the sphere of attention: according to expert assessments, a half of these measures are related to support of large and super-large enterprises; these measures account for 60% of total resources in the anti-crisis package; and about a third of the measures is intended for support of small businesses, but their aggregate weight in total resources is just only 5% of all measures assigned for their support.

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<sup>2</sup> We have to notice that our quantitative estimates slightly differ from the estimates of the volumes of tax and fiscal anti-crisis measures and their distribution among the lines of support that are given in the World Bank Report [World Bank 2009, p. 9-11]. This disparity is due to some differences in methodology – in particular, we analysed the announced measures in details and took their content into account in their classification (to specify, see the section “Main Ways and Procedures for Evaluating Anti-Crisis Measures”). Nevertheless, our conclusions are the same on the qualitative level.

4. In general, these policy steps are COMPENSATORY MEASURES intended to curb the losses made by large companies (as a rule, without any definite behavioral conditions). Much less attention has been given to support potentially competitive companies. There is also a certain shortage of measures, as well as resources, in such policy lines as incentives for innovations and technological modernization, support of high-tech exports, and the development of a competitive environment. So far, there have been no significant action to SUPPORT COMPANY GROWTH, to develop new sectors in the economy, or to upgrade performance of natural monopolies and large-scale state-owned companies.
5. At the same time, a number of strategic measures that had been planned earlier were rapidly put into practice under the auspice of the Anti-Crisis Program. In particular, these are: the further development of corporate legislation; the support of small and middle-sized businesses; lowering of administrative barriers to businesses and improvements in tax regulation. Among strategically meaningful measures, we can also mention the development of leasing and the improved regulation of the bond market. In this connection, it should be noted that, according to experts, about 7% of all measures will have a DELAYED EFFECT: although their anti-crisis effects are considered to be low, their role will probably become important and positive in the phase when the economy is recovering from this recession.
6. Implementation of the Anti-Crisis Program relies mostly on tools of industrial policy (70% in terms of assigned resources), which are for the most part selective ones, while systemic tools are limited. In this connection, many measures need high-quality manual control and a highly skillful choice of recipients, and for that reason pose great risks of administrative failure (40% of all measures).
7. The experts point out that about 20% of all measures will have a dual effect over time: they will be most likely positive during the downturn, but negative as soon as the economy reverts to growth. Some of these measures, the experts believe, can bring “inefficient equilibria” that will be quite costly to get rid off. Detection of such possible “traps” is a necessity in order to prepare in advance a set of additional measures for post-crisis development.
8. The anti-crisis effect is estimated as “strong” only for 10% of all measures, and as “moderate” for another 30%. We believe it is natural that the higher the assessment of an anti-crisis measure is, the more often this measure is claimed as most likely to work ambivalently. The greatest risk mentioned by experts was the danger of the deterioration of a competitive environment. At the same time, there is still some room for improving the efficiency of the declared measures and for curbing the possibly negative effects of their implementation. The experts believe that the potential effect of a number of the measures already taken is strongly restricted by their practical

design and tuning (legal conditions, procedures, boundaries, criteria), by the underdeveloped mechanisms of their implementation and by the inadequacy of monitoring requirements.

9. More than 40% of the measures that are being taken now more or less conflict with the “pre-crisis” approaches to the strategic goals of social and economic development. This does not seem to be a major problem, because the crisis is unique, and many measures are temporary. However, the temporary nature of certain measures, together with a lack of criteria (and conditions) for their cancellation, makes business conditions less predictable. Moreover, in the future, the cancellation of some concrete “tactical” measures is highly likely to face resistance by some vested interests. For this reason, on the one hand it is highly important to keep tactical “deviations” from the existing strategy under control, and on the other hand, in some cases, to develop new alternative approaches to the long-term goals of social and economic development.

## Introduction

Since October 2008, the Government of the Russian Federation has turned to the initiation and accomplishment of policy steps for minimizing the negative impact of the global financial crisis on the Russian economy. Up till now, the Government has devised and is putting into practice a most extensive range of anti-crisis measures, which is unique in terms of the diversity of ways of influencing the economy, and also in terms of the volume of allocated resources.

After the most urgent problems relating to the stability of our financial system are solved and the cycle of emergency mergers is completed, and as soon as the duration of the crisis is fully recognized, a *systemic evaluation* of the government's anti-crisis measures will come to the fore. In addition, suggestions on how to improve anti-crisis policies in the making and in practice will have to be made.

In the framework of this project, evaluation of anti-crisis measures had been roughly accomplished by March 15, 2009, before the Federal Government presented its Program of Anti-crisis Measures for 2009 (on March 19, 2009). This Program identified seven policy priorities, and classified the ongoing and planned measures according to the priorities.<sup>3</sup> However, the vast majority of these measures were declared earlier and are already evaluated by experts.

In our opinion, what is essential and needed in practice today is not so much a critical appraisal of the separate measures being implemented which were inevitably designed rather chaotically (especially in their initial stage), as the establishment of basic rules and approaches that will make *further* anti-crisis actions more effective and fruitful. This is particularly important now when *resource limitations are getting more stringent*. We have to emphasize that for us, the evaluation of problems and risks related to the anti-crisis measures under way has nothing to do with claims that 'the adopted measures are bad, but we know the good ones'. We are convinced that practically each anti-crisis measure comes together with substantial risks. These risks are different, and they need to be duly recognized so that their possibly negative effects can be limited.

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<sup>3</sup> According to Anti-crisis Program (2009) following priorities were announced: 1) The Government will fully honor its commitments to the public. Special attention will be paid to preserving the labour potential. 2) The industrial and technological potential of the future growth should be preserved and strengthened. The Government will not invest tax-payers' money in ineffective production lines. 3) Domestic demand should become the foundation of post-crisis recovery and subsequent steady advance. During the crisis, the Government's support for domestic demand (investments and contracts) will play an increasing role. 4) Main task on the road to modernization is to change the current model of economic growth. The Government will support major innovations-based processes, including higher energy efficiency of the economy. 5) Business should be freed from pressure of officials. It will also propose a new package of measures to enable small businesses to make steady progress despite the crisis. 6) The economy should rely on a powerful national financial system. 7) The Government and the Central Bank will conduct responsible macro-economic policy.

Assessing anti-crisis measures, we focus our attention not on a discussion of their suitability but on an evaluation of the regulatory tools that are being used, as well as the relevant *rules and mechanisms* that ensure their accomplishment. We choose this approach for a number of reasons:

- ✓ Each type of policy (for instance, taxes, customs tariffs, fiscal measures) and related tools have their own limitations and advantages (speed of realization, complicity of management, etc.);

- ✓ Groups of tools have a functionally different capacity for the allocation of benefits to economic agents (systemic and selective mechanisms). The successful usage of certain mechanisms basically depends on the general institutional environment (conditions for fair competition, etc);

- ✓ Changes in the existing instruments and the creation of new policy tools can substantially alter the ‘rules of the game’ for economic agents and have a long-term influence on Russia’s economic development. (The effects of certain instruments can prove to be fundamentally different in times of crisis and growth; there are risks of ‘institutional traps’). When financial resources are shrinking, a possible bias towards “moneyless” (regulatory) measures may fundamentally change the conditions for economic activity;

Certain tools (in the first place, those belonging to industrial policy) tend to divide economic agents into ‘those who won’ and ‘those who lost’ from anti-crisis measures, owing to their industrial affiliation and scale of business. This division can be explained not only by the redistribution of public resources but also by the changing ‘rules of the game’.

In general, we are working on the assumption that discussion of the very tools for the realisation of anti-crisis measures can prove to be pragmatic and productive and can create opportunities for building into the system of decision making certain procedures for a structured evaluation of measures.

## 1. Main Ways and Procedures for Evaluating Anti-crisis Measures

At the outset, let us point out that we are not going to examine the anti-crisis program from the position of its actual effect on the entire real economy or on some of its sectors. In many cases, this effect is too early to be measured. Besides, this task would be too complex and too large for this short-term project. We have focused the attention of our experts on the evaluation of *probable limitations, problems and risks* related to carrying out the anti-crisis program in two main dimensions:

(1) The formulation and implementation of anti-crisis measures, including such qualities as

- Timeliness, speed of formulation and implementation;
- Interaction with the business community in recognition (selection) of possible measures, as well as in the assessment of their outcome;
- Transparency of the formulation and implementation of the measures and the visibility of achievements;
- Predictability and clear sequencing of steps, and their capacity to complement the long-term strategy of development;

(2) key characteristics of the anti-crisis measures, in particular:

- The range of potential beneficiaries, and the conditions for their fair competition for support;
- Simplicity of administration, clearness of procedures, limitations on access, and transparency ;
- Availability of leverage (mobilization of private resources), risk sharing, presence of motivation for recipients to use their internal reserves, and the formation of positive modes of conduct;
- Possible future costs of the measures when the economy resumes growth.

Our analysis of the anti-crisis program is based on the following general *theses*:

- There are no “ideal” measures, but possible risks must be fixed; the potential effect of the most brilliant ideas can be strongly limited by the actual design of the adopted regulations and their subsequent administration ;
- The adopted measures are possibly (and sometimes inevitably) able to have conflicting effects in different sectors, but the areas of possible conflicts must be clearly defined; there are no crises without losses, but it is important to know how benefits and costs will be distributed among groups of companies and enterprise stakeholders, and how this distribution will be influenced by the adopted measures;

- It is often very difficult to estimate the actual effects (influence) of certain measures, but it is important to organize their efficient monitoring and make provisions for their tuning;
- Certain tactical measures have typically high costs of exit (cessation), and certain measures will inevitably run counter to some former approaches to the strategic tasks of Russia's economic development. For this reason, new ways and procedures will be required from time to time to cope with these tasks;
- The formulation and implementation of anti-crisis measures often call for an immediate reaction, manual control, and “volitional decisions”. However, this must be balanced with the higher requirements of transparency of options and substantiation of preferences.

The gist of our approach is *to make a “thorough” expertise of all measures in question in a single format* in the following basic directions:

- Instruments that are used for putting a measure into practice; their functional orientation; time-frame; approximate volumes of fiscal expenditures (lost revenue);
- Assessment from the position of correspondence to or departure from the long-term guidelines (principles) of government policy that were established earlier;
- Identification of the main types of beneficiaries and losers from the realization of the measure (by industry, scale of business, etc.);
- Assessment of underlying motivation (incentives for expansion and innovation for business enterprises); the presence of any behavioral requirement;
- Assessment of major risks (distorted ‘rules of the game’; higher uncertainty in the business environment; restricted competition; non-transparency of application; conditions for making opportunistic decisions; difficulties in management and tuning);
- Detection of possible ‘traps’, which can appear as soon as the economy resumes growth (risks of formation of “ineffective equilibria”);
- Detection of factors that can influence the efficiency of the measure (owing to its design, its need for tuning, influence of other measures and external institutional environment);
- Comparison of peculiar effects of the measure (instrument) in the crisis phase and in the phase of the return to economic growth.

### **Sequence of assessment**

*In the first stage*, we prepared and discussed a closed list of features of those measures that could be appropriate for expert appraisal. As a result, we set up a ‘format of assessment’, which includes a ‘certificate of the measure’ containing its formal parameters (legal texts that regulate realization of the measure; its time-frame, duration, an official estimation of resources, etc.) , a “format of expertise” containing an assessment of its attributes (main beneficiaries, risks related to implementation, its anti-crisis effect and its effect in the phase of exit from the crisis), and also a general conclusion of our experts

about this measure. At the same time we compiled a preliminary list of the measures liable for assessment, which was later corrected and expanded by our experts.

*In the second stage*, we identified the experts (groups of experts) according to the composition of the measures, and held consultations about the implementation of expertise. The expertise of anti-crisis measures was conducted in the established format in the period March 1-15, 2009. After that, we compiled summary tables with assessments of all measures. We obtained a database for analysis, overview and conclusions.

With regard to assessment of anti-crisis measures, naturally enough, we had to define their range. This turned out to be not as easy as it seemed at first glance. A number of measures now claimed as the anti-crisis ones were decided upon or discussed much earlier (such as changes in depreciation policy). One more problem is the abundance of quasi-state measures (relating to activities of large state-owned companies and systemically important banks) in the path of the government's anti-crisis policy : they are too opaque to be easily appreciated. Meanwhile, they are the very matters that can bring great distortions to competitive conditions and involve an unreasonable redistribution of resources. Nevertheless, we resorted to a formal rule for our preliminary selection, sorting out those measures that had been officially announced as anti-crisis ones<sup>4</sup>.

We used the following substantive criteria to select the measures to be analysed:

(1) The measures should be oriented towards the support (and development) of the real economy. We also examined the measures enhancing social welfare, supporting the labor market and expanding demand for goods (or services) of certain industries. However, we *didn't examine* measures that were meant to ensure the stability of the financial and banking systems or measures related to improving corporate laws;

(2) Implementation of the measures in question can substantially change the relative positions and behavior of economic agents, due to changes in the regulation and "tuning" of existing instruments, as well as the appearance of new instruments of government policy;

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<sup>4</sup> For a rather long while (November 2008 – March 2009) a single legal document existed which defined composition of the anti-crisis measures, their schedule times, and responsibility by ministry and agency. It was the Action Plan for Rehabilitation of the Financial Sector and Certain Industries, enacted on November 6, 2008. However, this Action Plan did not include a number of earlier measures, mostly related to tax policy and to some decisions that were made later, in particular, those related to automobile industry and agricultural machinery. In this connection, we also used the following documents: "Review of Anti-Crisis Measures for Rehabilitation of the Financial Sector and Certain Industries", placed on the official web-site of the Federal Government, and "List of Anti-Crisis Measures Being Implemented by the Russian Government and the Central Bank of Russia", placed on the official web-site of the Prime Minister. Recently (on March 19, 2009) a comprehensive "Anti-Crisis Program of the Government of the Russian Federation for 2009" was presented for public discussion for the first time. The Program is supplemented with a list of main anti-crisis measures taken by the Russian Government for rehabilitation of the Russian economy in 2009.

(3) Implementation of the measures in question will involve a substantial reallocation of public resources needed for the application of individual tools of government support.

As a result, we made *a list of about 100 arrangements, which had been claimed as anti-crisis measures* and which enabled us to evaluate the application of the instruments in use (either because regulations were being enacted, or because the measures were presented in clear and detailed wording)<sup>5</sup>.

The *informational base* for assessing anti-crisis measures was compiled from relevant *legislation* (laws, resolutions, directions, orders).

Our general principle has been to rely only on *the documents that are accessible to the general public*, including documents prepared for meetings of the federal government and transcripts (theses) of statements made by decision-makers, placed on official sites of the public administration<sup>6</sup>.

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<sup>5</sup> Some of the measures, according to application of a number of tools, were divided into “sub-measures” (for example, co-financing of regional programs for support of small and middle-sized enterprises, of co-financing of employment programs).

<sup>6</sup> We have to mention that official open information about Russian anti-crisis policy is abundant, but fragmented and placed piecemeal on a number of official sites of President, Government, ministries and agencies. Our work was made easier because many ministries conduct fairly open policy and have published theses and presentations made by their ministers and vice-minister on their web-sites.

## 2. Anti-Crisis Measures: Main Tasks

A large package of anti-crisis measures have been announced in a very short space of time (actually, since November 2008), which require not only the drawing up and adoption of a great number of legal acts but also the shaping of mechanisms for the manual control of certain instruments)<sup>7</sup>. Many measures were taken within strict time limits and under strongest pressure from various vested interests<sup>8</sup>.

As a result, *the public administration faced a much-increased workload, and on some occasions, the practical implementation of measures was de-synchronized*. For example, we can mention a great delay in government procurement orders with the result that the government was forced to help finance the largest systemically important companies and enterprises in the defense-industrial sector. What is most important, a gap opened up between the adoption of legal acts and the implementation of related measures, creating the impression that ‘there are many measures, but still no results’<sup>9</sup>. This possibly provided a stronger reason to design additional measures. So, arrangements for individual industries (sectors) and policy directions came in the mode of racing waves. By March 2009, the total set of anti-crisis measures appeared mixed and inconsistent. At the same time, it may be said that in its many aspects, the anti-crisis program helped accelerate a number of strategic policies that had been planned earlier, particularly in corporate law the support of small and middle-sized enterprises, and the improvement of tax administration.

In this connection, we considered it important to *reconstruct* the tasks of anti-crisis policy from the point of view of composition and features of the measures in question (see Table 2).

On the basis of our analysis, we can point out that the anti-crisis measures are centered on finding solutions to the following problems:

1. Expansion of access to financial resources (direct lending by government-affiliated banks and financial institutions for development, and the injection of public funds into these institutions; subsidizing interest rates and giving government guarantees of interest in order to provide incentives for private credit; giving recommendations to banks about lending; issuing shares and bonds and raising public funds to purchase these assets directly from the market by designated organizations).

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<sup>7</sup> Let us remind that the Program for Rehabilitation of the Financial Sector and Certain Industries, enacted on November 6, 2008, which includes only a part of all anti-crisis measures, contains 55 points (measures). According to this Program, documents related to 34 points were due as soon as in November, and related to another 10 points, in December.

<sup>8</sup> We can single out the following important measures that were taken in 2008: in December, refinancing of external indebtedness of major Russian companies; in November, endorsement of a package of laws for reduction of tax burden, changes in tax charge and improvement of tax administration; since November, enactment of a set of legal acts related to changes in rates of custom duties.

<sup>9</sup> At present, measures are under preparation to improve energy efficiency, to encourage innovations, to make further changes in taxation.

2. Reduction of the burden on businesses (a lower tax burden, lower rates of customs duties on exports; a lower administrative burden).

3. Easing of negative social consequences of the crisis and development of labor market (higher unemployment benefits, co-financing of regional employment programs<sup>10</sup>, and limitation on foreign labor).

4. Incentives for the expansion of domestic demand (government procurements, advances and preferences for domestic producers; procurements and investment programs of natural monopolists; leasing; customs protection and subsidized consumer loans).

5. Support of small and middle-sized enterprises (co-financing of regional programs for development of small and middle-sized businesses<sup>11</sup>, programs of lending from Vneshekonombank, the Bank for Development and Foreign Economic Affairs) and enhancement of competition.

We have to underline that a number of measures can hardly be related to a single designated task. For instance, some of the anti-crisis measures enhancing social welfare can also be regarded as expanding domestic demand for the production of certain industries and promoting enterprise activity.

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<sup>10</sup> Includes different lines; but the following are designated as priority lines: creation of temporary jobs (public works, on-the-job training), retraining of those who are likely to lose their jobs, assistance in moving to new places of work, support of self-employment and of small businesses.

<sup>11</sup> Includes a great number of lines, but the following are priority ones: subsidies to starting businesses, expansion of micro-credit, development of a system of guarantee funds and subsidizing of lending rates.

**Table 2 Anti-Crisis Measures of Greatest Resource :Volumes and Potential Effect on Real Economy**

Anti-Crisis Measures	1. Expansion of access to financial resources	2. Lowering of burden on business	3. Alleviation of social problems, development of labor	4. Creation of domestic demand	5. Development of competitive environment, support of SMEs	Estimated resources, billion rubles (October 2008-December 2009)
Lending by Vneshekonombank to Russian borrowers for refinancing their foreign loans against the pledge of assets in Russian territory	+					\$11,5 billion*)
Capitalization of the Agency for Housing Mortgage for expansion of mortgage	+		+			60
Capitalization of the Russian Agricultural Bank for expansion of financing of agricultural and grain market interventions	+					75**)
Changes in the Vneshekonombank Memorandum on financial policy in order to finance large-scale projects in agribusiness	+					60***)
Subsidies for repayment of borrowings by certain airline companies in order to support their operations	+					30
Credit guarantees to organizations for operating in the main areas of productive activity and capital investment	+					200
Credit guarantees to enterprises in the defense-industrial complex	+					100
Subsidizing interest rates on certain types of investment and short-term borrowings in agribusiness	+					17
Fiscal subsidies to enterprises in the defense-industrial complex for repayment of interest on borrowings made in 2008-2009, including borrowings for replenishment of working capital	+					15
Expansion of subsidies to enterprises in the defense-industrial complex for prevention of bankruptcies	+					3
Subsidies to enterprises in the defense-industrial complex for covering of costs or lost revenues on state-defense orders and government procurements	+			+		12
Expansion of subsidies to Russian exporters of industrial goods for partial reimbursement of interest on their borrowings	+					6****)
Subsidies to enterprises in agricultural machinery, automobiles and transportation machinery for reimbursement of interest on borrowings made in 2008-2009 and used for technological modernization	+					2,5
Subsidizing interest rates for consumer loans, used for purchase of automobiles made in Russia	+			+		2
Guaranteeing bond issue made by Russian Railways Co. by the Russian Government and Vneshekonombank for financing the company's capital investment programs	+			+		100
Assistance for the placement of bonds issues by Russian automobile companies with a guarantee from the Russian Government	+					60
Organization of additional issues of shares and bonds by certain strategically important enterprises	+					50
Subsidizing interest rates on borrowings of enterprises in fisheries and fish farming	+					1,1
Credit lines to leasing companies for Russian automobiles	+			+		1

<b>Anti-Crisis Measures</b>	<b>1. Expansion of access to financial resources</b>	<b>2. Lowering of burden on business</b>	<b>3. Alleviation of social problems, development of labor</b>	<b>4. Creation of domestic demand</b>	<b>5. Development of competitive environment, support of SMEs</b>	<b>Estimated resources, billion rubles (October 2008-December 2009)</b>
Guidance to commercial banks using different types of public support in allocation of their credit resources to defense enterprises, agribusiness and SMEs	+				+	
Recommendations to commercial banks using different types of public support for priority lending to certain industries: automobiles, agriculture machinery, air transportation, residential housing	+					
Limitation of increases in tariffs for products (or services) of natural monopolists		+				
Reduction in profit tax rate from 24% to 20%		+				294
Shortening of screening terms in calculation of customs duty rates for exports of oil		+				250*****)
Increase in depreciation of premiums for certain types of fixed assets from 10% to 30%		+				50,4
Increase in the non-taxable minimum of tax on mining of minerals from \$9 to \$15 per barrel of crude oil		+				104
Reduction in the period of acknowledgement of cost of licenses for use of mineral resources to 2 years, and for calculation of profit taxes		+				2
Granting tax holidays for mining of minerals in the continental shelf, in the Nenets Autonomous Area, on the Yamal Peninsula, and in Eastern Siberia		+				
Granting of the right to establish tax rates for simplified taxation schemes in the range of 5-15% to Constituent Entities of Federation		+			+	13*****)
Limitation of the number of inspections of business enterprises		+				
Protection of legal entities' and individual entrepreneurs' rights during the implementation of state and municipal control (supervision)		+				
Limitation of rates of increase in tariffs on products of natural monopolies		+	+			
Increase in the size of the maximum unemployment benefit to 4900 rubles, and in the period of payment, from 6 to 12 months			+			33,9
Tax deductions for people buying or building housing will be doubled to 2 million rubles			+	+		43
Providing housing for all Second World War veterans			+	+		35
Enabling families who possess a government maternity capital certificate to use such money for improvement of their housing conditions ahead of standard time	+		+	+		26,3
Co-financing of regional employment programs			+		+	77,6*****) *)
Restructuring of mortgage loans through the Agency for Housing Mortgages for persons who lost their jobs	+		+			

<b>Anti-Crisis Measures</b>	<b>1. Expansion of access to financial resources</b>	<b>2. Lowering of burden on business</b>	<b>3. Alleviation of social problems, development of labor</b>	<b>4. Creation of domestic demand</b>	<b>5. Development of competitive environment, support of SMEs</b>	<b>Estimated resources, billion rubles (October 2008-December 2009)</b>
or suffer a decline in income						
Reduction of quotas for foreign workers			+			
Compensation (through an increase of the authorized capital) of lost revenue of Russian Railways Co. in connection with subsidized fares for students in secondary and higher education.			+			2,3
Ensuring of bids for the 2009-2010 government procurement program in December				+		
Increased advance funding for the fulfillment of measures under federal targeted programs and the state defense order				+		
Preferential prices (from 5 to 25%) for suppliers of Russian goods under the state order				+		
Regulation of the procedure for buying the products of natural monopolies and state corporations, and for ensuring privileges for Russian producers.				+	+	
Increase in import customs duties on automobiles.				+		
Reduction of tariff quotas for imports of poultry and pork, substantial increase in tariffs on over-the-quota meat imports				+		
Use of the funds of the state corporation Housing and Utilities Reform Fund in 2008-2009 for the acquisition of economy-class apartments			+	+		50
Use of federal budget funds ("Housing" Program under the Ministry of Defense) in 2008-2009 for acquisition of apartments			+	+		32,6
Compensation (through an increase of authorized capital) of the Russian Railways Co, for revenues lost in connection with the slowdown in the rate of indexation of railway carriage tariffs for 2009	+	+		+		50***** )
Granting subsidies to the Russian Railways Co. to compensate losses from the transportation of new vehicles from European Russia to East Siberia and the Far East.			+	+		2
Implementation of a program to renew pools of automobiles used by municipal authorities				+		20***** )
Increase in financing of the purchase of automobiles for the needs of federal authorities				+		12,5
Increase in the market value of Rosagroleasing for the expansion of purchases of agricultural machines	+			+		25
Expansion in lending to SMEs by Vneshekonombank	+				+	30***** )
Granting support to regional programs for the development of SMEs			+		+	10,5***** )

Anti-Crisis Measures	1. Expansion of access to financial resources	2. Lowering of burden on business	3. Alleviation of social problems, development of labor	4. Creation of domestic demand	5. Development of competitive environment, support of SMEs	Estimated resources, billion rubles (October 2008-December 2009)
Required quotas for purchases for small and middle-sized companies will be extended to municipal procurements					+	25
Fees for connecting SMEs to small-yield power will be lowered (paid by installments).		+			+	

\*) Since 2009, acceptance of new applications for refinancing external debts has been suspended

\*\*\*) Initially, capitalization of the Bank was increased by 30 billion rubles, and later, by another 45 billion rubles

\*\*\*\*) This estimate was made according to comments made by representatives of Vneshekonombank about the portfolio of projects in agribusiness appropriated for lending; at present, Vneshekonombank is reported to have plans to finance agribusiness projects for 100 billion rubles

\*\*\*\*\*) The amount of subsidies provided for 2009 is 6 billion rubles; however, the increase from last year is about 3 billion rubles

\*\*\*\*\*) This estimate was made in the 2008; it is possibly overstated

\*\*\*\*\*) This estimate (made in the late 2008) is most likely to be overstated; so far, only 13 regions have set lowered rates under the simplified taxation scheme, in many cases with industry-wise limitations

\*\*\*\*\*) Including the adopted decision on financing for programs for active employment policy measures (33.9 billion rubles) in addition to the present financing (43.7 billion rubles), and also including regional co-financing (5%), the total amount of resources is estimated at more than 80 billion rubles

\*\*\*\*\*) In principle, in December 2008 a decision was made to increase the authorized capital of the Russian Railways Co. by 41.4 billion rubles. Possibly, 50 billion rubles is an additional capital injection

\*\*\*\*\*) Taking regional co-financing into account, total resources will amount to 30 billion rubles

\*\*\*\*\*) For 2009, the sum of 30 billion rubles was provided; the increase from last year's level is about 20 billion rubles

\*\*\*\*\*) For 2009, the sum of 10.5 billion rubles was provided; an increase from last year's level of about 6 billion rubles.

Taking regional co-financing into account, and lowering the requirement of its contribution to this fund from 50% to 30%, the total amount can be estimated at over 8 billion roubles. Certainly, this ranging of priorities by the number of relevant measures is very relative, taking into account that the appropriated resources are disproportionate in principle, and the scope of coverage of the economy by concrete measures is different. The issue of the *redistribution of resources* that have been appropriated for the design and implementation of the anti-crisis measures is also very important, but on this occasion, our evaluations are far from being exact, and are of an exceptionally demonstrative nature for a number of reasons.

#### **Some issues related to the redistribution of resources**

Problems and deviations in the estimates arise for the following reasons:

Many measures are “non-monetary”, such as the lowering of administrative barriers, so that their effect on the redistribution of resources is hard to estimate;

We failed to find any official estimation for some measures that will undoubtedly involve a substantial redistribution of resources (changes in tariffs for services of natural monopolists; lending to the real economy by the banks that have received government aid);

Assessments of fiscal losses from tax measures are extremely unreliable and tend to change a great deal in the course of time ( for instance, a shorter monitoring period for the calculation of customs duty rates on oil exports had a significant effect when world prices went down; the estimate of losses from lowered taxation of profits turned out to be grossly overstated because the tax base dwindled; the assessment of losses from granting regions the right to determine tax rates under a simplified taxation scheme basically depends on how widely and how long this option was used by the regions);

Beside federal fiscal expenditures, substantial resources are redistributed by state-owned financial institutions for development and by specialized banks; a number of measures are realized on conditions of sharing financial responsibility with the regions, which involves the question of whether these resources should be taken into account or not;

A sizeable redistribution of resources was made in the 4<sup>th</sup> quarter of 2008, which involves the question of demarcation with 2009;

Those measures that have official estimates of the resources in question (fiscal; some related to taxation, and some, to customs duties on exports) can be correlated with several groups in different types of classifications;

We consider only increases in the lines of resource provision under the anti-crisis program, although, naturally, these are followed with decreases in some lines.

In general, we estimate the total volume of additional resources, according to the existing assessments of the cost of anti-crisis measures designed for the real economy, at 2.1-2.5 trillion rubles in

the period from October 2008 to December 2009. *Firstly, these measures are aimed at providing wider access of entities in the real economy to financial resources (1.1-1.2 trillion rubles<sup>12</sup>); secondly, they are aimed at lowering the burden carried by businesses (fiscal losses about 500-700 billion rubles); thirdly, they are aimed at social welfare and related to the expansion of consumer demand and to supporting starting entrepreneurs (250-300 billion rubles, and further, 180-230 billion rubles), and in the last, they are aimed at the support of SMEs (60-90 billion rubles)<sup>13</sup>.*

This does not mean that there are no significant measures to be taken for the fulfillment of other tasks. We believe that a number of other measures are very important from the point of view of the scale of their effect on the real economy, such as the imposition of ceilings on the tariffs of natural monopolies, accurate assessment of their investment programs, recommendations to banks about lending to industries in the real economy and controlling the banks that have obtained public support. However, these measures are the most opaque ones for assessment as policy instruments.

We can notice that the main emphasis of the anti-crisis program is given to incentives for lending to the real economy – the share of relevant measures is about a half of total resources in the anti-crisis package. Another quarter of the resources are given to reducing tax burden. Measures for support of domestic demand (no more than 10% of total resources in the anti-crisis package) look quite scanty against this background. It can be seen that the *“anti-crisis package” contains a very limited range of export incentives, primarily, those aimed at the promotion of high tech exports, and few provisions are made for a competitive environment<sup>14</sup>* (excluding those designed to support SMEs). There are extremely few incentives for innovative activities and for the better performance of natural monopolies and large state-owned companies, and no measures are being taken to attract foreign investors and to develop special economic zones. In this context, there are some discouraging trends that can lower the importance and limit the capacities of some institutions entitled to encourage of innovations, support growth and capitalization of new hi-tech companies. The functions of government agents are getting stronger, to the detriment of the functions of development institutions (Vneshekonombank), and resources in command of certain development institutions (the Russian Corporation of Nanotechnologies, the Foundation for Assistance to Development of Small Industries in Research and Development) are diminishing, while criticisms of some of them (the Russian Venture Company) are getting stronger.

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<sup>12</sup> Reimbursement of external debts of the largest Russian companies by the Vneshekonombank in October-December 2008 is included, amounting to about \$11.5 billion, along with state guarantees for enterprise borrowings in 2009 amounting to 300 billion rubles.

<sup>13</sup> Since some measures were related to more than one task, our sum of assessments according to the appropriated tasks is slightly higher than the total sum.

<sup>14</sup> Here we can mention the importance of the Program for Development of Competition in the Russian Federation, which was approved by the Government on February 26, 2009, but not yet transformed into practical measures.

### 3. The Main Beneficiaries of the Anti-Crisis Measures

To identify the main beneficiaries of the realization of the policy measures, we can single out different dimensions. Comparing the benefits gained by *business scale* and the *industrial affiliation of companies* is the classical way of such a study.

According to expert assessments, the majority of measures are centered on the support of large-scale companies. In principle, most measures have no formal limitations for middle-sized enterprises, but the established order and procedures of decision-making give preferences to big businesses. According to expert assessments, *a half of all measures are addressed to the interests (problems) of super-large and large corporations* these measures account for 60% of total resources in the anti-crisis package; and about a third of the measures is intended for support of small businesses, but their aggregate weight in total resources is just only 5% of all measures assigned for their support.

This is partly due to the priorities of the anti-crisis policy, which are addressed, in the first place, to highly-concentrated industrial sectors and to the largest corporations. What is also important, a number of recipients of selective support are enterprises forming company towns (AvtoVAZ, KaMaz and other). Another important factor is that big businesses have direct access to different levels of legislation and public administration and so have more facilities for lobbying for their interests.

Some people maintain that supporting large companies allows channeling the benefits down through links of co-operation. However, we believe that this way is possible mostly in industries with rather rigid vertical organizational structures (such as the defense-industrial complex). At the same time, the losers are middle-sized companies in the sectors with a horizontal organization and in new sectors that have as yet few or no super-large companies<sup>15</sup>.

In principle, a substantial part of the measures are claimed to be addressed to the development of SMEs, but in reality they are related mostly to micro-enterprises and small businesses<sup>16</sup>, and besides, give practically no incentives to small companies for their expansion. As a result, middle-size companies (which produce the bulk of output in a number of industries) are at a disadvantage because they are entitled neither to receive general assistance addressed to small businesses nor to get selective support targeted at large corporations. In our opinion, there are only two important systemic arrangements that do not discriminate against middle-sized businesses: reduction in profit tax rates and the introduction of a

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<sup>15</sup> Perhaps for this reason, these measures are applicable on limited scale to logging and woodworking, or to light and food industries which have no leading companies that could be able to lift the whole chains of co-operation.

<sup>16</sup> Nevertheless, measures for support of SMEs are very important for labor market even in their present shape.

30%-increase in depreciation premiums, but the positive effect of these measures is becoming much less as the crisis grows more severe<sup>17</sup>.

In general, the anti-crisis measures are concentrated on the margins: big businesses and micro-businesses, in terms of quantity, as well as in terms of the redistribution of resources required for their accomplishment.

Enterprises that are affiliated to many industrial sectors are recipients of the anti-crisis measures. However, though these look fairly diversified, many industries get little or no special assistance. We refer to chemicals, logging and woodworking, light and food industry, building materials, and some others.

Judging by the quantity of measures, *industry-wise priorities* can be seen quite easily namely, automobiles and agricultural machinery, the defense-industrial complex, agribusiness, housing construction<sup>18</sup>. The set of measures addressed to automobiles and agricultural machinery is distinguished by a wide variety of tools. Judging not only by the quantity of measures but also by the scale of resources they involve, the oil and gas sector is certainly one of the industry-wise priorities, because the relevant enterprises will win an estimated 200-250 billion rubles from lowered burden. Direct and indirect<sup>19</sup> support of automobiles and agricultural machinery will “weigh” 190-200 billion rubles, and of the defense-industrial complex, about 180 billion rubles.

In general, the main beneficiaries of the anti-crisis measures are the traditional industrial sectors, and the most vulnerable ones, and the measures are chiefly aimed at compensating for the losses of larger companies. We believe it is important that *the majority of measures with substantial anti-crisis effects are of compensatory nature* (they alleviate the aftereffects of the crisis). However, there are practically no measures to encourage enterprises to undertake active tasks of their own (technological modernization, product diversification, opening of new markets, etc.). The importance of assistance to the most vulnerable sectors is understandable, but nevertheless, the impression is that there is a *shortage of measures that could ensure the conditions for new dynamic sectors and support the growth of middle-sizes companies*.

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<sup>17</sup> In the late 2008, the official estimation of fiscal losses from reduction in taxation of profits amounted to 400-500 billion rubles, and in March 2008, already to 294 billion rubles. Estimated fiscal losses from the 30%-increase in depreciation premium declined from 150 billion rubles to 50.4 billion rubles.

<sup>18</sup> Many measures claimed as addressed to social welfare are related to creation (support) of demand for housing, and so, housing construction is a significant beneficiary.

<sup>19</sup> In the case of automobile enterprises, their share of state guarantees (70 billion rubles) is taken into account, as well as assistance to floatation of their bonds (60 billion rubles); in the case of the defense-industrial complex, granting of state guarantees to defense enterprises is taken into account (100 billion rubles).

#### 4. The Main Tools Used for the Implementation of Anti-Crisis Measures

We believe that before assessing the anti-crisis measures used, it is important to take a view of these measures in the context of their belonging to *general economic policy or industrial policy*<sup>20</sup>.

We attribute to economic policy those measures that affect all economic agents (not necessarily equally). In general, they produce either changes in general tax treatment, or changes in the rules of the game in all markets or the majority of markets, and also affect an indeterminate range of agents. We attribute to industrial policy the measures that provide support to individual enterprises (selective measures), to groups of enterprises in a single sector, and to individual sectors of the economy<sup>21</sup>.

Following this classification we find that although measures attributed to general economic policy are fewer, their number is comparable to those attributed to industrial policy (41% compared with 55% of the total number of measures). However, *industrial policy has a much heavier weight in terms of resource endowment*. According to our estimates, in 2009, economic policy measures (primarily, lower taxation of profits and depreciation premiums) will cost *600 to 900 billion rubles*. Meanwhile, industrial policy (in particular, a rise in the non-taxable minimum of tax on the mining of minerals; support of housing construction in a number of ways; packages designed to assist individual industries, and subsidies and state guarantees) will cost *approximately 1.4-1.7 billion rubles*<sup>22</sup>.

Taking a look at the tools that are used by the government to put one or another anti-crisis measure into practice, we can see that their spectrum is wide and includes almost the entire set of levers at hand, from tax policy to administrative and organizational measures. However, the most frequently used tools can be classified into four groups: institutional changes (in rules and regulations); changes in taxation; facilitation of access to financial resources, and direct and indirect encouragement of demand for domestic production. These four groups of tools account for about 80% of the total number of measures<sup>23</sup>. Notice that two thirds of measures attributed to industrial policy are instruments facilitating access to

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<sup>20</sup> In a number of cases, labeling of the measures as belonging to a particular policy line is difficult because both producers in the real economy and households can be their beneficiaries. In these cases, we classified a measure by expertise, finding their main beneficiary. For example, we can refer to subsidizing interest rates on consumer loans for purchase of domestically produced automobiles. Formally, it is a benefit for final consumers who can save money, but directly, it is an incentive for expansion of demand for products of a particular industry.

<sup>21</sup> Industrial policy measures refer not only strictly to mining and manufacturing (enterprises and/or industries), but to other real economy sectors – agriculture, transportation, construction etc.

<sup>22</sup> In the cost of industrial policy, some “conditional” costs are also included – such as state guarantees for lending (300 billion rubles), which are unlikely to be completely used.

<sup>23</sup> This classification is informal and based on substantive expert estimations. For instance, changes in leasing rules and an increase in the market value of Rosagroleasing Co. formally looks like facilitation of access of agricultural enterprises to financial resources; but in our classification, it is included in creation of demand because we consider this goal as the principal one.

financial resources and encouraging demand in specific markets, while about a half of the measures attributed to general economic policy are the ones of an institutional nature.

Now let us consider the tools that are used to put anti-crisis measures into practice from the point of view of *main types of government policies*. In this context, the most widely used groups of instruments are:

(1) *Tax policy* (lowering of certain tax rates; changes in the procedure of tax charging);

Tax policies are mostly related to novelties in the taxation of profits. The effects of these measures, such as lower taxation of profits and higher depreciation premiums, tend to decrease along with a deterioration in the financial health of enterprises, diminishing returns, rising uncertainty about business conditions and soaring prices of imported technological equipment.

(2) *Customs policies* (multiple changes in customs duty rates in different directions);

The activity of the government has increased a great deal in changing customs duty rates<sup>24</sup>, above all, import rates. To say that this is a policy of frontal customs protection against imports is incorrect, not least because decisions have been taken both on raising and lowering import rates. There are signs that the tariff schedule is getting more individually targeted, that the list of foreign economic activities is becoming more detailed due to the addition of sub-sub-positions, and that the regulations are addressed to the interests of certain big corporations and some large-scale projects rather than to the relevant markets.

(3) *Procurements for public needs* (their timely placement, larger advances, extension of rules for public procurements to purchases of natural monopolists and state-owned companies, introduction of preferences for purchases of Russian-made goods);

Measures addressed to public procurements for the expansion of demand lag far behind the schedule of other measures. As a result, their effect in preventing the spread of the crisis in the economy has become much weaker. So far, problems of larger advances and guarantees for advances are unresolved. Measures for the extension of rules for public procurements to purchases of natural monopolies have not yet been introduced, although they give the impression of being quite substantial (if they are supplemented with efforts to improve the management of these companies). The development of leasing, to which little attention was paid earlier, deserves a generally positive assessment.

(4) *Fiscal measures* (subsidizing of interest rates; state guarantees; injections of capital in specialized banks and financial institutions for development in order to increase their loans to the real economy, and replenishment of the capital of individual systemically important enterprises).

These measures, which are the most widespread, are mainly aimed at expanding loans to companies. A special emphasis is placed on subsidizing interest rates and state guarantees for loans.

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<sup>24</sup> Since November 2008 till February 2009, the Federal Government passed 23 resolutions on changes in customs duty rates (of which, 17 established temporary rates for nine months). In the same period of November 2007 to February 2008, 14 resolutions on changes in customs duty rates were passed.

Efforts are also being made to create facilities for the issuance of infrastructure corporate bonds and for progress in the regulation of this area.

Some anti-crisis measures designed by the government of the Russian Federation presume that *regional governments will take an active role* in their adaptation to regional conditions and in their practical implementation. These measures include:

- Granting the right to differentiate to some extent; rates in the simplified taxation scheme,
- Expansion of regional quotas for limiting the size of the foreign workforce;
- Co-financing of programs for renewing municipal transport pools;
- Extension of the requirement to place a some orders among SMEs to municipal contracts;
- Co-financing of regional employment programs;
- Support of programs for the development of SMEs.

In our opinion, the measures that are aimed at supporting programs for employment activity and programs for the development of SMEs require the energetic and reasonable participation of regions to the greatest extent, because these programs involve a large number of different mechanisms with some significant innovations. The newly- established rules give regions great flexibility and many opportunities to vary the content of these programs and to give emphasis to some of their components according to the situation. The effect of these measures will mostly depend on the reasonable actions of local authorities. This will require *monitoring the results, their inter-regional comparisons, and rewards for best practices*.

Concerning *ways of distributing benefits from achievements among economic agents* we can provisionally draw attention to three groups of tools in practice:

(1) *Selective ones* (choice of individual enterprises and individually- tailored decisions according to many criteria that are hard to formalize);

(2) *Competitive ones* (competitive bidding with clear criteria for selection and access);

(3) *Systemic ones* (all enterprises, or those that meet certain size of product line requirements, get the benefits).

As our analysis has demonstrated, a half of all measures under our consideration can be attributed to systemic ones; 20% require competitive bidding providing that economic agents meet formal criteria, and 30% are selective ones. At the same time, *selective measures* lead in the anti-crisis package in terms of volume of resources allowed for redistribution (47%). The reason is that the anti-crisis policy focuses on large and super-large corporations, which involves a great number of volitional decisions, increases vulnerability to pressures from various vested interests, and intensifies lobbying for the additional funding of selective measures.

In principle, selective measures are reasonably important under conditions of crisis, but not on this massive scale and not with such great variety of instruments. Some of the measures relating to

changes in customs duty rates could be regarded as systemic ones, but are actually used as selective ones, because they are taken to meet the needs of individual economic agents.

The role of *competitive measures* is generally on the decline. Expansion of outlays for selective measures involves an extensive search for additional resources at the cost of reduced expenditure on target fiscal programs. The role and place of such programs in crisis conditions are still unforeseen. As a result, *lobbying will probably move from programs (while the formation of new programs under existing rules is rather costly) to expansion of selective measures and to their additional funding*. So far, an extension of the rules for public procurements to purchases of natural monopolies and state-owned companies is not bringing any positive results. Consequently, *selective measures can be, for objective reasons, extended to the enterprises that fail to wait for procurements*.

In terms of resources, the *systemic* measures already taken show declining efficiency and orientation towards compensation of losses. They are not aimed at the encouragement of positive results (company growth, opening of new markets, including export markets, effort to attract foreign investments, increase in energy efficiency).

So, we can note a certain *imbalance in favor of selective measures*, and, as long as negative influence of the crisis grows, this bias can become stronger. To a certain extent, this is the result of the *absence of a well-developed set of systemic instruments for industrial policy*.

At the same time, some of the measures that at present are actually being used as the selected ones (for instance, subsidized interest rates, state guarantees) could be transformed into competitive measures. We also believe that it is important to increase expenditure on active measures for the promotion of employment and support of SMEs, but in mandatory combination with a basic improvement in the monitoring of results and the development of tools for the dissemination of best practices.

## 5. Description and General Assessment of Certain Directions within the Anti-Crisis Policy

We believe it is important to give a more detailed examination of measures relating to tax policy, customs policy, and to policy oriented towards the development of SMEs. We have chosen these because the effects of the related measures are predominantly systemic, and due to specific ways of decision making in these areas (the existence of guidelines for tax policy in the planning period<sup>25</sup>; the presence of Government Commissions<sup>26</sup>).

### 5.1. Measures Concerning Tax Policy

1. The bulk of these measures have been in force since January 1, 2009. Two of them, aimed at the reduction of the financial burden on enterprises, have been in force since 2008: changes in the scheme of paying value added tax (VAT) and the optional transfer to payment of VAT on the base of actual profits before the year's end. The right to change the schedule for the computation of advance payments of profit tax within a fiscal period was granted to enterprises only in 2008. Conditions for taking advantage of this right had a strictly limited term-frame. For this reason, the anti-crisis potential of this measure was used by a half, at most.

2. The group of tax measures to come into force from 2009 is mainly related to innovation in the taxation of profits. They include a decrease in the tax rate from 24%, to 20%, an increase in depreciation premiums for several groups of fixed assets from 10% to 30%, and a change in the schedule for writing off costs of licenses for mining of minerals on expenditures. These measures have a certain motivating power, which can encourage growth. However, in a time of economic downturn, enterprise profits diminish, and this motivating power remains, for the most part, unused. These measures will have a stronger effect as soon as the economy resumes growth.

3. The measures related to VAT are mostly aimed at eliminating artificial restrictions on tax deductions. The most influential of them is the granting of a right to deduct VAT from advances and the cancellation of the obligation to transfer VAT in cash when a settlement is non-monetary.

4. Exemption from VAT of imports of technological equipment that has no analog in domestic production is an important innovation. This regulation is designed to replace the exemption from VAT, of imports of equipment as investments in charter capitals and it will be put into practice after the government of the RF makes a relevant list of technological equipment. The effect (either a positive or a negative one) will largely depend on the principles of compilation and on the final composition of this list.

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<sup>25</sup> Guidelines for Tax Policy in 2009 and in the Planning Period of 2010-2011; Guidelines for Customs Tariff Policy in the Medium-Term Outlook for 2009 and in the Planning Period of 2010-2011.

<sup>26</sup> The Commission of the Government of the RF for Protective Measures in Foreign Trade and Customs Policy; The Commission of the Government for Development of Small and Middle-Sized Enterprises.

5. A number of tax measures are aimed at the reduction of the tax burden on oil extracting companies. This group includes a rise in the non-taxable minimum for computation of the rate of tax on mining of minerals from 9% to 15%; the introduction of tax holidays for some sites that are difficult to explore because of harsh weather conditions, and the above-mentioned change in the schedule for writing off costs of licenses for the mining of minerals. It is worth mentioning that all these measures were adopted as early as in July 2008, and no corrections were made for putting them into practice. While the rise in the non-taxable minimum and the change in the schedule for writing off costs of licenses refer to all oil-extracting companies (to be correct, the latter is applied not only to oil extracting but to all mining companies), tax holidays give preferences to individual companies that already have licenses for relevant drilling lots.

6. With regard to small businesses, a major innovation is the granting of the right to differentiate, in the range from 5% to 15%, the rate for a simplified taxation scheme (when the taxpayer chooses taxable income after deduction of expenditures) to constituent entities of the Russian Federation, depending on the category of taxpayers. (Formerly, there was only a single level of 15%.) However, the single rate of 6% remains unchanged in cases where income is the tax base. This object of taxation was mostly used by enterprises in the simplified scheme.

7. In addition, a number of point-focused measures were adopted to reduce the tax burden on individual groups of taxpayers. In particular, tax deduction was increased for the individuals buying houses; small enterprises in fishing and fish farming that form company towns and townships were permitted to pay a single agricultural tax; pharmacies were allowed to defer the application of limitations on the use of a single tax on imputed income.

8. The package of tax measures also includes changes in due dates for tax payments. The Minister of Finance has got the right to give, for the period of 2009, tax deferment or tax credit for federal taxes over a period of less than five years in cases where a company's arrears are more than 10 billion rubles and a one-time repayment may pose a threat of negative social and economic after-effects. A list of grounds for obtaining investment tax credits has been expanded to include the state defense order. Both measures are discretionary, addressed to large companies and opaque in terms of application.

□ The total of tax measures in the government anti-crisis package includes a multitude of tools that have different aims, time-frames and influence. We believe that they do not form a single consistent system. Many of them were planned even before the crisis.

□ The basic positive component of tax innovations is an improvement in tax charges and tax administration.

□ Tax measures aimed at reducing the burden of the taxation of profits have a limited anti-crisis effect, but can be considered as important when the economy resumes growth.

□ For the most part, these measures are aimed at compensating for losses, and in the crisis period, they do not create direct incentives for innovations and for the expansion of businesses' scale .

□ Certain measures call for specific attention to their administering and monitoring of their application (the increase in depreciation premiums; cancellation of VAT for imports of technological equipment that has no analog in domestic production). Imperfect procedures and improper administration can severely limit their effects.

□ For a number of measures, maybe some way out will have to be found when the economy resumes growth (differentiated rates in simplified taxation schemes and taxation in cases of non-monetary settlement).

## *5.2. Measures Concerning Customs Tariff Policy*

1. Steady and substantial increases in the tariff rates on imports during the entire period of 2001-2008 were limited to meat and automobiles. They were continued under the anti-crisis program as well. The level achieved is already fairly high.

Among the goods tending to have lower or stable rates, tariffs were increased on such commodity groups as dairy products, iron and steel products, pipes, buses and some types of special automobiles, and forestry equipment. The increase was rather moderate, rarely exceeding 10%, mostly 5-10%. A larger increase of more than 20% was made for forestry equipment. Tariff rates were increased by over 5 points on iron and steel products, trucks and forestry machinery, which formerly were charged less than 5%.

2. Tariff rates on meat and used automobiles were increased sharply (by over 30 points). An intermediate increase (substantial, but not a peak one) was made on such goods as butter, iron and steel products, buses, new automobiles, and forestry equipment. Insignificant increases (of less than 5 points) were made on dairy products (except butter), and on some sorts of pipes and buses. Import tariff rates were lowered on some commodities, including natural rubber and iron and steel inputs (scrap, waste products, shavings). Some tariff schedules were elaborated in detail under the anti-crisis program, for such goods as meat, iron and steel, components for car assembly, automobiles, and aircraft.

3. According to estimations made on the 2007 database, changes in import rates cover a volume of imports of about \$30-billion. About 75% of this volume was charged at rates 5-10-point higher; the rates on about 7% were increased very sharply by more than 35 points, and the rates on 3% were lowered. On commodity groups imported in larger volumes, the rates were changed less than on those imported in smaller volumes.

□ We must note that tariff instruments, in essence, have a limited capacity to compensate the negative outcomes of the crisis and to create domestic demand. This is mainly because higher tariff rates can bring price hikes in the domestic market and as such, reduce total demand. To avoid this negative effect, consumers are expected to rapidly turn to buying domestic products. This may be possible

on condition that there are idle facilities or investment resources to rapidly expand domestic production (in a time of downturn, investment activities, naturally, will be rather weak, and this factor will more likely work nearer the end of the crisis); and also, if imported and domestic goods are highly interchangeable.

□ As for interchangeability, it should be mentioned that most studies (and experts) show that so far, local and foreign goods cannot be considered fully interchangeable in the Russian market. Moreover, raw materials, semi-finished goods and agricultural products (mass produced goods) are much more interchangeable. Interchangeability is lower for technologically sophisticated and high value-added goods. For this reason, it is more reasonable to apply tariff measures to iron and steel products, but in this case, deliveries from CIS countries should be excluded because they are not liable to tariff measures.

□ So, the efficiency of tariff instruments in a period of downturn is limited by a number of factors: tariff protection of iron and steel producers has a limited effect because it will deprive consumers of metals, agricultural production cannot be swiftly expanded in idle facilities, and machinery faces the problem of interchangeability.

□ For this reason, we believe reliance on tariff instruments during a recession is most reasonable as a principle of effective tariff protection: customs rates should be decreased on those imported raw materials and equipment that are essential for the stimulation and support of industrial activity and cannot be supplied by local producers. This scheme is effective both during a depression and during the revitalization of the economy. However, this type of measure is offered in the anti-crisis package on a very limited scale.

□ In some areas, antidumping, compensational and special protective measures can be more effective. Antidumping and compensational duties can be quite harsh and selectively applied against the producers who use means of unfair trade and, as such are most dangerous in times of recession. These mechanisms are used in a regime of higher transparency, and this can diminish the risks of negative aftereffects and allows taking into account the interests of consumers. In addition, these mechanisms are much more useful for entering into cooperation with enterprises and for giving the business community the chance to play a more active role in market regulation and compensation for factors that worsen economic conditions.

### *5.3. Measures for the Development of Small and Medium-Sized Businesses*

1. Supporting small and medium-sized businesses in crisis conditions is very important as an incentive for economic growth, and also as a way to sustain employment and mitigate the effects of the crisis in the social sphere. Judging from the number of measures addressed to SMEs, this line really looks like one of the major priorities of the anti-crisis program. Sixteen measures are directly addressed to this segment of the economy, and thirty others affect it indirectly. The volume of resources assigned by the government for this is: 6 billions roubles as an additional allocation from the Program for Financial

Support of Small and Middle-Sized Businesses; 30 billion rubles as a transfer from Vneshekonombank to support the loans to SMEs. In crisis conditions, very important “non-monetary” institutional measures can be related to ensuring access by small and medium-sized businesses to the procurement of goods (or services) to natural monopolies and state-owned corporations, as well as to municipal procurement orders, given that the procedures are competitive and transparent.

2. The whole set of measures can be classified into four groups: those in the framework of the program for the financial support of small and middle-sized businesses with additional funding for several lines; those related to incentives for loans to SMEs in crisis conditions; those related to lowering administrative barriers for businesses and giving SMEs better access to the infrastructure; and those related to ensuring access of SMEs to federal and municipal procurements.

Among the most important new “monetary” measures, we can mention grants to starting entrepreneurs for the creation of their own businesses. According to estimates, this can cost up to 4.5 billion rubles, and about 15,000 starting entrepreneurs are entitled to these grants. The experts show a generally positive appreciation of this measure, but notice that it is hard to manage, and involves many risks because of lack of experience. Besides, the largest possible grant to a person starting a business (300,000 rubles) is much lower than what is actually needed to launch one. Generally speaking, many measures to help launch new enterprises, which are claimed as anti-crisis ones, are belated: they could have been more effective earlier, in the growing economy.

The last observation refers to a number of other measures as well, such as the support of educational programs for small companies, the lowering of charges for connecting small volume consumers to power networks; supporting energy-conservation programs, and developing entrepreneurship in the younger generation. A number of important and potentially productive measures, including the development of facilities for micro-financing, will hardly have any effect before the end of 2009.

A large number of measures designed to support small businesses require competitive bidding, sometimes even two-staged bidding (the first for inclusion into regional programs, the second for entitlement to regional support). In the first place, such measures lack an immediate response, and in the second, they are highly dependent on clearness of criteria for selection and efficient control. Otherwise, their effect will be many times lowered and distorted by corruption, which is a possible component of any selective decision. In general, we should note that the effect of the majority of measures to support SMEs strongly depends not only on decisions made by the federal authorities, but also on the way these decisions are realized in the field.

Two stages are also envisaged in the “strongest” measure for the expansion of lending to SMEs through Vneshekonombank. In 2008, the total quota for this activity was 9 billion rubles, and about 5,000 small and medium-sized enterprises were entitled to these loans: a tiny fraction of the total number of

small and medium-sized businesses (2.4 million entities). According to estimates made by experts, actual resources will come from the program of Vneshekonombank to final borrowers no earlier than the middle of 2009. Nevertheless, this measure may be speedier in terms of effect than most other measures.

3. A right to cut tax rates down to 5% according to the simplified taxation scheme which is given to regional authorities can be regarded as the most fast-acting anti-crisis measure for the support of small and medium-sized enterprises. However, this arrangement is not free of substantial shortcomings. In reality, its beneficiaries are micro-enterprises, because there are strict eligibility limitations. Moreover, the majority of firms that use the simplified scheme apply a 6%-rate, which remains unchanged. Finally, not all regions have hurried to use this opportunity; by the beginning of March, appropriate laws were enacted only in 13 constituent entities of the Russian Federation, and in some cases, they are applicable only to certain business lines.

□ In general, the complex of anti-crisis measures for support of SMEs is not inconsistent, and it creates incentives for the development of this segment of the economy. At the same time, some measures are not prompt enough and are due to bring about results no earlier than in summer or autumn 2009. This gives us no grounds to evaluate them as high in the acute phase of the crisis. Nevertheless, they are likely to be helpful for an earlier revitalization after the lowest point of the crisis has passed.

□ Unfortunately, so far, some “extraordinary” administrative measures have not been put into practice, although they could really have a substantial effect. We mean, in particular, an offer to declare a moratorium on the inspection of business enterprises during crisis period. The imposition of this moratorium (not for a fixed term but “until further notice”) could reduce the burden on small enterprises in the acute phase of the crisis and improve the business climate in general.

□ The most effective measures to support SMEs entail a considerable amount of risk. For example, they presuppose that a great number of decisions must be efficiently administered at the regional level, and in regional banks and municipalities. In this connection, it will be very important to monitor the results and to compare efforts in support of SMEs region by region.

□ It should be specially mentioned that most of the measures that were declared as assistance to small and *medium-sized* businesses are in reality addressed to small businesses alone.

Moreover, it should be noted that in comparison with the pre-crisis strategy and the Program for The Financial Support of SMEs, this Program shows a certain shift from supporting innovative small firms towards supporting small businesses as a whole. The increase in funding in general follows the lines of subsidizing interest rates, developing micro-credit and the assignment of grants to starting entrepreneurs. At the same time, for a number of effective tools, such as The Foundation for Assistance to Small Firms in Science and Technology, allocation of resources has not been increased but has even been decreased to a certain extent. In principle, such a change of emphasis in crisis conditions is

explainable, but the priority of innovations, the establishment of new ventures and the creation of an appropriate infrastructure should not be lost.

## 6. Risks Involved in Implementation

We have already mentioned that *there are no measures that can be realized without any risks*; but it is essential to define the risks related to each measure and to work at finding ways (mechanisms) to minimize them.

The most frequently mentioned negative outcome was *deterioration in competitive environment (46% of total measures under consideration)*. Such conclusions were related not only to enactment of some protectionist customs regulations or preferential treatment of domestic producers, but also to strong distortions of competitive environment in the cases when different categories of Russian business would receive unequal treatment, particularly in their access to government support.

As a rule, “strong” tactical measures have a difficult problem of “exit” when a measure that was declared as a tentative one either has no built-in criteria for termination, or its abolition is going to create risks and increase further uncertainty in the changing environment. In many occasions, cancellation of temporary measures will be troublesome because of powerfully lobbying for their preservation. The implementation of the anti-crisis measures is taking two directions (in terms of choice of instruments):

- (1) Efforts to scale-up resource endowment for selected instruments;
- (2) The creation of new instruments.

Both ways have their advantages and costs (risks). In the first case, the measure can be carried out swiftly, as there is a routine system of administration, but in crisis conditions, an instrument may happen to be insufficiently effective and (or) reproduce unreasonable limitations.

*We can give examples such as the increase in the depreciation premium and partial subsidizing of interest rates on loans to exporters of products with a high level of processing. The depreciation premium works efficiently during upswings, but has a very limited effect during downturns when enterprise profits fall and when investment activity weakens because imported technological equipment becomes very expensive. As a result, the main benefits of this measure tend to go to large companies whose investment programs are “protected”, natural monopolies in the first place.,*

*The choice of partially subsidizing interest rates on loans to exporters was made because this, perhaps, is the only workable instrument to support high-tech exports. However, it contains (and contained formerly) barriers for new exporters (a three year-long history is required to be entitled to this instrument). Besides, its compensatory effect was increased by a partial reimbursement of interest paid for borrowings made after 2005.*

In the second case, a larger anti-crisis effect can be hoped for, but the risks become too high: hazards related to overrated expectations, inaccurate initial tuning, delays in putting new instruments into practice, and “exit problems” as soon as the crisis is over.

*Examples are: granting support to starting entrepreneurs and partial compensation of interest rates to individuals who borrow to purchase domestically produced automobiles. We believe that granting support to starting entrepreneurs is one of the “breakup” measures, but what are essentials here are the conditions of their implementation and management under regional programs, efforts to follow up the real effects and an accurate definition of affordable expenditures on subsidies. What is also fundamental is the risk that potential positive effects were overstated at the start, so that this cutting-edge instrument will be regarded with skepticism. Partial subsidizing of interest rates on lending to individuals is one of the few measures aimed at the creation of consumer demand. Let us notice that initially it was claimed as a clearly selective tool for the creation of demand for products of a single motor car factory, but it was further expanded to cover a fairly wide range of automobiles made in Russia, including global brands. However, it is quite unclear how this will actually meet the needs of consumers .*

Sometimes, the risk of inaccurate initial tuning of new instruments is further intensified because the *preparation of different lists* that are endorsed by the government’s agencies *is made without clear procedures of discussion and conciliation of various interests*, and the criteria for the preparation of such lists are absent, at least the very general ones.

#### **Exemption from VAT of imports of technological equipment that has no analog in domestic production**

Exemption from VAT of imports of “technological equipment (including components and spare parts) that has no analog in domestic production in accordance with the list approved by the Government of the Russian Federation” is proclaimed as a measure for the encouragement of technological modernization. So far, there is neither any information about a document that approves this list, nor any announcement about when it is planned to be accepted (the regulation will be enforced only after this list is approved), nor about the criteria to be used in the preparation of this list. At this stage, this measure looks completely opaque. This measure is also very “pointed” because VAT on imported equipment is often much higher than customs duties<sup>27</sup>.

Obviously, in order to ensure that this measure will produce real systemic incentives for the economy, the criteria and principles for compilation of this list should be openly defined. If not, there will be no practical way of creating a sufficiently stable and understandable system of incentives and signals for enterprises. We realize that elaboration of a universal list of equipment that could impartially show the sense of this measure is an extremely difficult task. To this end, criteria should be set for the identification of equipment analogs, which is always very difficult. For instance, there is the

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<sup>27</sup> It is important to notice that this measure actually means subsidizing of imports, because foreign suppliers get more favorable conditions for competition with Russian enterprises. Similar measures in terms of economic sense (although different in terms of methods) were applied in the early 1990s to the so-called “critical imports”.

problem of a variety of criteria to choose from: technical parameters alone, generic features or the commercial interchangeability of a good.

Understandably, practical approaches to the compilation of a list of technological equipment may vary a great deal. This measure may be addressed to the facilitation of imports of a rather narrow range of equipment and to assistance for running individual large-scale projects. If so, it is far inferior to the former measure (that is still in force), which determines exemption of imports of equipment from VAT as contribution to charter capitals in order to attract foreign technological partners.

### **Partial subsidizing of interest rates on loans to individuals buying passenger automobiles made by domestic manufacturers**

This measure implies the compilation of a list of automobiles, which will allow the individuals who buy them to be entitled to partial subsidizing of interest rates on loans. It was announced that this list would include inexpensive automobiles priced below 350,000 rubles. The government issued an order to the Federal Ministry of Industry and Trade to uphold this list, giving no other criteria.

After approval of the list of automobiles<sup>28</sup> by the Ministry of Industry and Trade, a number of car manufacturers expressed disagreement with the omission of some automobiles of their making from this list. The Federal Antimonopoly Service of the Russian Federation also formulated its claims to this list; in particular, it mentioned the vagueness of the principles of its compilation and the absence of a number of automobiles made by GAZGroup, Avtotor Co. of Kaliningrad and TagAZ (Taganrog Automobile Plant).

Representatives of the Ministry of Industry and Trade, in turn, have pointed out that:

- Price limit was only one criterion for the selection of automobiles;
- Automobiles whose prices might potentially be lowered were included in the list: such models as Volkswagen Jetta and Ford Focus;
- In general, priority was given to automobiles in categories B and C, so that the Volga Siber model, which was classified as luxury sedan D, was not included,
- Foreign brands of automobiles were included only if they were assembled in Russia under agreements on assemblage, so that models made at Avtotor and TagAZ were not included because these two companies had no such agreements.

We are not going to discuss the arguments and counter-arguments of parties in this dispute, although the criteria given by the Ministry of Industry and Trade seem rather unconvincing, especially those about makes whose prices might be lowered, and the categories of automobiles.

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<sup>28</sup> The order №77 issued by the Ministry of Industry and Trade on February 20, 2009, “On affirmation of the List of passenger automobiles produced in the territory of the Russian Federation, for which, in case of purchase by physical persons on credit in 2009, credit institutions would receive compensation of lost income at two thirds of the Central Bank of Russia’s rate of refinancing”.

The main lesson is that absence of initial criteria for the compilation of the list (or an indication that the agency responsible for its compilation must define and publish these criteria) lowers both the transparency of final decisions and the predictability of market conditions and creates more grounds for disputes.

We believe that the *risk of administrative failure*, which must be taken into account when a measure is designed, is highly important. This risk is higher for those measures which require that decisions about rendering support should be made by skilled public servants (or commissions), and which need competence in economic and even technical matters and/or availability of information that may be given only by the recipient and can hardly be verified, etc. Sometimes, the high risks of administering are related not so much to the difficulty of the decision per se, but to a great number of individual decisions, which can either overload the officers of relevant agencies and bring decision-making to a standstill, or delay this process. If risks of this type are high, it may be better to change the design of the measure and simplify the procedures and criteria used for decision-making.

The analysis of consolidated assessments made by experts *shows that the risks of administrative failure are considered to be high for 42% of all measures; moderate for 21%, and low for 37%*. Other things being equal, low risks are more typical of measures with routine administrative procedures (payment of unemployment allowances, fixation of tariffs), or of tax policies that are simple in terms of design (such as lowering of tax rate on profits). Concerning the correlation between administrative failures and instruments in use, we can point out that *means for the expansion of demand* (in the first place, government and municipal procurements) and *means for the stimulation of lending* (including subsidized interest rates and state guarantees) are most liable to such failures.

The risk of administrative failure is mostly determined by the type of instrument in use (a selective, a competitive, or a systemic one). Systemic measures entail the lowest risks of administering (less than 30% of them are highly risky). Strange as it may seem, the measures involving competitive methods of selection are the most risky ones (66%), while only 46% of selective measures are considered to be very risky.

Let us notice that *the measures that have strong anti-crisis effects more often bear higher risk of administrative failure* than the measures with relatively weak effects. High risks of misadministration are typical of 30% of all measures with weak effects, 43% of all measures with moderate effects. Among the measures with strong anti-crisis effects, 57% have high risks of administrative failures.

Let us emphasize that the presence of high risks of administrative failure does not mean that the measure in question is unproductive. This matter must be taken into account, and decision-making must be subjected to more carefully elaborated regulations (criteria, terms, requirements of decision makers, and so on).

Typically, many measures involve *risks of insufficient transparency of results, and in some cases, the risk that the procedures of decision-making will have low transparency*. To regard only selective measures as sources of such risks would be incorrect.

#### **Measures related to tax policy**

Almost every year, a dispute is underway about how some tax innovations that have come into practice, particularly those related to tax incentives, are affecting economic development. Public discussions usually deal only with overall fiscal losses and different evaluations of the effects of tax measures based on surveys of entrepreneurs and CEOs. There are no official data to illustrate the scale of the actual use of certain tax incentives by sectors of the real economy. Reasons for substantial discrepancies between anticipated and real fiscal losses are never discussed in public. This heightens the risk that situational, tactical decisions will be “pushed through”.

#### **Recommendations to commercial banks that have received public support for priority lending to certain industries**

This is an important measure to help companies get easier access to financial resources, but an opaque one, because the amount of expanded lending is unknown. Indicators for monitoring the activities of such banks are unclear, and how their decisions can be influenced by the government is undecided.

#### **Preservation of scales for the investment programs of natural monopolies**

This measure is important for the creation of investment demand, but it is unclear whether these companies have plans to enhance effectiveness of their investment programs, whether they have an agenda for resource conservation, and what measures will be taken for technological modernization.

As for selective measures, we believe it is important to ensure the *transparency* not so much of their principles as of the *final results for the selection of enterprises that will be entitled to support*. Certainly, many reasons can be found to justify the imposition of certain restrictions on information about concrete recipients at this “sensitive” time. This will probably require finding a reasonable compromise. However, if in principle dissemination of information cannot be limited, the best way is to present it officially within some limits in due time after decisions are made. If not, uncertainty will only grow, and the business environment will deteriorate.

A lesson can be learnt by referral to the refinancing of external debts of the largest Russian companies by Vneshekonombank.

#### **Refinancing of the external debts of the largest Russian companies by Vneshekonombank**

In this case, on the one hand, procedures for decision-making were transparent: the appropriate Federal Law was passed<sup>29</sup>, and the Supervisory board of the Bank approved the necessary procedure<sup>30</sup>, which adequately established clear criteria and limitations and was placed on the website of the Bank.

However, further official commentaries by the Bank did not mention the concrete recipients of the support.

October 31, 2008

*Vneshekonombank started refinancing the liabilities of Russian companies to foreign financial institutions. A total sum of US\$7.8 billion was allocated to a number of companies in the fuel and energy complex, metals, building materials, transportation and communications.*

November 21, 2008

*The Supervisory Board approved participation of Vneshekonombank in refinancing a number of dealings of enterprises in mining and micro-electronics which engage in activities considered as important for the Russian Federation, to the sum of about US\$ 2 billion.*

*Thus, at present, the total sum devoted to refinancing foreign liabilities of entities in the real economy, which was approved by the Supervisory Board, amounts to about US\$ 10 billion.*

December 31, 2008.

*The Supervisory Board has also approved participation of the Vneshekonombank in refinancing of foreign liabilities of companies in mining and metals, which engage in important activities for the Russian Federation, to the sum of about US\$ 1.5 billion.*

At the same time, wide discussions and comments were launched in the mass media (including foreign ones) on the data describing concrete recipients and amounts of aid. ( There were some contradictions about the sums, but all the names of companies were identical.) Reference was made to information obtained from persons closely connected to decision-makers; to statements made by individual recipient companies, and to information coming from partners of the recipients. Understandably, official information was probably limited because of an unwillingness to undermine the bargaining positions of the recipient companies. However, information about these companies very soon went public, although unofficially.

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<sup>29</sup> Federal Law №173-Ф3 of October 13, 2008 “On Additional Measures for Support of the Financial System of the Russian Federation”.

<sup>30</sup> The procedure for implementation by the State Corporation “Bank for Development and Foreign Economic Affairs (Vneshekonombank)” of measures stipulated by Sections 1 and 2 of the Federal Law №173-Ф3 of October 13, 2008 “On Additional Measures for Support of the Financial System of the Russian Federation”, approved by Supervisory Board of the Bank on October 13, 2008, Minutes №11 (with changes approved by Supervisory Board of the Vneshekonombank, Minutes №20).

## 7. Evaluation of the Impact of the Anti-Crisis Measures. Possible “Traps” and “Bifurcations”

The measures under review are very different not only in terms of costs of resources, but even more in terms of anticipated anti-crisis effects<sup>31</sup>. Considering that so far most measures have produced no influence on the real economy, the experts, naturally, often had to estimate hypothetical or potential effects on the basis of their own understanding of the importance of individual measures in the fields of their expertise (industries, or policy direction), and also had to take into account the legally determined conditions for carrying out each measure.

However conditional such assessments may be, we can observe that *just a little over 10% of all measures were assessed as bound to have a strong effect in the crisis phase*; about 30% will have a moderate effect, and about 60% a weak one. Among those with a strong anti-crisis effect are direct assistance to enterprises (state guarantees on loans to enterprises), some arrangements in customs policy (certain means of protection), the regulation of natural monopolies, and a number of tax measures. At the same time, assessments of the effects far from always correlate with the amounts of resources allocated by the state for putting these measures into practice.

We note that *the measures that have strong anti-crisis effects more often entail a higher risk of administrative failure* than the measures with relatively weak effects. High risks of misadministration are typical of 30% of all measures with weak effects and of 43% of all measures with moderate effects. Among the measures with strong anti-crisis effects, 57% have a high risk of administrative failure.

We believe it is important that *the majority of measures with substantial anti-crisis effects are of a compensatory nature* (that is, they alleviate the aftereffects of the crisis). However, there are practically no measures to encourage enterprises to undertake active tasks of their own (technological modernization, product diversification, opening of new markets, etc.).

As a rule, the higher an assessment was given to an anti-crisis effect, the more frequently it was mentioned as likely to bring conflicting results (20% of the total number of measures). The most frequently mentioned negative outcome was a *deterioration in the competitive environment (46% of total measures under consideration)*. Such conclusions were related not only to the enactment of some protectionist customs regulations or preferential treatment of domestic producers, but also to strong distortions of the competitive environment where different categories of Russian business received unequal treatment, particularly in their access to government support.

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<sup>31</sup> It is difficult to correctly estimate quantitative effects that are expected from most measures. However, in the course of this study, our experts gave their assessments of anti-crisis effects wherever it was possible, using such terms as “insignificant”, “low”, “moderate”, “strong”, and so on. On the base of these qualitative assessments, a scale of effects was built in rough intervals from “strong negative” to “strong positive”. The experts were asked to estimate, besides the short-term anti-crisis effect (approximately in the current year), the impact of individual measures in the end phase of the recession and in the starting phase of economic growth.

We believe it is very important that, according to the experts, the *influence of certain measures can be quite different in the recession phase and in the phase of recovery from recession*. Among the measures that could be assessed both in the recession phase and in the recovery phase (they number 66), slightly less than 60% will have positive effects in both phases. Seven out of those 66 measures (or about 10%) can be referred to as those with a “delayed effect”: the experts have estimated their anti-crisis effect as “nil” or even negative, but they are regarded as positive on the way out of the crisis. A disturbing fact is that *about 30% of total anti-crisis measures were considered as positive during the recession, but potentially negative when the peak of the crisis is over*.

As a rule, “strong” tactical measures have a difficult “exit” problem when a measure that was declared as a tentative one either has no built-in criteria for termination, or its abolition is going to create risks and increase further uncertainty in the changing environment. It is important to detect possible “traps” for the successful elaboration of future measures and strategic tasks for the post-crisis period.

Here we give examples of *some possible “ineffective equilibria”*, which are related to the implementation of certain anti-crisis measures.

### **1. Cancellation of an obligation to transfer VAT when settlements are non-monetary**

This creates the risk that the spread-off of barter transactions will restrict economic growth in the phase of recovery from the recession. Non-transparency of barter transactions involves risks to the fiscal system and to enterprise owners. The economy can be prevented from sliding down into ineffective equilibrium if the tax administration brings price setting in barter transactions under successive and severe control. However, this type of control per se can create strong negative consequences for the business climate.

### **2. Lowering tax rates under a simplified taxation scheme**

The rate of income tax (6%) may turn out to be higher than the tax rate on income with a deduction of expenses (possibly, 5%). Taking into account the disparity in tax bases, differentiation in the tax burden of identical enterprises can become considerable. This will create a strong incentive to break up small companies artificially, to abandon existing small firms and to establish a new firm (or firms) in order to shift to simplified taxation. When the economy resumes growth, the firms that were using the simplified taxation scheme will lose the incentive to expand their businesses and to raise productivity, because when income in the taxation period exceeds 30.76 billion rubles (the level for 2009), the firm will lose the right to use the simplified taxation scheme.

### **3. Refinancing of liabilities of the largest Russian companies to foreign financial institutions by Vneshekonombank**

Risks of non-repayment will be high; this will require either refinancing the liabilities anew or increasing Vneshekonombank’s share in the capital of the company, which will make it unclear how to carry out further operations with collateral parcels of shares. There will be a high risk that some

companies will lobby for further refinancing of the already-accomplished credit deals with Vsheshekonombank. Foreign financial institutions will show much stronger interest in a definition of the level of possible government support.

#### **4. Recommendations to commercial banks using different types of public support for priority-lending to certain industries: automobiles, agriculture machinery, air transportation, residential housing**

This will create the prerequisite of banks to make inefficient decisions, of there being stronger public administration influence and of the vulnerability to lobbying of certain decisions arising. This can make the banks less responsible, encourage their internal opportunism, and push them to appeal to the government once again for a further package of help because of their “wrong decisions”. They will attempt to share liability for these decisions with the government. In general, commitments will become more opaque, and the sharing of risks between the banks and the government will become uncertain.

#### **5. The temporary increase in tariff rates on imports of new automobiles**

This measure is intended to compensate partially the makers for a decline in demand for domestically-produced automobiles. This will probably result in an additional continuation of domestic automobile manufacturers lagging behind foreign competitors. If the industry can carry out relatively successful modernization, a positive effect is possible when the economy recovers. But this measure is tentative, and the behavior conditions are not defined. There is a high risk of lobbying for the prolongation of this measure.

#### **6. The reduction of quotas for the demand for foreign workers**

This involves the risk of decline in the competitive power of Russian goods and services in the global market because of rising labor costs. Certain regions cannot satisfy their demand for labor with local labor resources due to structural disequilibria in their labor markets. This measure will disrupt the conditions for fair competition between the enterprises that are actively using and those that are not using a foreign labor force. The economic and social consequences of this measure will come into conflict. Also, this measure will come into conflict with the deregulation and limitation of inspections of business enterprises. It poses the risk of turning into a mere declaration, and corruption may flourish during the establishment of control over the observance of this limitation.

#### **7. Granting of (legal) preferences to small businesses for the purchase of rented state-owned and municipal property**

The better-performing enterprises, which are able to privatize assets in competitive bidding, will lose their right to purchase this type of premises. Situations can occur when firms will use their right for earning a one-time income rather than for developing their businesses. Regional authorities can be expected to try to break their rental contracts. Pressure to prolong the term of this measure may occur. This measure is related to the high risks of corruption. There is a risk that during a specified period of

time, “inner circles” of small and middle-sized enterprises may be established as receivers of this priority right after 2010.

Many of the approved measures will bring certain *deviations from the approaches to the long-term economic strategy that was accepted earlier*. According to the experts, such measures amount to *more than 40% of the total number of measures under way*. On many occasions, the cancellation of temporary measures will be troublesome because of powerfully lobbying for their preservation. In some cases, as we have mentioned above, “inefficient equilibria” may occur. Sometimes it will be necessary to consider “*new bifurcations*” and new decisions about the ways to achieve the long-term goals of social and economic development.

We have made an attempt to single out some of *the expected “crucial” decisions*, which will be related both to the anti-crisis measures and to the changes that had been planned earlier. In our opinion, the nature of these decisions can strongly affect not only “windows of opportunities” further in the anti-crisis policy, but also the principles of long-term social and economic development.

<b>Anti-crisis measures</b>	<b>Probable (necessary) time of making decisions</b>	<b>Issues to be discussed</b>
Limitation of rates of growth in tariffs for goods (or services) supplied by natural monopolies <sup>32</sup>	April 2009	<i>Influence on development of various sectors; Investment programs of natural monopolies ; Reserves for improvement of efficiency and related incentives</i>
Definition of additional measures for tax incentives <sup>33</sup>	April 2009	<i>Reform of the single social tax; Sources of funds for the pension system; Increased burden on business enterprises; Abolition of special tax regimes and ways of compensation; Additional instruments for tax incentives, including those for higher energy efficiency</i>
Introduction of temporary import customs rates (the term of temporary rates will expire September-December 2009)	August 2009	<i>Changes in competitive environment in markets; Costs for consumers; Behavior of “protected” firms; Systemic nature of changes,; Expanded use of anti-dumping instruments</i>
Refinancing of external	September	<i>Prospects and risks of inviting f foreign investors;</i>

<sup>32</sup> It was planned to return to this issue in the 2<sup>nd</sup> quarter of 2002.

<sup>33</sup> In relation to a great number of new offers, and also to the expected coming into force on January 1, 2010 of a legal norm for replacement of single social tax with social insurance contributions, which can raise the maximum rate from 26% to 34% of the wage fund.

indebtedness of companies by Vneshekonombank (the term of repayment of borrowings will expire October-December 2009)	2009	<i>Additional refinancing; Restructuring of tax arrears; Temporary nationalization; Realization of bankruptcy procedures</i>
Introduction of quotas for foreign workers in retail trade (in force till January 2010)	December 2009	<i>Influence on entrepreneurial activity; Competitiveness of businesses; Real possibilities and costs of control; Risks of higher administrative burden on enterprises</i>
Introduction of temporary price preferences for Russian goods in government procurements (in force till January 2011)	December 2010	<i>Changes in process and quality of supplies; Effect on enterprise behavior and innovation Competitive mode of procurement</i>

## 8. Main Problems and Contradictions of the Anti-Crisis Policy

In this section, we summarize some basic problems, which were revealed as a result of the expert assessment of a wide range of measures taken by the government of the Russian Federation in order to ease the consequences of the economic crisis in 2008-2009. Although these assessments are based on the working materials submitted by the experts, certain conclusions may not reflect the point of view of the entire group of experts, but present the opinions of the authors. Nevertheless, we hope that our analytical work can become a reason for constructive changes, first of all, in the procedures of elaboration of new measures, in the optimization of the measures under way and in further monitoring of their effects.

### *8.1. Some Fundamental Reasons Why the Effects of the Anti-Crisis Policy Have Grown Weaker*

In crisis conditions, the need to take prompt and radical measures that often go counter to the accepted logic of strategic decisions and former principles of economic policy is a serious test for any system of government. This is clearly demonstrated by the present practice of invention and acceptance of anti-crisis measures both in the EU countries and in the United States where decision-making has a long history of correction and tuning. This is an all the more serious trial for the Russian government because in this country, asystemic approach to the elaboration of economic policy was still unaccomplished before the crisis, so that making decisions and especially controlling their results in practice was never efficient enough.

We believe that a whole range of basic problems has been revealed because the system of decision-making suffered a rapidly increasing workload. These problems were acknowledged earlier but until the present made no serious negative impact on the quality of governing. In our opinion, analyzing the emerging problems of the anti-crisis policy provides a good occasion to have a look at the whole system of taking economic decisions, and possibly, to find some ways of reforming it. This will help improve the quality of governing and administration not only in times of crisis but also afterwards.

Below, we draw attention only to those basic problems of governing that predetermined many shortfalls in the anti-crisis actions of the Government since October 2008 till March 2009.

*Lack of powerful interest groups that are oriented towards modernization, and the absence of effective ways to communicate with them.* Failure of the authorities to create a “coalition for modernization” in the years of economic growth and to set up powerful groups of interests around the goals of renewal is perhaps the most fundamental problem of the design and implementation of economic policy in Russia. Many attempts were made to build mechanisms for interaction or, at least, for “reciprocal informing” between the authorities, the business community and society (deliberative bodies, public chambers, forums, efforts to involve representatives of business into discussions about agendas and concrete decisions), but *no efficient system for the coordination of interests and the elaboration of*

*concerted decisions as established.* Communication with the business community was often limited to a narrow circle of large and super-large corporations; general distrust between the authorities and businesses continued, and a mechanism for private-public partnership, which had been declared a priority, remained uncalled for. It would be unfair to blame only the state for the failure to build such a coalition. Poor communications efficiency was largely the fault of weak and inefficient business associations, and underdeveloped institutions and organizations of civil society. Nevertheless, the very fact that the government did not fully recognize its own need for such a dialogue is the main reason why many initiatives for modernization were slowed down and stalled, and offers to develop new instruments for economic policy were useless.

*The imited potential of the administrative system.* Even before the crisis arose, the public administration could hardly cope with its workload. Because anti-crisis measures are multiple and mostly selective (so that they need reliance on the operations of different inter-agency groups), the potential for public administration is limited, and *facilities for designing, discussing and putting into practice an anti-crisis policy which is both integral and divided into echelons are in short supply.* For this reason, the anti-crisis policy is open to the risks of lobbying and the making opportunistic decisions. This drawback is becoming a serious problem against the inconsistent and fragmented informational background of the anti-crisis policy, when the government is failing to distinctly advocate the concrete measures to be enacted.

*The range of tools for governmental influence is limited.* When the crisis broke out, the government had a limited range of tools to influence the economy (federal target programs, public procurement orders, taxes, tariffs etc.). Many of them are not flexible enough and have no devices for the regular optimization, improvement and transfer of best practices. When financial resources were abundant, the state had few good reasons to make them more effective and transparent and to create a system for high-quality monitoring the state of affairs by industry and sector (especially outside the area of government's influence). These defects were slightly moderated because *before the crisis there was enough time for the gradual tuning of certain tools, for their better administering and for learning to use them more skillfully first and foremost paying attention to the reactions of the business community.* At that time, the public administration could concentrate its efforts on the enactment of regulations rather than on monitoring their practical effects. In crisis time, it is impossible and even dangerous to tune the tools in the manner of "let us first act, then watch, and then react", especially because systemic mechanisms of interaction between the state and the business community have become much weaker.

We believe that *reserves for making the anti-crisis policy more effective* can be found not so much in putting forward one new proposal after another but rather in *improving the tools for their implementation.* Some arrangements, even conceptually correct and progressive ones, happen to lose their

clout because their tools are wrong, or their tuning is inaccurate, and because their procedures are inexact and non-transparent, poorly administered and formally monitored.

## 8.2. *Special characteristics of the generation and implementation of the anti-crisis policy*

We are aware of the fact that in the dire economic situation of autumn 2008, the government of the Russian Federation was obliged to take many measures in a hurry, in response to the arising threats, often having incomplete information about evolving affairs and no time for a careful evaluation of the measures it was taking and their possible aftereffects. The list of these measures is partly a reflection of the lobbying activities of certain companies or industries, and partly a result of “a surge of anti-crisis creativity” in ministries and agencies.

Hastily-declared measures in many cases were not, and could not be supported with carefully-designed legislation to ensure that these declarations could be put into practice. For this reason, actual execution lagged far behind the declared time limits. As a result, the *preemptive anti-crisis potential of a number of measures* remained unused. We have to recognize that on many occasions, the government overestimated its real administrative ability to enact the declared measures

The need to generate anti-crisis measures immediately had another important result: their initiation and provision was opaque, and the course of their accomplishment was non-transparent. Obviously, the *losses and risks from insufficient transparency tend to increase many times during a crisis*. We can describe this as counteracting asymmetric information.

(1) The government is not familiar enough with the current situation in Russian industries and their prospects. Consulting services that were helpful earlier are now working poorly. They give a better view of the state of large and super-large corporations, which are presented better, but depict the potential of medium-sized companies and new industries in an extremely fragmented way. This situation involves higher risks of lobbying for selective decisions and gives the entire anti-crisis program a bias towards the traditional economy;

(2) In turn, the business community and society are ill-informed about the sequence of the main steps of the anti-crisis program and about how the declared measures work in practice. As a result, their motivational power is lost, giving way to trading in insider information, so that the top echelons of officials get no adequate target information from the business community and society about the actual use and effects of the measures.

Without a doubt, there are different considerations in favor of limiting information. However, such limitations are likely to help make concrete decisions in the mode of a situational “trade” between agencies. This makes middle-level bureaucrats feel more at ease, reducing the risk of exposure of their blunders, and letting them readily declare, without good reason, that their actions have great practical possibilities. Such limitations diminish the responsibility of business associations (their accountability to

the members) and give an advantage to representatives of large and super-large corporations, who have better personal access to internal documents decision-makers.

From the point of view of the assumed measures, the main practical emphases of the anti-crisis policy are:

- To support the fuel and energy complex for the sake of fiscal stability;
- To support the investment programs of natural monopolies in order to expand domestic investment demand, with no serious steps taken to improve their management;
- To support manufacturing in order to diversify the economy, but with the stress on selective assistance to large companies that are often uncompetitive in the global market;
- To support small firms, but with the stress not on the growth of small businesses and their transformation into middle-sized ones, but rather on increasing their number.

This, in our opinion, can produce a *redistribution of resources in favor of traditional sectors; preserve an obsolete technological setup, create distortion in regulations and restrict conditions for the recovery of high economic growth after the crisis is over.*

The fact that a number of measures are not coordinated with the long-term strategic goals of economic development is fraught with the danger that the system may weaken: prospects for firms will become more uncertain, conditions for fair competition will be broken, and incentives will become destructive. This applies to the measures that are taken on one occasion only, such as the injection of additional capital, or the buying-up of bonds, etc., which leave recipients and other economic agents with unjustifiable hopes that similar measures can be repeated in future. This is also true of some institutional changes that will have long-term consequences. The essentially extraordinary anti-crisis measures, which distort the natural institutional structure and substantially change the “rules of the game”, are often taken with no strict time limits or at least an indication of the conditions when their abolition will be debatable. On a number of occasions these changes have led to “traps” (inefficient equilibria) that may require new sets of “post-crisis” measures in order to find a way out.

In our opinion, many defects that are typical of some means for directly supporting producers could be avoided with a wider set of “counter-requirements” to the recipients of state assistance. This should not be requests for fixed or controlled prices (although this can be possible if a recipient is a monopoly), but demands for modernization and improvement of competitive power. No doubt, in many cases such “counter-requirements” exist in reality, but they are also opaque and non-public.

### 8.3. Tendencies and Dangers

1. An expected radical decrease in the amount of resources at the government’s disposal for the anti-crisis support of the real economy will no doubt become the main tendency. This decrease will occur for natural reasons, because tax revenue and other fiscal revenues will decline. The needs for social support, first of all for the underprivileged, will grow; difficulties will arise in many regions, and inter-

government transfers will have to be extended. Enterprises forming company towns will probably face new challenges.

2. If the global crisis is prolonged (which no one can rule out), focusing on instruments for selective assistance will be produce areas of “chronic distress”, which will call for more and more spending. Industry-wise priorities in the anti-crisis policy that are determined now (they are addressed to the most vulnerable sectors) have become predominant in the direct or indirect allocation of resources through systemically important banks. This can lead to excessive concentration of public and private funds a given to solve the problems of large companies, while more promising firms will face additional resource constraints. This approach can be acceptable only if one is sure the crisis will end after 2009.

3. A prolonged crisis can turn temporary protectionist measures into constant ones and encourage interest groups seeking wider and stronger protection from foreign competition to exert powerful pressure on the government of the RF. If this practice becomes widespread, it will increase the risk of inflation and suppress final demand. This outcome is undesirable in the phase of recession as well as in the phase of revival.

4. An extension of assistance to private businesses in exchange for a higher share of the state in equity capital can unfold another round of “creeping nationalization” without any improvement in performance. This will impose a higher responsibility on the state for everything that happens in the economy.

5. Facing a lack of ready cash for aid, the government will find a way out in withdrawals of money from institutions for development (which were established in order to achieve the ambitious goals of the technological modernization of the Russian economy). The government will exert fiscal and administrative pressure on “affluent” enterprises that have managed to adapt themselves to new conditions and survived without any public assistance. Moreover, a decrease in resources for the anti-crisis policy will expand the range of non-monetary (regulatory) measures.

6. If the federal authorities are unable to support regional economies in distress, the regions will most likely unfold unauthorized anti-crisis activities of their own, relying on an abuse of their administrative power.

We have indicated the negative effects that *can come into being* if approaches to the design and implementation of anti-crisis measures are not renewed even in 2009 in a relatively “calm” situation (in comparison with October-November 2008), and if there is no coherent program which will not only alleviate the recession and compensate for its negative effects but will also offer real ways for modernization (the development of new industries, human capital and innovations). In this context, we only have to express our regret that the Anti-Crisis Program for 2009 of the government of the Russian Federation which has been presented for discussion is more exactly an attempt to organize all measures

that are under way or were declared earlier. At the same time, we appreciate the very fact that the compilation of this Program and its presentation to the public is an extremely positive one.

## 9. Recommendations

The authors of this report do not claim to know the secret of how to carry out anti-crisis measures successfully. As we have already mentioned, these measures can be elaborated only in a dialogue between the government, the business community and society. Nevertheless, in this report, considering the decisions that have already been accepted by the government we have tried to understand their possible short-term and long-term outcome and to assess the costs and risks of putting them into practice. In addition to the qualitative conclusions presented in the previous section, this kind of analysis has enabled us to formulate some definite ways of improving the mechanisms of their implementation.

For a start, it would be reasonable to make the *procedures of the generation and implementation of the anti-crisis policy* more substantiated and transparent.

Firstly, an initiated and, what is more, an accepted measure must be declared clearly in relation to its ultimate goal. It must contain assessments of its main beneficiaries, its expected effects and possible problems (risks).

Secondly, the concrete design of a measure, including the ways of giving support, must be made about the projected enactment (conceptions of legislative documents), in consultation with businesses and concerned social organizations. It is important that business associations and social organizations should request the publication of official assessments.

Thirdly, schedules must be set for putting each measure into practice, with test points for controlling them together with the business community and society.

In fourth place, all enacted legislation on anti-crisis measures must undergo mandatory tests for the availability of adequate and strict requirements for the disclosure of information and transparency of decisions.

The availability of such predetermined test points and an appropriate level of disclosure of information will make monitoring the implementation of the anti-crisis measures feasible and will enable the opening of feedback channels, which can permit decisions to be made for the correction or abrogation of relevant measures, if necessary.

We recognize that under present conditions, there is an objective need to transfer a number of important decisions to the level of the government of the RF in order to meet the challenges of this crisis more flexibly and immediately. Nevertheless, we believe it is reasonable to apply some elements of the information that is regularly prepared in support of law enactment to government regulations in order to ensure their proper grounding. For instance, deliberation of a bill involves, in addition to its text, the availability of its certificate, an explanatory note, evaluation of the fiscal results of its enactment, and

letters of approval from steering committees of the State Duma. The Government is using procedures that are similar in many respects for the deliberation and approval of federal targeted programs.

In our opinion, if there is a need to adopt additional anti-crisis measures, the availability of their certificates, explanatory notes, evaluations of the fiscal costs (losses) of their enactment, and letters of approval from relevant ministries and agencies must be made mandatory. In our opinion, to make an all-inclusive appraisal of a proposed measure, the conclusions of concerned business associations and social organizations are also necessary, as well as the results of expertise on possible corruption, of which the Ministry of Justice is in charge, and a schedule for the implementation of the measure.

We believe that the range of instruments for the anti-crisis policy must be gradually enlarged. With this end in view, the laws and regulations in force must be systematically improved to facilitate a more flexible reaction to coming challenges. In a recession, we perhaps cannot do without “calling fire brigades” for the alleviation of its social and economic problems. Nevertheless, we must urgently begin to design in advance the measures that will be needed by the final phase of the crisis. These measures must include bills, prepared beforehand and ready to be enacted without delay for the abolition (at once or step-by-step) of the measures that were in force during the recession but will then disagree with national strategic interests. Among others, this refers to the problem of “how to exit from nationalization”.

Special attention should be paid to an improvement in performance of state-owned companies and natural monopolies, along with a revision of their development strategies that must comply with national needs both during the recession and the time of economic upturn. This segment of the economy is, for the most part, the area of government responsibility, and its impact on the rest of the national economy is very strong. We believe that in the preparation of measures that will support certain industries or enterprises, there must be the lowest level of inefficient substitution. Social policy tasks such as support of the unemployed and the creation of new jobs must not be substituted by the artificial support of extra demand for hopelessly poor products. Support of demand can be justified only in cases where there is a need to maintain not only jobs but also facilities and skilled personnel. This is reasonable either when it is certain that these resources will remain in need after the crisis is over, or when this policy is justified for national security reasons.

Finally, it is important to define and begin to put into practice, even in the phase of recession, the measures that could enable us to shift from protection of “the most vulnerable” economic agents to support of “new engines of growth”, which can greatly accelerate the post-crisis economic revival.

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