

News Analysis: Why Putin Isn't Raising Utility Rates

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Prime Minister Vladimir Putin's decision to moderate the annual increase of key energy and railroad rates next year has more to do with upcoming presidential elections than an attempt to spur economic growth, economists said Tuesday.

Ostensibly, if the government-regulated rates for electricity, natural gas and rail freight services increase in the tempered fashion that Putin ordered late Monday, it could dampen inflation and encourage companies to borrow for development. But analysts see a different agenda.

"It's clearly related to elections," said Peter Westin, an economist at Aton. "I would argue that the net effect is actually negative from this decision, and it's purely driven by politics."

Except for rail freight, other state controlled rates will now go up July 1, six months later than in the past — so people will not see higher household bills until after presidential elections

in March. Putin, or incumbent Dmitry Medvedev, is strongly expected to run.

Rail freight tariffs will go up from Jan. 1, as has been the custom for all such hikes.

First Deputy Prime Minister Igor Shuvalov denied late Monday that any electoral motives underlie the decision on rates. It is not a one-off measure, he said, and changes to regulated rates, if any, will from now on always take place in July.

A Putin-chaired budgetary meeting, which ended close to midnight on Monday, not only delayed expected rate increases, but also kept them lower. It was decided that state-owned Russian Railways can charge only 6 percent more next year for carrying freight — in line with how consumer prices will presumably grow — starting in January. Russian Railways asked for a 7.4 percent hike.

Instead of the higher rate, the government will provide a subsidy of up to 40 billion rubles (\$1.3 billion) at the end of this year, about the amount that the rail monopoly wanted next year in order to make up the shortfall.

Regulated rates for electricity will also rise only 6 percent, in contrast to the previous plans to raise them as much as 15 percent, Putin said. The same increase will apply to electricity transmission through power lines and heat generation. In what further undermines the industry's expected profits, the new rate will not come into effect until half of the year is over.

The move sharply contrasts with the government's previous promises of greater revenues for the sector. Foreign investors, such as Italy's Enel, purchased stakes in electricity-generating companies from the state, committing to enormous upgrade and expansion plans. Although many industrial consumers pay liberalized prices, the government still regulates the rates for household users and sales of electricity on the capacity market — which, combined, generate more than half of the income of power companies.

In what will mitigate the effect of harsh tariff control for electricity producers, the price for natural gas — their key fuel — will also stay unchanged until July 1. But then, according to Putin's decision, Gazprom and other suppliers will be able to charge 15 percent more.

The government significantly raised the gas extraction tax for Gazprom as of next year, Shuvalov pointed out Monday. That means Gazprom will not see additional profit from the rate hike, he said.

Natalya Novikova, a Citibank economist in Moscow, conceded that keeping the rates down would reduce inflation. Still, the measure is not enough to allow the bank to forecast greater economic expansion next year, she said.

Novikova, who also described the decision about tariffs as elections-related, said the government could revisit the matter after the vote.

Aton's Westin said the government's plan would most harshly affect electricity-generating companies, which are in "dire" need of investment. A better policy to boost economic growth would be to reduce budget expenditures, he said, admitting that approaching elections make spending cuts challenging.

"Price controls never work," he said. "All you do is just postpone the problem."

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