

Full Transcript: Gabriel Di Bella (IMF Resident Representative in the Russian Federation), with Dmitry Butrin (Commerzant).

*1. We know you not only as an international organization, but we use your reports and your research, and could you describe your current program of research in Moscow for the next two years?*

Let me first tell you that yes, the Fund does analysis and research on Russia. The type of analysis that we do is framed in the context of what we call "Article IV consultations". These Article IV consultations refer to the part of the IMF Articles of Agreement that define the type of surveillance activities that we do in our member countries. In a nutshell it works like this: a team of the IMF comes to Russia and discuss with the authorities the economic challenges in the short term and the medium term, and tries to identify and propose adequate policies to address these challenges. What we bring to the table is the experience of the 189 member countries of the IMF, and we leverage that experience in the discussions with the authorities. So let me tell you a bit about the conclusions and what we talked about in the last of these consultations in 2016. Basically we analyzed how the economic stabilization was proceeding and how to make sure that the policy mix that was implemented simplified the adjustment and resumption of growth. Also from the medium and long-term perspective what we tried to analyze what reforms are needed to resolve bottlenecks and promote higher long-term growth. In the next few years, we are going to do is, in general, try to continue this research agenda. What we expect for 2017 is that the economy will resume growth, but since the output gap is not very large, growth in the short term will not be very high. In this context we are for sure going to continue the analysis of medium-term reforms that are needed to jump-start a process that would lead to higher medium-term growth.

*2. In Russia we are having a great discussion about the slow-down in growth in the last three years, yesterday in the government there was a discussion, and I was participating, and there were actually several models or explanations offered. I argued that Russia is in a very unusual middle-income trap, other experts think that it is an ordinary structural constraint that we have failed to remove. My question proceeds from my assumption that we have a unique combination of a cyclical downturn and structural constraints on growth. What model does the IMF use? What are the Russia-specific reasons behind the slow-down?*

That's a great question. To answer the question, we need to put Russia's growth in context. It is absolutely clear that the conditions Russia is facing right now are completely different from the conditions Russia was facing at the beginning of the 2000s. And I use the beginning of 2000s because that was a period that witnessed very high rates of GDP growth in Russia as well as very high rates of consumption growth. It is essential to understand where the Russian economy stands now and where Russia stood at the beginning of the 2000s. At the beginning of the 2000s Russia had very low rates of capacity utilization. This means that Russia could grow just by taking advantage of installed unused capacity. The second element

that was present was relatively low oil prices; third, there were large technological gaps, including in the energy sector; and fourth, there were relatively low, competitive wages. The increasing oil prices during the first few years of the 2000s allowed the country to increase demand and grow in part by using that unused capacity. Of course, this also allowed the technology gaps to be closed, in particular in the energy sector that now is internationally competitive, but at the same time demand expanded too fast and that made wages to grow more than productivity. Where is Russia right now? After the devaluation of 2014-2015 and given that this devaluation was higher than inflation Russia is in a situation in which wage competitiveness has been restored. But the picture regarding capacity utilization is completely different. Levels of capacity utilization are high, and to that we must add that the prospects for labor supply are not very bright because given demographic trends it is expected that working age population will decrease. So right now we are at a point where Russia needs to rethink its growth model. The question is how to make sure that given these initial conditions Russia begins growing more. It is clear that since Russia is at high levels of capacity utilization, that the only way to grow more is to increase capacity – through higher levels of investment. In terms of the labor force the way to go about the constraint that the shrinking working age population is going to represent for the economy is to make sure that policies that aim at fostering human capital are put into place so productivity growth compensates decreases in labor supply. And in general Russia needs to ensure market competition so resources go to those sectors in which they are most efficiently used.

*3. Proceeding from what you have just said, from the picture and from your framework my understanding is that one of the key constraints is the labor market and the capacity in this area. Proceeding from that we may infer that a key reform could be in the labor legislation. What principles should we be guided by in reforming our labor legislation, what could be done? Having in mind two things: in Russia, we have a long social and democratic tradition, but on the other hand we have no trade unions in this country, effectively. So what would you suggest, how should the government or people in the government who are thinking about that, how should they proceed and what should they have in mind thinking about this reform?*

That's a good question and maybe I should have emphasized when I answered the previous question that I focused on the main, broad, determinants of growth, but that there are other determinants to growth as well. In terms of needed reforms, labor market policies are not the only area that needs attention. And before discussing other reforms, let me clarify that we think reforms need to be implemented in the right sequence. Reforms work better when they are properly sequenced and prioritized. And so the first of these reforms is to make sure that oil price fluctuations do not unduly affect competitiveness in Russia. What has happened in the past is that oil prices had been very much driving economic cycles in Russia. And at the heart of this is the role that the budget has played propagating into the economy fluctuations in oil prices. So, to go back to your question, having an adequate and well-functioning labor market most likely is not going to be very effective in promoting high growth rates if on the other hand the economy is not competitive because the exchange rate is too appreciated. This

is what I mean by proper sequencing. First of all, I think that Russia needs a macro situation that is stable and predictable. And in that sense the adoption of a new fiscal rule is essential, it is essential because it's going to break the link between fluctuations in oil prices and fluctuations in economic activity, and thus fluctuations in competitiveness. Going back now to labor market policies, when you look at Russia's labor market in comparison to that of other countries, Russia's labor market legislation does not actually compare badly. But the angle that we think deserves a deeper look is the implementation of policies to create and support human capital. Because as I said before the problem in Russia in the next few years is that working-age population will shrink in size. There is a need for better connection between businesses and education institutions, vocational schools. A more integrated and mobile labor market would also be helpful. Policies to support human capital and infrastructure formation are important, but then there are other reforms that need to be taken into consideration. Pension reform would also help, by supporting increases in labor participation rates, at the same time that would promote fiscal sustainability. Moreover, to take advantage of the fact that Russia has a large market size, it is important that administrative pressures are reduced, that property rights and governance are strengthened, as this would contribute to improve the perceptions of economic agents and promote investment. One additional thing that I would say is that in Russia there is a large divergence in income per capita and productivity across regions. And so it would also be important to implement policies that gradually reduce these gaps.

*4. It's an issue discussed by several government councils, because we have several points of views on this. Maybe it's not a decision because this gap is native. WE are discussing the destiny of one such regions, close to the western border, Novgorod region. The main reason for economic depression in this regions has roots in World War II. This region was severely affected by the occupation and after that it has been in economic depression for 70 years. It's impossible to do anything with history. This region as an administrative region is dead. There is no economic mechanism, no community, it's finished. However, our government spent a lot of money in attempts to revitalize this dead community. The spending on this region is two or three times more than any usual spending for other regions, there are no taxes, but there is still no industry and a devastated agriculture – only tourism (Novgorod is a medieval city). Why do we need to spend so much money there?*

These challenges do not exist only in Russia. And of course, historical considerations shape what the challenges are now. It is possible that policies may not have worked. But at the same time I think the question continues to be relevant. The issues that you point are important issues and point to having the right mix of government programs to help regions cope with their structural problems. But I would not say that the right decision is just to forget that the challenge exists. The challenge is there, and the question is then how to address the challenges in order to solve the problems that Russia has.

*5. In the list I had a question about the tax reform, which we may consider as a structural reform. It's what here in Russia we call a tax maneuver, but what is called fiscal devaluation everywhere in the world. It's about decreasing the payroll tax while increasing indirect taxes, VAT specifically. Is there any international experience that you could cite that could give us bearings to do it appropriately because this is something that the government seems to be about to do.*

I have read about this debate that began, if I am not mistaken, already in 2016, and now it seems to have resurfaced. And in that sense let me tell you a number of things. First of all, Russia has done quite a bit in improving its tax system, and also tax administration has much improved. This needs to be recognized. At the same time, talking about what needs to be done, I think that the implementation of the policy that you are mentioning would be actually quite sound. However, there are some elements that need attention. The first is that a reform should be revenue-neutral. If payroll taxes are going to be reduced and VAT increased, the reform should be implemented so fiscal revenues do not decrease. This is essential. The second thing that I would say is that the distributional aspect of the reform needs to be taken into consideration. Decreasing taxes on labor could, in principle, facilitate that sectors that are now informal become formal, and this is a good thing. At the same time, taxes on consumption are heavier on the sectors of the population with relatively lower incomes. So analyzing the distributional impact on the reform is important. But, overall, we think it is a good idea. In terms of what you say about fiscal devaluation, it is true. This is something that has been widely analyzed during and after the global financial crisis in Europe. The example that comes to my mind is Spain. But there are others. And so in that sense there is policy precedents in countries in Europe that can be taken into consideration while analyzing the implementation of a reform like this.

*6. There is mixed experience from Hungary and Romania. In Hungary it was very difficult, and as I understand they want to cancel this fiscal devaluation, and in Romania it works, and I can't understand differences. They seem to be doing the same things, but the result is different. I can't understand why and I hope to find some analysis in your policy papers. It is so interesting, and I know people are working on it.*

I think there are two different issues, two angles from which you can look at these questions. There is a "principles" perspective and then there is an "operational" perspective. What I tried to address in the first part of the question was the point of view from the "principles" perspective. And from that point of view the idea is a good idea. But as you rightly point out there are operational challenges associated with implementation of a reform like this. And so what I would think that could give some clues as to why it has worked better in some countries than in others is not necessarily because the principle is wrong but because operationally the sequence of implementation of policies may need revising.

*7. To finish up with my questions about structural reforms, my last question would be about tax administration and about informatization – about building an integral information system to cover, to embrace everything that is happening in this country. Today is an important day in this respect, because today a government resolution was passed to put in place an MIS for social payouts. These efforts have been going on in the last seven years, and now they have finalized that. In the next three years hopefully there will be a really great MIS covering retail payments, bank payments, taxes, social payments and everything else. Of course, it is an important development because it will bring into the light many shadow sectors of the economy, but what do you think, we all know there are some sectors that cannot exist out of the shadows, they can exist only in the shadows because otherwise they won't be competitive. How would you estimate the ultimate effect of this MIS being built to cover everything, will the real effect on growth or economic performance be really as great as we may imagine?*

*Of course we understand there will be a lot of labor released in these sectors, but on the other hand this is not skilled labor, so it may just result in higher unemployment. So there may be negative implications of these technological improvements?*

First of all, I agree completely with you that this is good news from the point of view of tax administration. There was also one piece of news at the beginning of 2016, good news, related to the fact that the Ministry of Finance has now the collection of taxes and social security contributions under its purview, and this creates the scope for more coordination and collaboration between agencies, and that should result in a more effective fight against tax evasion. I think that you rightly point out that there are challenges associated with more pressure to collect, but in that sense I think that the reform that you mentioned a few minutes ago, increasing taxes on consumption and decreasing payroll taxes would go into easing part of the pressure that some of the firms may be feeling. In the end I cannot see the informatization of the tax agencies and more collaboration between them to fight tax evasion as something that is bad.

*8. Before we pass on to the next question, maybe you have something to add about the structural reform. In the last two years Dmitry has been asking the government about what structural reform they are going to implement, and apparently there are four of them, and two of them are quite good.*

We have been talking already of reforms and I think I have covered what we think is most important. But let me reiterate that it is essential to ensure that the economy does not fluctuate every time that oil prices fluctuate. In that sense I think that the lower oil prices have actually catalyzed some reforms. If you look at the implementation of inflation targeting, if you look at the implementation of a floating exchange rate -these reforms are not easy reforms-, and they have been implemented and have eased the adjustment after the dual shocks of 2014. The government is also taking incremental steps to formally adopt a new fiscal rule, and if this is done it is going to significantly change the way Russia's economy

operates, because it is going to make the economy much more stable and make it less dependent on oil prices. So there are many policies that have already been implemented, and if they are consistently implemented through time, basically if they are not reversed, they would very gradually change the face of the Russian economy. But it is important to point out that the reforms that I described before are not going to result in a huge impact on growth in the short term. And also, that in order for these reforms to produce effects they need to be consistently implemented during long periods of time. I will give you an example. For instance, Chile during the 1970s and a good part of 1980s, it was an economy that was very much exposed to fluctuations in copper prices. And the composition of its exports was non-diversified, was mainly related with copper. It took Chile a long period of time – 15 to 20 years – of consistent implementation of clear macroeconomic rules, of consistently implementing prudent policies at the central bank, to begin diversifying and have an economic structure that is much more resilient and diversified. So this is the time frame that we are talking here. And what we have in Russia is a certain reform cyclicality. When oil prices are low there is more incentive to push for reforms because the budget constraint becomes binding. But when oil prices are high this binding constraint is not there any more. And so, while diagnostics are right and everyone knows what policies need to be implemented, reforms proceed more slowly. This type of reform cyclicality needs to be broken if Russia is to increase long-term growth.

*9. It's interesting. When we talk to people they have a question: what do we need to export in ten years? Lasers, heavy machinery, copper, IT exports? I would answer these people: you shouldn't be bothered by this, nobody knows what will happen in 10 or 20 years. Chile may be not a wine exporter and not a grain exporter but maybe seafoods or roses. Nobody knows what we'll be in a new world. Maybe we'll be a great automobile player, maybe an agricultural machine player, or something else. But we hope that in the next 10 years we'll be somebody in the world market.*

*I've been telling these people, vice PMs in the Russian government, you don't have to put your finger on it, why do you want to know what specific exports Russia will need to have in 20 years? You just need to create an environment, you need to create a conducive environment for everything to develop and evolve how it should and then in 20 years we'll see what comes of it, what emerges, what grows in this fertile soil. How is it done globally? Do other countries and their governments also want to put their finger on what they are going to produce in 20 years and what they are going to export in 20 years, or there is a psychological understanding that they should create a conducive environment and let everybody flourish in this environment?*

I think you make a very good point. And I think the truth may be a little bit in the middle. Let me tell you why. It goes back to something I said before. Prioritization of reforms. Adequate sequencing. I fully agree with you that one of the main tasks of the government is to create adequate conditions for investment to happen. I fully agree with that. At the same time, I

think that there are policies that operate very gradually and also simplify the task of identifying those products that you mentioned. For instance, if the country associates with India, it will create incentives for specific sectors to develop. India has a specific market size, has a specific demographic situation, has a specific growth rate, has specific needs. And so what India needs is different from what Germany needs. And it's different from what China needs or Argentina needs. And so in a way policy should operate at the two levels. Policy should operate at the level to establish adequate conditions for investment. Because if the country does not establish those conditions, even if you know everything about India, the country will not be able to export to this market. At the same time policy should operate at the level of finding markets and simplifying the operation of firms dealing with those markets. Policy makers should try to identify what the most dynamic markets will be and you associate with them. This is the kind of strategy that successful countries like South Korea or Australia have applied. They have opened to trade, they have implemented these policies consistently during a long period of time, with results that happen relatively slowly but incrementally.

*10. My next question that is not often asked in this country is about institutional reforms. The government now seems to think that institutionally they are ok, that they have a stable institutional structure. What is your view? Do you think something can be done in this area, some institutional reform is still needed that can facilitate our development?*

That's a good question. There should clarify that the IMF has a specific focus and a specific mandate, and our mandate is related to analyzing the economy and what reforms in the economic environment can be implemented to ease adjustment in the face of shocks, to promote stable growth in the short term and increased growth in the medium term. In that sense the reforms that we are talking about here are reforms that would affect economic institutions. And this is the reason why we talk about fiscal rules, why we talk about policies to support infrastructure and human capital formation, that's why we are talking about reducing the footprint of the state in the economy. In particular, with regard to this last element, we know that such a footprint is quite large, and we think that there are elements that could be improved. For example, I have not seen any study analyzing the impact that the large number of state owned enterprises has on competition in different market segments. Russia has around thirty thousand state-owned enterprises combined at the federal and regional levels. So the question is: What is the impact from these thirty thousand state-owned enterprises on competition?

*11. I have one awkward or unpleasant addition to this question dealing with the recent upsurge in autopiloted vehicles. The government is concerned about this, and in the last month they have been talking a lot about what to do with it. To put a ban for the next ten years? That's what they would like to do, but they realize that it may be impossible. On the other hand, they have their national security concerns, because their arguments are that these evil foreign states may at any point stop it, impose cybernetic sanctions, etc. If we allow*

*this to develop in this country we will be dependent on foreign states who source these things, because we are not participants in these global efforts. I realize that we cannot quantify the potential negative contribution of this factor but do you think it has a relevance?*

With respect to this specific issue I have to admit that I probably have not much to add. I could say something about innovation and technologies in general, to go on to something more general than the specific point that you make. I think that with respect to the adoption of technologies and innovation, we could focus on two things. First, with respect to policies geared at facilitating the adoption of new technologies, I would go back to what I said before. The right sequencing of policies makes the adoption of technologies more feasible. If the economic environment is characterized by inadequate relative prices, the adoption of technologies is going to be more difficult. The second thing I would say is that the adoption of new technologies creates winners and losers, and so if policies promoting the adoption of technologies are successful then there will be a distributional implication. And this distributional implication needs to be taken into consideration. It is similar to what happens around trade. International trade creates winners and losers. And if policies don't take into consideration that distributional impact, then countries are prone to experience negative reactions from those who lose.

*12. Now let's pass over to international trade. That was a long question, Dmitry is saying it will not be included in the questions, but he is just giving you examples for the sake of this discussion. In January, he had a discussion with somebody from the European Commission who was asking him "Are you really sure you want to produce all this stuff locally? We all know that you can do it, but what do you want it for? Do you realize that it will be twice as expensive as imported goods? Of course, Dmitry realizes that and many other people do, but on the other hand there seems to be a sentiment here that we should produce everything that we can produce locally. Is it really reasonable? Does the IMF discuss this issue of international division of labor with the government and try to get it across to the government that you don't need to produce everything here because it's not efficient and the issue of costs and benefits is really important here.*

I understand, but I am not sure I agree with the premise of the question. In our discussions with the authorities –we may have been talking with different interlocutors–, we do not perceive that the aim is to produce everything here. At the same time, I think that there is a recognition that Russia was too expensive before the devaluation and then a more appropriate level of prices, and by that I mean a complete set of prices including wages, that is more consistent with Russia's productivity, would automatically create opportunities for import substitution. In that sense, the process that Russia has experienced in the last two years goes is the consequence of realignment of relative prices. What we see is that during both 2015 and 2016 the factor that acted as buffer to the economic downturn was net exports. This is an absolutely reasonable and normal process. There is a domestic market, this domestic market was importing too much, because the ruble was too expensive, and having a ruble that is



much more in line with the country's productivity creates opportunities for domestic producers to actually supply to domestic consumers. This is not bad. At the same time, I take your point, and the point you make is reasonable. No country can produce everything efficiently. But again the sense that we get from our discussions with the authorities is not that the objective is produce everything domestically. One additional point that I would make is that many of the foreign firms that came to invest in Russia during most part of the first decade of the 2000s had the objective to supply the domestic market because income per capita were growing very fast and the size of the market was expanding very rapidly. The fact that Russia has a real exchange rate that is now more aligned with fundamentals creates two answers for the question: Where to sell? Firms in Russia can now sell domestically, including substituting imports, but the option to sell abroad has also opened. – Russia is more competitive now. This process has just begun. And in order for Russia to begin exporting more and not just doing import substitution what is needed is stability and predictability in macro environment. This means implementing consistently – I know I am repeating this quite a bit, but it's essential – implementing consistently a good fiscal rule and implementing consistently inflation targeting. This is going to create the conditions for more diversification. These policies are not sufficient for investment to happen, but they create the basis, the necessary conditions for investment to happen.

*13. Let's talk about the government's role as an investor, since we don't have a capital inflow yet, and the government has to look at itself as an investor.*

*We can see that the government realizes all the weaknesses of this solution of being an investor*

In what sense? Through state-owned enterprises or through federal and regional governments?

*Rather through state-owned enterprises. Dmitry thinks that the government sees all the weaknesses of this solution, and it does not want to be an investor at this point, it is trying to avoid it, but is it possible as a second-best solution, potentially possible solution for the period when we have sanctions. What does the IMF think?*

Let's put it like this. There are two issues: the first issue is the issue of basic infrastructure and human capital. Sanctions or no sanctions, the federal government and regional governments have a role to play. We recognize that going forward – and this is done in the three-year budget – consolidating fiscal finances is needed. At the same time, we think this consolidation should be done in a growth-friendly manner, preserving infrastructure and education spending in order to support human capital formation. At the same time public resources are not unlimited. There was a law that was approved last year on Public Private Partnerships, and we think that it may provide an avenue for solving for instance the need to expand and improve infrastructure. Now, in terms of state-owned enterprises – and I touched

on this issue before – I think that irrespective of sanctions the footprint of the state in the economy is large. There are some estimates here and there but there are no official statistics for how large the overall government is as a share of GDP. This is something that would be very interesting and useful to know. The IMF does not have a “principles” position that private is always better than public. We don’t say that. What we say is that if there is going to be a participation of the state in the economy, it is important to define why that participation is needed, and that if indeed the state will participate it should be done efficiently, without creating contingent liabilities for the budget, and without preventing competition from happening, because when competition is prevented then the adoption of technology is slower and in general economic dynamism suffers. Of course, in the presence of low oil prices or economic sanctions the conditions to privatize are more difficult. But then again the general point that I am making is valid with or without sanctions.

*14. Talking about the state footprint in the economy in Russia, - this question is not in the list, but I think it is important to discuss it. A specific feature of Russia is that this footprint concerns first of all the banking system, and government banks are very much involved in the economy, so participation of the government is via lending by government banks. What can be done about it? Is it so bad? We realize that we cannot privatize these banks at this moment at least because there are no buyers for them – nobody wants to buy these banks. Dmitry calls it nationalization of credit. Do you think it’s an issue and what can be done about it?*

So I am sure you know that last year around this time the IMF together with the World Bank conducted what we call a Financial Sector Assessment Program. The analysis in these reports attempted to establish whether the Russian banking system is stable, what risks the Russian banking system is exposed to, whether the framework of supervision is adequate and how to improve it. This is in very general terms what they cover; the documents are available – they are public information. There are a number of conclusions that came out of these reports. In that regard what you say is true – that there is high concentration in Russia’s banking system, which has a very large number of banks – around 700 – but at the same time is deeply concentrated – the top ten-fifteen banks concentrate about 70 percent of all assets and liabilities. The report concludes that in spite of the fact that the state has a controlling share in the largest banks, these banks are managed relatively efficiently and operate with commercial purpose. And this is one of the reasons that has given resilience to the core of the banking system. I understand the point that the largest banks have a large share of the state in their capital but it has not prevented them from operating efficiently and commercially.

*15. The last two questions. Concentration of output on productivity and growth rates. It is related to the previous question because of course the practices of state-owned banks, even commercial banks, are still different from those of private banks.*

Going to concentration outside the banking sector. Russia inherited some of the features of the Soviet Union, and this is reflected in high concentration in industries like energy, metallurgy, utilities. What I would say is that in sectors that economists call “natural monopolies” concentration is to be expected. In these sectors what is important is that adequate regulation protects consumer rights and ensures that investment in modern technologies happens and that users receive good service. But there are other sectors that are not necessarily natural monopolies in which concentration is high and where decreasing barriers of entry -formal and informal barriers of entry-, would increase competition and productivity and facilitate the adoption of technology. I think this is a challenge. And to go back to the footprint of the state on the economy, I think it would be interesting to analyze - and this is something that we are analyzing- whether there is an impact of this large number of firms into how competitive or concentrated markets are in Russia. The issue again is not that there are public enterprises. The issue is whether the existence of public enterprises actually prevents competition, adoption of technologies and economic dynamism. There is no fundamentalism in terms of private or public. We are not saying that private is always better than public, not at all. What we are saying is that if there are public enterprises, let’s see if these public enterprises prevent competition or make the economy less dynamic.

*16. Public administration. Whenever we talk about constraints on growth and the economy everybody would be saying that the key problem is public administration and we should do something about it. In this country, in the past three years, the government seems to be embracing very actively and enthusiastically corporate governance practices like for example project management, which is quite in the vogue now – the project office in the government, trying to do everything on the project basis. What does the IMF think? Does the IMF see any specific risks in this adaptation of corporate governance practices to public administration? Or it’s possible and good and useful?*

This exceeds a bit what I can say because this is very recent and many of these issues we are going to discuss with the authorities in the next Article IV consultation. In that sense we need time to analyze the implications of this for public administration, we need to discuss with authorities the details and only then we are going to have a better idea and a complete judgement. At the same time, I take your point that public administration is one of the issues that is usually put near the top of the list of things that need to be improved to make Russia more attractive to business. But let me tell you one thing because maybe we have not emphasized enough this point. Now I am going to talk much more generally. When one looks at Russia, at its implementation of reforms in the last 15 years – and we did this analysis in our last Article IV consultation – what one sees is that Russia actually has done quite a lot, that competitiveness gaps of Russia vis-à-vis OECD countries have decreased quite substantially. In public administration, for instance, there have been a number of reforms - I am sure you are aware of them – procedures that before were very time-consuming, were quite cumbersome, now can be done online faster, at a lower cost and more efficiently. At the same time there are areas where the authorities themselves recognize that progress is needed.

And they are related with public administration quite concretely. The first one is the so-called administrative pressure, inspections, how these inspections actually work and how much undue cost they generate, especially for SMEs. Another issue somewhat related to public administration is customs. And in turn this is related to the ability for export diversification and import substitution. And there, in spite of the fact that Russia has consistently improved in rankings of cross-country competitiveness, no matter if you use the World Bank Doing Business indicators or the World Economic Forum Global Competitiveness Indicators, we see consistent improvement across a range of indicators, but for customs operations Russia continues to compare quite poorly with peer countries. In this area there is an opportunity, because improvements would simplify enormously the business of firms that want to export, that want to access other markets, that want to diversify.

*17. One of the key risks that local businesses are concerned about is the risk that competent managers come to the Customs. Because they already have an experience with the consumer watchdog (Rosпотребнадзор). Because a strong state for them means a change of the rules of the game, and they are afraid that they won't be able to adapt to this change quickly.*

Just one quick comment on that. It is quite interesting what you say because we have access to surveys and communication with experts at Russian universities – conversations with businesses both Russian and foreign, and what they tell us is that improvements in customs administration would make their work much easier.

*18. Many people in this country think that even if we don't do anything, if we don't undertake any structural reform, don't take any efforts we'll still be growing at some 0-1.5 and after all everything will be as it is now. What do you think are the possible exits from this situation? Is it so that if we don't do anything we'll just stagnate and go on like this for some twenty years and nothing will happen or there may be various options?*

Basically the question is if there are no reforms what is going to be the outcome of this no-reform scenario? The outcome of the no-reform scenario is low growth for a long time. As I said before, Russia is facing a situation with decreases in working age population, where capacity utilization is very near the average of the last five years so growing out of unused capacity it is actually quite impossible. In addition, productivity growth is actually at the lowest point in the last fifteen years. Of course, productivity growth -that I measure by output per worker- is being influenced by the recession of the last two years, but nevertheless around 2012-2013 one can already observe a decrease in growth in output per worker. And this actually reflects the point that the growth model that worked in Russia during the first ten-eleven years of the new century has been exhausted and thus a new, different growth model is needed. You asked before about the middle-income trap and the challenges that it poses and I would say that the challenge is that in order not to fall into that trap Russia needs to implement reforms that leverage, that take advantage of what has been already achieved like price competitiveness, and continue the consistent implementation of inflation targeting,

and complete the adoption of a fiscal rule, - these are important reforms that need to be consolidated. Other reforms that we discussed before, need to be adequately sequenced, adequately prioritized and consistently implemented. If this does not happen then Russia's growth is not going to be too high.

19. This is not the question for us to ask or answer. This is a question for policy-makers to ask and try to answer. And for the Russian population to decide whether they would be comfortable growing at zero or they would want their sons and daughters to be better off than the current generation. This is a question that exceeds us. What I would say is that in general our advice –IMF's advice- is geared at how to avoid stagnation, how to improve the functioning of markets, how to make sure that better technologies are adopted, how to make sure that the macroeconomic situation remains stable and creates conditions for growth. I think it is really useful for citizens, for policy makers, to be thinking about these issues because then a search for reasons, for appropriate diagnostics occur, and only then the right policies can be identified and implemented. I would also say that this period of low growth has not lasted for that long. I would say that after the decrease of oil prices of 2014, a consensus has been achieved that the factors that prompted large growth rates during the first decade of the 2000s are not there any more, that Russia will not achieve those high growth rates in the short term, and if reforms are implemented consistently and without pause, then Russia can grow more and go beyond the low growth rates that were experienced in the last few years. But again our role as an institution is to bring international experience to the table and discuss with authorities how to overcome stagnation and low growth. It is for others to decide whether stagnation can be a good or bad social outcome.