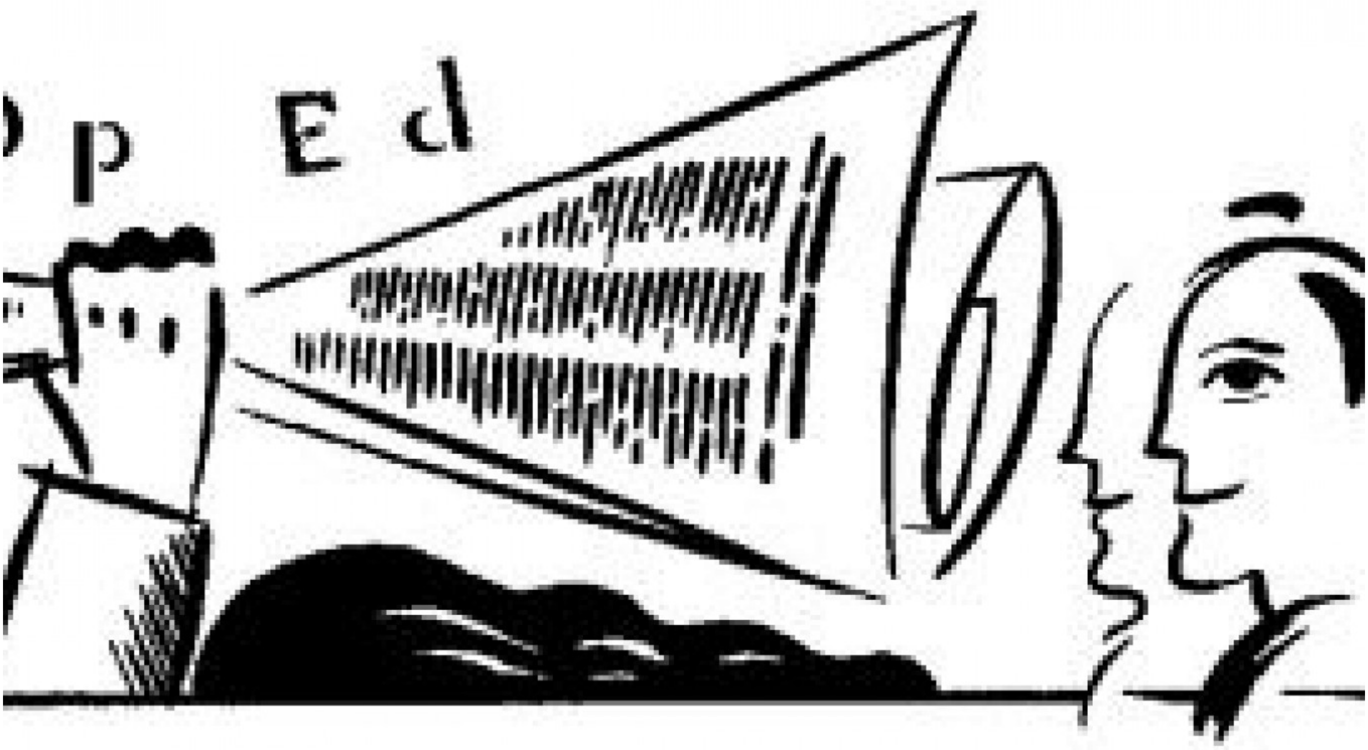
The Moscow Times
30 YEARS
INDEPENDENT NEWS FROM RUSSIA

Tight Autocracies and Disorderly Democracies

By Maria Snegovaya

October 17, 2013



The International Monetary Fund and the World Bank found themselves in an eerie ambience when they met in Washington last week. Along with a mass shooting at a military facility, a fatal car chase after a woman attempted to ram the gates of the White House and a self-immolating man on the National Mall, the economic situation did not leave many reasons for optimism. Surprisingly, developed economies have been slowly recovering, but emerging markets like Russia and Brazil — traditional growth engines — have continued to slow down, with their growth estimates decreasing to 4.5 percent in 2013 and 5.1 percent in 2014 .

For the last four years, quantitative easing, combined with Western deleveraging, provided investors with abundant and cheap cash to invest in higher-yield developing economies. But the proliferation of investments in emerging markets, regardless of their political system, will end with the U.S. Federal Reserve's policy changes, which will bring back competition from developed markets, create large current account deficits and highlight structural problems in developing economies.

This fortune reversal is not the only fallout from the global slowdown. The international financial crisis of 2008-09 incentivized governments to use increasingly interventionist policies to stabilize domestic economies. The past few years have seen political choices create different economic outcomes in countries like Russia and Brazil. Economically similar but politically very different — in 2013 Brazil scored "free", Russia scored "not free" on the Freedom in the World ranking — the two countries' policy choices are strikingly illustrative of different outcomes.

Brazil and Russia are both among the largest countries in the world, are similar in terms of population, gross domestic product and the substantive growth rates in the last decade that followed long periods of economic stagnation. Both countries recently benefited from high commodity prices, improved trade balances and growing foreign direct investment. Both have similarly poor infrastructure, abundant corruption and are close to each other in the World Bank Doing Business rankings. In its recent report, the IMF cut Russia's 2013 growth forecast by almost half, from 2.5 percent to 1.5 percent, while the IMF kept Brazil's 2013 growth estimates at its July prediction of 2.5 percent, a number which is expected to be repeated next year.

So far, Brazil's recovery from the slowdown has been much more successful than Russia's, in part due to the much better quality of its institutions. In addition, the slowdowns were not synchronized: Brazil's downturn happened much earlier and its economy slowed to less than 1 percent growth in 2012, while Russia only started its slowdown in the middle of 2012, so its cycle has been occurring on a delay.

While Brazilian President Dilma Rousseff is preparing for an upcoming re-election bid in 2014 her country's economic advantage may disappear. Although Rousseff's electoral favorability is almost unquestionable at this point, her prospects were less obvious last summer when the country was shaken by a series of mass protests in response to the overall economic slowdown. In a situation of public unrest, democratic governments are unlikely to enact "hurtful" policies that take people's money or benefits away. But, at the same time, tightening liquidity urges the Brazilian government to signal the country's credibility to investors at a time of increased competition. A mixture of both factors is unlikely to result in a sustainable Brazilian economic policy in the future.

Rousseff's endeavor to kill both birds — public opinion and investors — with however many stones it takes is reflected in current policy switches. Her government's decision to decrease funding to federal state-owned banks revealed an attempt to please investors and ratings agencies ahead of the election. But, simultaneously, the government passed a range of infrastructure projects requiring increased federal funding, indicating that fiscal policy improvements will be largely incremental.

Trying to buy popular support, Rousseff has passed a 2014 budget with overly optimistic tax collection estimates and a more than 10 percent expansion in public expenditures. This budget, however, will be hard to sell to much-needed investors who are interested in more orthodox economic policy amid rising inflation. Populist electoral considerations seem to be trumping fiscal responsibility in the run up to the 2014 elections.

The policy uncertainty stemming from Brazil's democratic system contrasts with the political advantages of Russia's authoritarianism. A government that is less driven by electoral populism can avoid excessive public spending and fiscal irresponsibility, allowing it to shrink some of its spending during economic downturns more easily. On the surface these uncontested policy moves seem ideal. While central banks worldwide have been using novel approaches to monetary policy, Russia has been remarkable for its devotion to a more orthodox stance focused on sustainable monetary politics and fixed interest rates. Although Russia expanded expenditures during the 2012 elections by 6 percent of GDP in the first quarter, that temporary stimulus was reversed in the second and third quarters, contrasting with Brazil, which is unlikely to let go of its increased spending tendencies. Moreover, during the slowdown, Russia has been the only BRICS country to decrease federal government spending, going from 20.78 percent to 18.6 percent of GDP between 2009 and 2012. Government devotion to fiscal conservatism has been even more striking in the 2014 budget, with a simultaneous decrease in education, healthcare and social policy spending in addition to the recent pension system overhaul that took place despite a growth slowdown and growing public unrest.

However, instead of praising the Kremlin for economic conservatism, observers should consider other areas of Russia's budget and how they contrast with the alternatives taken by a fellow BRIC like Brazil. Rather than increasing public expenses in the face of popular unrest, authoritarian Russia, already 3rd in the world in 2013 defense spending, has been steadily enhancing its defense expenditures since 2011, planning a 18.4 percent increase for 2014. The defense and security spending's share in total government expenditure will increase from 15.6 percent in 2013 to about 20.6 percent in 2016. Brazil, with defense spending constituting a quarter of Russia's $116 billion in 2013, shrank its military expenditures in favor of measures to reduce inflation.

Contrary to Rousseff's attempts to secure support by investing in public expenditure, Putin's government, faced with increasing popular unrest across the country, is ensuring its own military buttress. While suppressing unrest may work in the short-term, longer-term demands for real economic reforms will eventually butt up against the government's desire to preserve its own entrenched interests. The Brazilian approach is arguably preferable for any developing society. By using social spending to preserve power and paying attention to a democratic structure rather than focusing on securing an autocratic one, governments like Brazil's end up being more sustainable and will be able to adapt to society's needs with public support. Perhaps only a political regime change will give Russia a real chance to reform.

Maria Snegovaya is a researcher at the National Research University-Higher School of Economics and a PhD student at Columbia University.

Original url:
https://www.themoscowtimes.com/2013/10/17/tight-autocracies-and-disorderly-democracies-a28718