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The review provides a detailed analysis of main trends in Russia's economy in 2015. The paper contains 6 big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and credit spheres; financial sphere; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts.

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## Russia's State Budget in 2015<sup>1</sup>

### 2.2.1. Basic parameters of Russia's budget system

The basic parameters of budget execution at various levels are shown in *Table 6*. In 2015, the general government increased their budget revenues in absolute terms by Rb 123bn from 2014, however the revenues dropped by 0.9 percentage points of GDP and by 13% in real terms (including CPI). The general government increased their budget expenditure both in nominal terms and as a percentage of GDP by 1.5 percentage points of GDP, whereas expenditure in real terms were cut by 7% over values seen in 2014. As a result, the general government ran their budget with a deficit of 3.5% of GDP (the 2014 budget deficit was 1.1% of GDP). Note that the 2015 deficit was many times the value recorded in 2013–2014, both in absolute terms and as a percentage of GDP, whereas a surplus was recorded in 2011–2012. Thus, in 2015 Russia's budget system saw its balance deteriorate seriously over values seen in 2011–2014.

In 2015, the federal budget revenues fell by Rb 841bn in nominal terms, by 1.6 percentage points of GDP from 2014, and by 18% a in real terms. The federal budget expenditure increased by 0.4 percentage points of GDP, whereas they were cut by 9% in real terms. The 2015 federal budget ran a deficit 2.4% of GDP, by 2.0 percentage points of GDP above values seen in 2014. Note that while according to the originally approved parameters the 2015 federal budget was projected to run a deficit of 0.6% of GDP,<sup>2</sup> the April update expected deficit to reach 3.7% of GDP.

Table 6

### State budget revenue and expenditure in 2011–2015

	2011		2012		2013		2014		2015		Deviation as percentage points of GDP, 2015 or 2014
	rubles in bil-lions	as % of GDP	rubles in bil-lions	as % of GDP	rubles in bil-lions	as % of GDP	rubles in bil-lions	as % of GDP	rubles in bil-lions	as % of GDP	
<b>Federal budget</b>											
Revenues	11366	19.0	12854	19.2	13020	18.3	14497	18.6	13656	17.0	-1.6
Expenditure	10935	18.3	12891	19.3	13343	18.8	14831	19.0	15611	19.4	+0.4
Deficit (-) / Sur-plus (+)	431	0.7	-37	-0.1	-323	-0.5	-334	-0.4	-1955	-2.4	+2.0
<b>Consolidated budgets of subjects of the Russian Federation</b>											

<sup>1</sup> Authors of this section: Belev S. – RANEP, Mamedov A. – Gaidar Institute for Economic Policy, Fomina E. – Gaidar Institute for Economic Policy.

<sup>2</sup> Federal Law “On the Federal Budget for 2015 and the Planning Period of 2016 and 2017” No. 384-FZ dated December 1, 2014. See versions dated April 20, 2015; July 13, 2015; November 28, 2015).

Revenues	7644	12.8	8064	12.0	8165	11.5	8906	11.4	9308	11.6	+0.1
Including inter-budgetary transfers	1644	2.8	1680	2.5	1577	2.2	1728	2.2	1617	2.0	-0.2
Expenditure	7679	12.9	8343	12.5	8807	12.4	9353	12.0	9480	11.8	-0.2
Deficit (-) / Surplus (+)	-35	-0.1	-279	-0.4	-642	-0.9	-447	-0.6	-172	-0.2	-0.4
<b>General government budget</b>											
Revenues	20853	34.9	23089	34.5	24082	33.9	26371	33.9	26494	32.9	-0.9
Expenditure	20005	33.5	22826	34.1	24931	35.1	27216	34.9	29308	36.5	+1.5
Deficit (-) / Surplus (+)	848	1.4	263	0.4	-849	-1.2	-845	-1.1	-2814	-3.5	+2.4
<i>For reference: GDP, rubles in billions</i>	59698		66927		71055		77893		80413		-

Sources: Rosstat, Russia's Ministry of Finance, Gaidar Institute's own calculations.

Consolidated budgets of subjects of the Russian Federation saw less serious changes in 2015. Consolidated budget revenues of subjects of the Russian Federation increased by 0.1 percentage points of GDP. Consolidated budget expenditure of subjects of the Russian Federation stood at 11.8% of GDP, by 0.2 percentage points of GDP below values seen in 2014. Consolidated budget deficit of subjects of the Russian Federation in 2015 decreased by 0.4 percentage points of GDP to -0.2% of GDP.<sup>1</sup>

Overall, the general government's budget structure that prevailed in 2015 was characterized by high sensitivity of the Russian budget system to trends in the global energy market, that in 2015 were driven by sharp plunge in prices. Prices of crude oil and of natural gas that started to go down in the mid-2014 continued to fall in 2015. For instance, in 2015, the Urals crude price averaged not higher than \$51 a barrel compared to \$97.6 in 2014.

With shrinking resource base of Russia's budget system, the Reserve Fund at the federal level and debt-based fundraising at regional and municipal levels were important sources of financing of public and municipal expenditure. The dynamics of debt owed by budgets at various levels is shown in *Table 7*.

*Table 7*

**Volume of public debt in 2011–2015 by budget system level,  
as % of GDP**

	2011	2012		2013		2014		2015	
	value	value	growth	value	growth	value	growth	value	growth
<b>Federal level</b>									
<b>Russia's internal debt</b>	7.0	7.4	0.4	8.1	0.6	9.3	1.2	9.1	-0.2
<i>excluding state guarantees</i>	6.0	6.1	0.1	6.2	0.2	7.0	0.8	6.9	-0.1
<b>Russia's external debt</b>	1.9	2.3	0.4	2.6	0.3	3.9	1.4	4.5	0.6
<i>excluding state guarantees</i>	1.9	1.8	-0.1	2.0	0.3	3.1	1.0	3.5	0.4
<b>Total, rubles in billions</b>	9.0	9.7	0.8	10.6	0.9	13.2	2.6	13.6	0.4
<i>excluding state guarantees</i>	7.8	7.9	0.0	8.3	0.4	10.1	1.8	10.4	0.3
<b>Subnational level</b>									
<b>Debt owed by subjects of the Russian Federation</b>	2.0	2.0	0.1	2.4	0.4	2.7	0.2	2.9	0.2
<i>excluding state guarantees</i>	1.8	1.9	0.1	2.3	0.4	2.5	0.3	2.8	0.2

<sup>1</sup> Refer to the respective section for details on budgets of regions.

<b>Debt owed by municipalities</b>	0.4	0.4	0.01	0.4	0.04	0.4	0.00	0.4	0.02
<i>excluding state guarantees</i>	0.3	0.3	0.01	0.4	0.04	0.4	0.00	0.4	0.03

As of January 1, 2016, the Russian Federation owed Rb 10954bn (13.6% of GDP) in sovereign debt, including Rb 7308bn in public internal debt (9.1% of GDP) and \$50002m in public external debt (4.5% of GDP). The total volume of debt in 2015 stood at 0.4 percentage points of GDP (excluding state guarantees, the growth was 0.3 percentage points of GDP). The public external debt saw a more notable increase of 0.6 percentage points of GDP (excluding state guarantees, the increase was 0.4 percentage points of GDP) amid inconsiderable decline in public internal debt (excluding state guarantees, the decline was 0.2 percentage points of GDP and 0.1 percentage points of GDP). As a result, the structure of public debt in 2015 changed due to shrinkage of the share of public internal debt to 66% (from 70–78% in 2011–2014). The volume of public external debt in ruble terms increased as a percentage of GDP mainly due to depreciation of the Russian ruble, whereas it was lower in foreign currency terms than that seen in 2014. In 2015, the volume of ruble state guarantees dropped both in nominal terms (by Rb 30bn) and as a percentage of GDP (by 0.1 percentage points of GDP). This suggests that state guarantees at the federal level were not used for supporting Russian enterprises amid recession.

At the subnational level, in 2015, subjects of the Russian Federation saw their debts increase by 0.2 percentage points of GDP (excluding state guarantees, the debts saw equal changes in value). At the same time, debts at the municipal level increased by 0.02 percentage points of GDP (excluding state guarantees, the growth was 0.03 percentage points of GDP). The data show that state guarantees at the subfederal level were not used actively, too.

Overall, the volume of both federal and subfederal debts is at safe level, posing no threat to macroeconomic stability. As to the regional level, however, the situation differs largely from one region to another.

### 2.2.2. New tax revenues in Russia's budget system

2015 was the first year after the crisis of 2009, when revenues from all the main taxes dropped in real terms. For instance, tax revenues to Russia's budget system dropped in general by 13.6%, and the tax burden as a percentage of GDP was eased by 1.8 percentage points to 29.8% of GDP (see *Table 8*). As a result, the level of public withholdings in 2015 turned out to be lower than 30.8% of GDP during the crisis of 2009. Analysis of the basic components of tax revenues as a percentage of GDP shows mixed dynamics: revenues from some taxes declined at slower pace than GDP.

*Table 8*

#### **Revenues from main taxes in the budget of general government of the Russian Federation in 2008–2015, as % of GDP**

	2008	2009	2010	2011	2012	2013	2014	2015	Percent change 2015 from 2014	
									as percentage points of GDP	in real terms, %
<b>Tax burden level</b>	35.7	30.8	31.1	34.9	34.6	34.3	31.6	29.8	-1.8	-13.6
Profit tax	6.1	3.3	3.8	4.1	3.8	3.1	3.0	3.2	0.2	-3.1
personal income tax	4	4.3	3.9	3.6	3.7	3.8	3.5	3.5	0.0	-7.9

UST/insurance contributions*	5.1	5.5	4.9	6.3	6.3	6.7	6.1	6.6	0.5	-0.4
VAT	5.1	5.3	5.4	5.8	5.7	5.3	5.1	5.3	0.2	-4.8
Excise duties	0.8	0.9	1.0	1.2	1.4	1.5	1.4	1.3	-0.1	-11.7
the mineral extraction tax	4.1	2.7	3.0	3.7	4.0	3.9	3.7	4.0	0.3	-1.6
Customs duties and charges	8.6	6.8	6.8	8.3	8.0	7.6	7.0	4.1	-2.9	-46.4

\* in 2010, the unified social tax (UST) was transformed into insurance contributions charged directly to offbudget funds.

Sources: Russia's Federal Treasury, Rosstat, Gaidar Institute's own calculations.

Drastic decline in the volume of customs duties and charges (by 2.9 percentage points of GDP or by 46.4% in real terms from 2014) contributed most to the decline in general government's budget revenues. In addition to customs duties, only excise duties dropped as a percentage of GDP by 0.1 percentage points of GDP or by 11.7% in real terms. Insurance contributions were ranked first in terms of upward dynamics (an increase of 0.5 percentage points of GDP and a decrease of 0.4% in real terms), followed by the mineral extraction tax (grew up by 0.3 percentage points of GDP and went down by 1.6% in real terms), profit tax (went up by 0.2 percentage points of GDP and slid by 3.1% in real terms), VAT (an increase of 0.2 percentage points of GDP and a decline of 4.8% in real terms), the personal income tax (remained at the level seen in 2014 as a percentage of GDP and dropped by 7.9% in real terms).

The structure of tax budget revenues of the general government is shown in *Fig. 18*. Two aspects are worth noting here. First, insurance contributions became the basic tax withholdings in economy. Second, in 2014 customs duties and charges moved down to third place, giving way to not only insurance contributions but also VAT.

As *Fig. 19* suggests, revenues from the personal income tax and GDP changed at nearly similar pace, so the volume of revenues as a percentage of GDP remained at the level seen in 2014. Given that real personal income continued to fall in 2015 (although cash income increased as a percentage of GDP), regions are expected to face problems while fulfilling their budget commitments in 2016, because their own tax base – with the personal income tax being ranked first – may shrink.

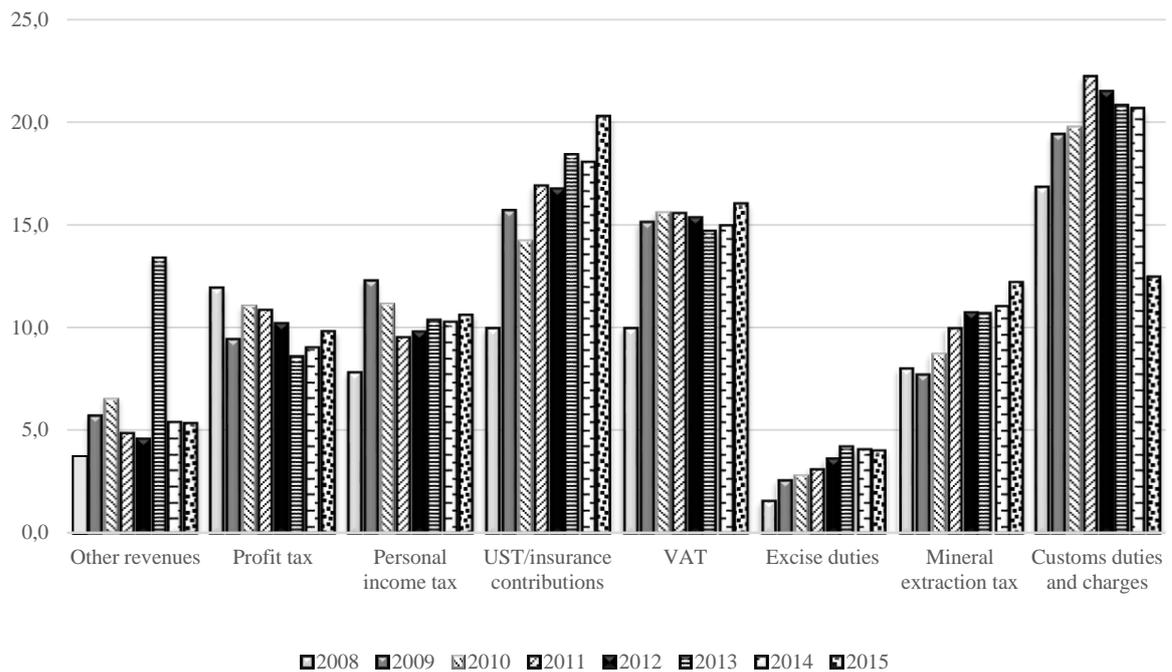


Fig. 18. Share of tax revenues of general government's total budget revenues in 2008–2015, %

Source: Russia's Federal Treasury.

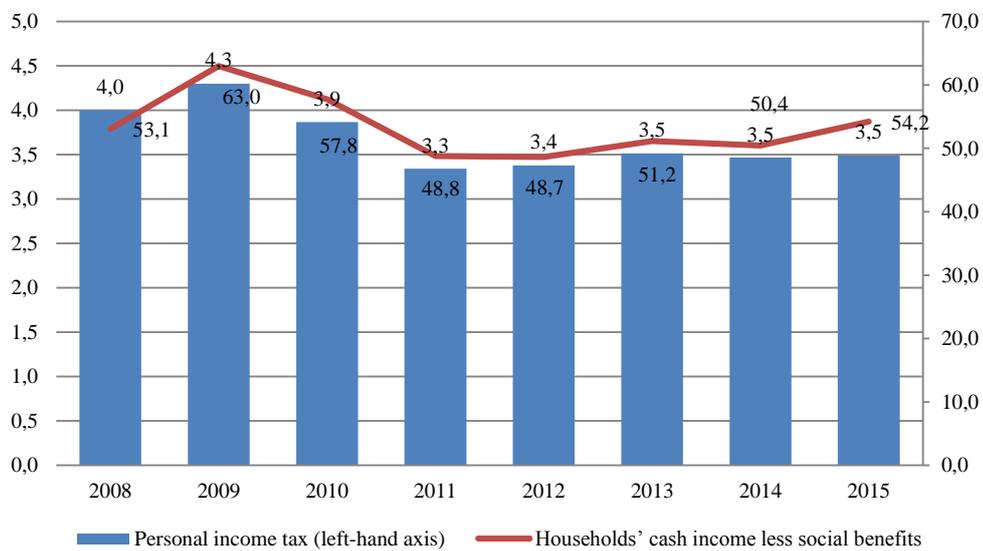


Fig. 19. Comparison between dynamics of personal income tax and dynamics of households' cash income less social benefits in 2008–2015, as % of GDP

Sources: Russia's Federal Tax Service, Rosstat.

2015 saw revenues from profit tax decline in real terms and increase slightly as a percentage of GDP (by 0.2 percentage points). At the same time, the balanced financial result of organizations of all the industries as a percentage of GDP increased more notably from 7.1% to 10.5% of GDP (see Fig. 20) in part due to depreciation of the ruble that helped Russian exporting enterprises to enhance competitiveness against foreign manufacturers by partially offsetting the effect of falling aggregate demand, as well as to generate “extra” revenues for such enterprises. At the same time, the share of loss-making organizations of Russia’s economy remained at the level seen in 2014 (28.1%). Overall, the relatively favorable dynamics of the profit tax in 2015 is rather temporal, and it may deteriorate as early as 2016, affecting first of all budget revenues in regions.

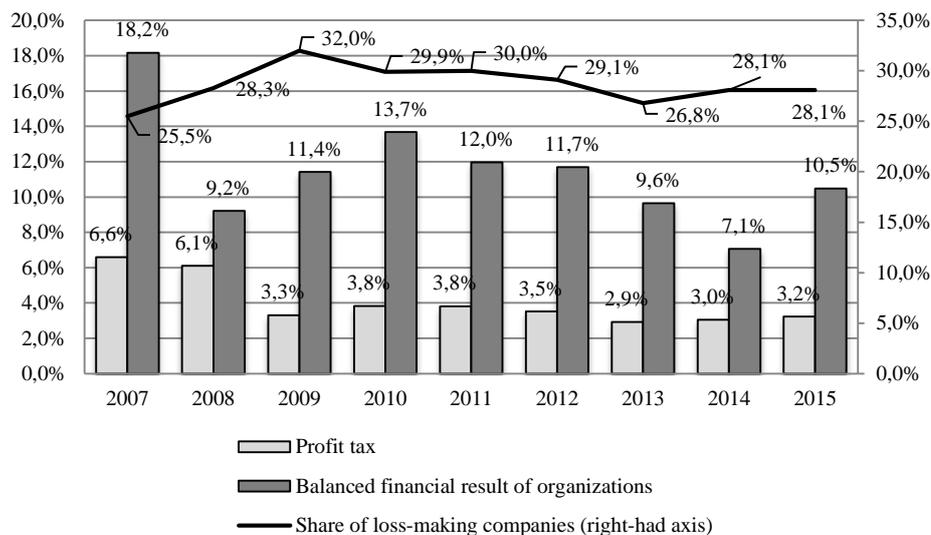


Fig. 20. Dynamics of profit tax revenues in Russia’s state budget, balanced financial result of organizations and share of loss-making companies in 2007–2015, as % of GDP

\* based on Rosstat’s preliminary estimates.

Sources: Russia’s Federal Tax Service, Rosstat.

The decline of global crude oil prices in 2015 had a strong adverse effect on federal budget revenues from oil and gas (more than \$40 a barrel of Urals crude oil at prices for tax purposes). In 2015, oil and gas budget revenues plunged below the level seen in 2009 (7.4% of GDP in 2015 compared with 7.9% in 2009) (see Table 9). The ruble’s devaluation failed to offset the decline in crude oil prices.

Revenues from the mineral extraction tax increased by 0.3 percentage points of GDP, and the dynamics of the second component, that is, export duties on energy-carrying materials (3.4% of GDP in 2015 against 6.5% in 2014) contributed most to pushing down oil and gas revenues as a percentage of GDP. At the same time, revenues from customs duties on natural gas were driven by more favorable dynamics than those on crude oil and refined petroleum products (see Table 10). The difference in dynamics of the oil extraction tax (inconsiderable growth) and customs duties on crude oil and refined petroleum products (sharp plunge), as well as more favorable dynamics of customs duties on gas, are determined first of all by the commencement of a so-called ‘tax maneuver’ in the oil sector in 2015. As part of this oil sector taxation reform, the basic rate of oil extraction tax was lifted from 493 to 766 rubles per ton,

whereas the marginal rate (coefficient in equation) of customs export duties on crude oil was cut from 59% to 42%.

Table 9

**Volume of oil and gas revenues and mineral extraction tax  
in 2008–2015**

	2008	2009	2010	2011	2012	2013	2014	2015
Oil and gas revenues, as % of GDP	10.9	7.9	8.4	10.3	10.6	10.0	10.2	7.4
the mineral extraction tax, as % of GDP	4.1	2.7	3.0	3.7	4.0	3.9	3.7	4.0
Crude oil extraction, including gas condensates, tones in millions	488	494	506	512	519	522	525	534
Urals crude average annual price, USD a barrel	90.7	60.7	76.2	109.6	110.6	108.0	97.6	51.0
Central bank's average annual RUB/USD exchange rate, rubles per dollar	24.78	31.90	30.37	29.31	31.05	31.20	38.63	60.98

Sources: Rosstat; Russia's Central Bank; Federal Customs Service, Federal Tax Service; Gaidar Institute's own calculations.

Table 10

**Revenues from customs duties in 2008–2015,  
as % of GDP**

	2008	2009	2010	2011	2012	2013	2014	2015
Export duties on energy-carrying materials	6.8	5.2	5.3	6.6	6.6	6.1	6.5	3.4
- on crude oil	4.3	3.1	3.6	4.2	4.0	3.5	3.7	1.8
- on natural gas	1.2	1.1	0.4	0.7	0.7	0.7	0.7	0.7
- on petroleum derivatives	1.3	1.0	1.3	1.7	1.8	1.8	2.1	0.9
Customs duties and charges	8.6	6.8	7	8.4	8.0	7.6	7.0	4.1

Sources: Rosstat; Russia's Federal Treasury; Gaidar Institute's own calculations.

In 2015, VAT on goods sold on the territory of the Russian Federation ("internal VAT") rose slightly as a percentage of GDP (by 0.2 percentage points), whereas VAT on goods imported in the territory of the Russian Federation remained the level seen in 2014 (see *Table 11*). Russia continues to have better tax collection rate of VAT on imported goods over that on goods manufactured in Russia, as well as a downtrend of the VAT effective rate on imported goods.

In 2015, like in 2014, revenues from excise duties went down as a percentage of GDP. As *Fig. 21* suggests, excise duties on tobacco products turned out to be the sole excisable products on which charges increased as a percentage of GDP. At the same time, excise duties on tobacco products were for the first time ranked first in volume of revenues (0.47% of GDP in 2015). A policy of higher-than-inflation indexation of rates resulted in a decline of revenues from excise duties on alcoholic products (from 0.39% in 2014 to 0.34% of GDP in 2015). Revenues from excise duties on refined petroleum products dropped from 0.47 to 0.44% of GDP, too. Revenues from excise duties on sales of motor vehicles and motorcycles continued to make up an inconsiderable share of revenues.

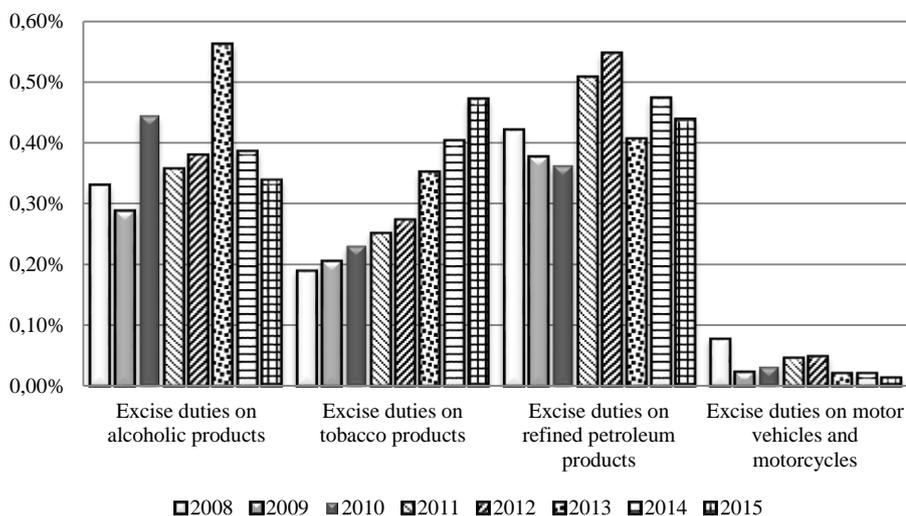
Table 11

**Dynamics of imports and VAT revenues in Russia's budget system  
in 2008–2015, as % of GDP**

	2008	2009	2010	2011	2012	2013	2014	2015
VAT revenues	5.2	5.3	5.4	5.8	5.7	5.0	5.1	5.3
VAT on goods sold on the territory of the Russian Federation	2.4	3.0	2.9	3.1	3.0	2.6	2.8	3.0
VAT on goods imported in the territory of the Russian Federation	2.8	2.3	2.5	2.7	2.7	2.4	2.3	2.3
VAT effective rate <sup>1</sup> , %	8.4	7.6	8.2	9.3	8.3	7.4	7.0	7.2
VAT effective rate on goods sold on the territory of the Russian Federation <sup>2</sup>	5.4	5.5	5.8	6.9	6.4	5.7	5.5	5.8
VAT effective rate on goods imported in the territory of the Russian Federation <sup>3</sup>	12.5	11.0	11.9	12.3	12.1	11.1	10.7	10.4
Imports*	22.1	20.5	21.1	21.9	22.4	21.1	20.9	21.3

\*Share of imports of GDP was measured as the ratio of imports values based on Rosstat's data and GDP.

Sources: Rosstat; Russia's Ministry of Finance; Gaidar Institute's own calculations.



*Fig. 21. 2008–2015 revenues from excise duties by group of excisable goods, as % of GDP*

Source: Russia's Federal Treasury.

Note that efforts to turn excise duties into a source of budget revenues are exposed to serious risks that elasticity of demand for respective goods might happen to be so high as to lead eventually to decline in charges. *Table 12* shows that consumption of all types of alcoholic and tobacco products continued to decline in 2015. Thus, alcoholic products faced the risk in practice.

*Table 12*

<sup>1</sup> The ratio of VAT revenues to final consumption.

<sup>2</sup> The ratio of revenues from VAT on goods sold on the territory of the Russian Federation to final consumption less the value of imports.

<sup>3</sup> The ratio of revenues from VAT on goods imported in the territory of the Russian Federation to the value of imports.

**Volume of alcoholic and tobacco products consumed in Russia  
in 2008–2015,  
dL in millions**

Product	2008	2009	2010	2011	2012	2013	2014	2015
Alcoholic products								
vodka and liqueurs and spirits	177.2	166.1	157.8	156.4	153.0	133.6	112.4	104.9
Vine products (except champagne and sparkling vines)*	102.9	102.5	103.4	97.1	93.6	83.6	90.4	89.6
low-alcohol beverages (with ethanol content of 9% or less)	–	–	31.9	31.4	26.9	23.3	17.8	13.8
cognac, brandy spirits (including brandy, calvados)	10.8	10.6	11.1	11.6	12.4	12.1	11.5	11.0
Champagne and sparkling vines	26.0	25.5	27.3	28.5	28.3	27.7	26.4	24.6
Beer	1138.2	1024.7	1004.0	1011.5	1017.5	984.2	895.9	868.1
Cigarettes, pieces in billions	393.6	398.7	371.8	358.0	355.7	359.1	338.6	326.7

\*Until 2012, ‘Grape and Fruit Vines’.

Source: Rosstat.

Overall, 2015 turned out to be an extremely off year for state budget revenues: all types of tax revenues dropped in real terms. Oil and gas revenues of the federal budget were hit the hardest amid drastic slump of global crude oil prices, whereas budget revenues in regions saw “extra” profit tax revenues due to devaluation of the Russian ruble. However, one should realize that this effect covered a limited number of subjects of the Russian Federation, whose economy relies on export-oriented industries such as oil and gas sector, metallurgy etc.

### 2.2.3 Characteristics of Russia’s budget system

With a decline of 0.9 percentage points of GDP in budget revenues of the general government in 2015, the volume of the country’s budget system saw a reverse dynamics, that is, a growth of 1.6 percentage points of GDP (see *Table 13*).

*Table 13*

#### General government budget expenditure in 2011–2015, as % of GDP

	2011	2012	2013	2014	2015	Change 2015 from 2014, percentage points of GDP
Expenditure, total	35.5	34.1	35.1	34.9	36.5	1.6
General National Issues	2.8	2.7	2.8	2.8	3.1	0.3
Public and Municipal Debt Service	0.6	0.6	0.6	0.7	0.8	0.1
National Defense	2.5	2.7	3.0	3.2	4.0	0.8
National Security and Law Enforcement	2.5	2.9	3.0	2.8	2.6	-0.2
National Economy	4.7	4.9	4.6	5.8	4.7	-1.1
Housing and Utilities	2.0	1.6	1.5	1.3	1.2	-0.1
Environmental Protection	0.06	0.06	0.07	0.09	0.09	0
Education	3.7	3.8	4.0	3.9	3.8	-0.1
Culture, Cinematography and Means of Mass Media	0.7	0.7	0.8	0.7	0.7	0.0
Healthcare and Sports	3.5	3.7	3.6	3.6	3.9	0.3
Social Policy	10.9	11.0	11.8	10.8	12.5	1.7

Sources: Russia’s Federal Treasury, Rosstat; Gaidar Institute’s own calculations.

In 2015, the general government saw serious changes in their budget expenditure: values of financing of various types of expenditure in 2015 varied from 2014 within a range of 0.1 and 1.7 percentage points of GDP.

The biggest expenditure were recorded for ‘Social Policy’ (an increase of 1.7 percentage points of GDP and of 3.5% in real terms). At the same time, expenditure for social policy increased mainly for ‘Pension Provision’ and ‘Other Matters Related to National Policy’. As a result, expenditure for ‘Pension Provision’ remained at the level seen in 2014 (declined by 1.1% in real terms). However, indexation of pensions in 2015, namely the insurance part of labor pension by 11.4% (from February 1, 2015) and social pensions by 10.3% (since April 1, 2015), was not followed by higher pension payments: the actual inflation rate (12.9%) was above indexation rates. Additionally, in 2015 pension accruals were transferred to nongovernment pension funds at 2013 year-end (the transfer was “frozen” in 2014 simultaneously with “freezing” the transfer of new contributions of the then current year of 2014 to the funded pension component), which explains the growth of expenditure for ‘Other Matters Related to National Policy’.

The uptrend since 2011 towards expenditure for ‘National Defense’ continued in 2015, an increase by 0.8 percentage points of GDP. Military spending in real terms reached 11% (total expenditure were cut by 7%). The increase in government spending for this line item is first of all associated with further implementation of measures as part of the State Armament Program for 2011–2020.

Additionally, expenditure for ‘General National Issues’ and ‘Healthcare and Sports’ increased slightly each by 0.3 percentage points of GDP, however a minor decrease within 1% was reported in real terms for each of the line items. A detailed analysis of expenditure for healthcare shows a decline in expenditure for ‘Inpatient Medical Assistance’ and ‘Outpatient Medical Assistance’. At the same time, expenditure for ‘Other Healthcare Matters’ increased notably in real terms by about 8%. The growth in expenditure for ‘Other Healthcare Matters’ was possibly determined by increased funding of, above all, certain measures implemented as part of the Healthcare Development Program financed under this line item. As a result, a redistribution of funds between financing the expenditure for inpatient and outpatient medical assistance was performed in favor of financing the Healthcare Development Program.

In 2015, government spending for ‘National Economy’ were cut considerably by 1.1 percentage points of GDP (nearly 4.7% of GDP). However, note that the decline below the 2014 parameters is technical and related to Rb 1 trillion in asset contribution from the federal budget to the Deposit Insurance Agency (DIA), that took place late in 2014.<sup>1</sup> The appropriation was envisaged as part of state support for the banking sector. Excluding the contribution, the expenditure for the national economy in 2014 would make up less than 4.5% of GDP. Overall, the level of financing measures of support for the national economy in 2015 is comparable with that in 2011–2013 (4.6–4.9% of GDP). Extra spending for support of the banking sector via the DIA can be actually attributed to both 2014 (when the foregoing operation was performed) and to 2015 (when the DIA could have spent the funds). Thus, with mounting crisis developments in the economy, government expenditure for the national economy increased in 2014–2015 as part of spending on anti-crisis measures.

In 2015, national defense expenditure continued to decline to 2.6% of GDP, by 0.2 percentage points of GDP below the level seen in 2014, and they were cut in nominal terms, too. The rest of the budget expenditure line items saw no notable changes in 2015 (within 0.1 percentage points of GDP).

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<sup>1</sup> In December 2014, these funds were transferred using federal government bonds (OFZ) and were allocated to increase banks’ capital. The DIA was entitled to use the contribution to increase the capital of systemically important banks whose capital is worth not less than Rb 100bn.

In general, note that in 2015 the prevailing upward dynamics of the general government's budget and the resource base shrinkage contradict in a way the policy aimed at spending less budget funds in order to prevent the risk of "inflation spiral" and of higher than normal deficit in the budget system. Also, what raises concern is the decrease in real terms of "productive" expenditure for education and healthcare amid growing "nonproductive" expenditure for defense and social policy. It is important to realize that the decline in expenditure for human capital may worsen the problem of Russia's economy entering a new growth path in the mid- and long term perspective.

#### 2.2.4. Basic parameters of the 2015 federal budget and outlooks for 2016

The federal budget revenues in 2015 (see *Table 14*) stood at 17.0% of GDP, a decline of 1.6 percentage points of GDP below the value seen in 2014, and the decline was driven by falling oil and gas revenues. In 2015 they were 2.4 percentage points of GDP below parameters seen in 2014. At the same time, oil and gas revenues reached nearly 9.7% of GDP, an increase by 0.8 percentage points of GDP over the value seen in 2014. The volume of federal budget expenditure increased by 0.4 percentage points of GDP to 19.4% of GDP. Overall, the 2015 federal budget ran a deficit of 2.4% of GDP, a growth of 2.0 percentage points of GDP over the value seen in 2014. Furthermore, oil and gas deficit stood at 9.7% of GDP, a decline by 0.4 percentage points of GDP over the value seen in 2014.

*Table 14*

#### Federal budget basic parameters in 2011–2016

	Actually executed				2015 executed	2016		Deviation in 2015 from 2014, per- centage points of GDP
	2011	2012	2013	2014		Federal Budget Law for 2015– 2017	Federal Budget Law for 2016*	
Revenues	19.0	19.2	18.3	18.6	17.0	19.0	17.5	-1.6
Including:								
oil and gas revenues	9.6	9.8	9.3	9.7	7.3	9.7	7.7	-2.4
oil and gas revenues	9.4	9.4	9	8.9	9.7	9.3	9.8	+0.8
Expenditure	18.3	19.3	18.8	19.0	19.4	19.6	20.5	+0.4
Including: conditionally approved	0	0	0	0	0	0.5	0	0
Deficit (–)/ surplus (+)	+0.7	-0.1	-0.5	-0.4	-2.4	-0.6	-3.0	+2.0
Oil and gas deficit	-8.9	-9.9	-9.8	-10.1	-9.7	-10.3	-10.7	-0.4
GDP, rubles in billions	59.698	66.926	71.055	77.893	80.412	83.208	78.673	-
Urals crude price, USD**	109.6	110.6	108.0	97.6	51.0	96.0	50.0	-

\* Federal Law "On the Federal Budget for 2016" No. 359-FZ dated December 14, 2015.

\*\* Average annual value.

Sources: Russia's Federal Treasury, Gaidar Institute's own calculations.

The 2015 federal budget parameters were updated due to a worsening macroeconomic situation early in 2015. The federal budget law was updated three times in 2015 (in April, July, and in November). Updates to the key macroeconomic indicators budgeted for 2015 were approved in April, whereby the crude oil price was down from \$100 to \$50 a barrel, the ruble to US dollar exchange rate was up from 37.7 to 61.5 rubles per dollar, the inflation rate was up from 5.5% to 12.2%. Given the approved updates, the forecast for revenues was downgraded by 2.4 percentage points of GDP, and the expenditure plan increased by 0.8 percentage points of GDP, with the result that budget deficit increased to 3.7% of GDP (a growth of 3.1 percentage points

of GDP). The updates in July 2015 concerned Rb 20.1bn in financing of measures to ensure sustainable economic growth and social stability. A share of the funds was allocated to support the economy in the form of deposits and grants to joint-stock companies and federal unitary enterprises; the volume of grants to strategically important organizations of the Military-Industrial Complex (MIC) increased, too. Updates to the basic macroeconomic and budget parameters (increase of GDP, growth in federal budget revenues and expenditure) took effect in November 2015.

Let's analyze in detail the ultimate parameters of federal budget execution in 2015.

Overall, tax revenues dropped considerably by 2.6 percentage points of GDP below the level seen in 2014. Analysis of the structure of tax revenues (see *Table 15*) shows that in relative terms revenues from the mineral extraction tax increased by 0.3 percentage points of GDP, revenues from VAT on goods sold on the territory of the Russian Federation were up by 0.2 percentage points of GDP, and revenues from the corporate profit tax rose by 0.1 percentage points of GDP. In 2015, the year-end revenues from customs duties plunged sharply by 2.9 percentage points of GDP. The dynamics of mineral extraction tax and customs duties was driven by two factors, namely by the decline of global crude oil prices and by the abovementioned "tax maneuver" in the oil sector. Revenues from VAT on goods imported in the territory of the Russian Federation, and from excise duties (both "import" and "internal" ones) remained at levels (expressed as a percentage of GDP) seen in 2014.

*Table 15*

**Main tax revenues of federal budget  
in 2014–2015**

	January-December 2014		January-December 2015		Change as per- centage points of GDP
	rubles in billions	% of GDP	rubles in billions	% of GDP	
<b>Tax revenues, total</b>	<b>13.366</b>	<b>17.2</b>	<b>11.886</b>	<b>14.8</b>	<b>-2.4</b>
corporate profit tax	411	0.5	491	0.6	0.1
VAT on goods sold on the territory of the Russian Federation	2.181	2.8	2.448	3	0.2
VAT on goods imported in the territory of the Russian Federation	1.750	2.2	1.785	2.2	0.0
excise duties on goods manufactured on the territory of the Russian Federation	521	0.7	528	0.7	0.0
excise duties on goods exported to the territory of the Russian Federation	72	0.1	54	0.1	0.0
mineral extraction tax	2.858	3.7	3.160	3.9	0.3
revenues from foreign economic activities (customs duties)	5.445	7.0	3.295	4.1	-2.9

*Sources:* Russia's Federal Treasury, Gaidar Institute's own calculations.

All things considered, the following can be concluded: the dynamics of tax revenues of the federal budget in 2015–2016 was determined basically by a decline in oil and gas revenues amid falling global crude oil prices, whereas main types of non-oil and gas revenues were relatively stable.

*Table 16* presents actual execution of the federal budget in 2015 in terms of functional classification of expenditure.

*Table 16*

**Federal budget expenditure in 2014–2015  
(functional classification of expenditure)**

	2014		2015		Change as percentage points of GDP
	rubles in billions	as % of GDP	rubles in billions	as % of GDP	
Expenditure total, including:	14.831	19.0	15.611	19.4	0.4
General National Issues	1.350	1.7	1.627	2.0	0.3
National Defense	2.479	3.2	3.181	4.0	0.8
National Security and Law Enforcement	2.086	2.7	1.966	2.7	-0.2
National Economy	3.063	3.9	2.324	2.9	-1.0
Housing and Utilities	120	0.2	144	0.2	0.0
Environmental Protection	46	0.1	50	0.07	0.0
Education	638	0.8	611	0.8	-0.1
Culture and Cinematography	98	0.1	90	0.1	0.0
Healthcare	536	0.7	516	0.6	0.1
Social Policy	3.452	4.4	4.265	5.3	0.9
Physical Culture and Sports	71	0.1	73	0.1	0.0
Mass Media	75	0.1	82	0.1	0.0
Public Debt Service	416	0.5	519	0.7	0.1
General Purpose Inter-Budget Transfers	816	1.0	682	0.9	-0.2

*Sources:* Russia's Finance Ministry, Gaidar Institute's own calculations.

Overall, the federal budget expenditure in 2015 were 0.4 percentage points of GDP above those in 2014. However, the inflation-adjusted expenditure in 2015 was down by 9%. Spending for 'Social Policy' increased by 0.9 percentage points GDP, for 'National Defense' by 0.8 percentage points of GDP, for 'General National Issues' by 0.3 percentage points of GDP, and for 'Public Debt Service' by 0.1 percentage points of GDP. Note that in 2015 the expenditure for the above listed line items increased not only as a percentage of GDP but also in real terms: the dynamics of growth varied between 4% and 11%.

In terms of equality in spending, note that in January-March 2015 military spending were higher than other types of expenditure. For instance, in January, allocations accounted for 21.6% of the updated quarterly expenditure worksheet for 2015, and for 49.2% as a whole in January-March. This effect was smoothed in the months that followed in 2015. The drastic growth in military spending in 2015 was driven first of all by financing of measures envisaged as part of the state defense order. The growth of 7% in social spending in real terms was driven first of all by the growth (by 13% in real terms) in the pension provision expenditure due to indexation of pensions.

The expenditure for 'National Economy' were cut the most, by 1.0 percentage points of GDP. As noted above, the wide gap in volumes of expenditure in support of the economy in 2014 and 2015 is partially "technical" and related to appropriations to the DIA for support of the banking sector. Additionally, federal budget expenditure for 'National Security and Law Enforcement' were cut by 0.2 percentage points of GDP, for 'Inter-Budget Transfers' by 0.2 percentage points of GDP and for 'Education' by 0.1 percentage points of GDP. Note that even expenditure related to investment in human capital – most "productive" government expenditure – were cut in nominal terms. In real terms, the federal budget expenditure for education and healthcare reached about 17% in 2015.

*Table 17* presents the dynamics of federal government spending budget as regards to operations in the public administration sector (economic classification of expenditure).

*Table 17*

**Federal budget expenditure in 2011–2015  
(economic classification of expenditure)**

	2011	2012	2013	2014	2015
<i>Total expenditure, rubles in billions</i>	10.935	12.891	13.343	14.832	15.611
Growth in real terms, %	-0.3	12.2	-3.0	3.1	-8.9
including:					
<i>Investment expenditure, rubles in billions</i>	1.660	1.753	1.659	1.773	2.476
Growth in real terms, %	7.5	0.5	-11.4	-0.9	20.9
Including growth in the value of shares and other types of shareholding	410	505	315	264	388
Growth in real terms, %	14.4	17.3	-41.6	-22.3	27.3
<i>Current expenses, rubles in billions</i>	9.275	11.137	11.684	13.059	13.135
Growth in real terms, %	-1.6	14.3	-1.7	3.7	-12.9

Sources: Russia's Federal Treasury; Gaidar Institute's own calculations.

The dynamics of federal budget expenditure slowed down in real terms by 8.9% in 2015 from 2014. Current expenses made up most of the structure of federal budget expenditure. The 12.9% decline in current expenses was responsible largely for the decline in total amount of expenditure. By contrast, investment expenditure increased in real terms by 21% against the 0.9% decline a year earlier. Budget investment increased considerably (about 39%) due the growth under the item 'Increase in the value of fixed assets', that was determined possibly by increase in spending related to the state defense order. It is difficult to perform quantitative assessment due to a lack of data as regards to classification of operations in the state administration sector for a few expenditure items in the Federal Treasury's reports. The volumes of budget financing for 'Growth in the value of shares and other types of shareholding' were declining steadily in nominal terms throughout the entire period of 2013–2014, possibly evidencing that charter capital contributions and purchases of shares became a less important tool of supporting enterprises. However, in 2015 this trend gave way to a 27% increase in real terms in these expenditure.

The Russian government's policy aimed at curtailing growth and cutting back gradually on the volume of government spending appears reasonable. It is unreasonable and highly risky to increase the volume of expenditure by increasing the volume of deficit. The current level of federal budget expenditure is above the level of corresponding current macroeconomic context. Government expenditure were too "fat" in the period of high crude oil prices, with further growth thereof during the crisis of 2009–2010, but then they were cut down to the pre-crisis level of 18% of GDP (the expenditure have recently been steadily above 20% of GDP).

The principal feature of the **2016 federal budget** was the need to adapt to the new context of very low oil prices of about \$30–40 a barrel, whereas the federal budget was approved on the assumption that the crude oil price is \$50 a barrel, and the budget balance is reached when the oil is traded at \$82 a barrel, as estimated by Russia's Finance Ministry.<sup>1</sup>

Given the fact that the key macroeconomic indicators are volatile and difficult to forecast, the 2016 federal budget was adopted for a single year (as was the case with the 2010 budget). However, as early as May 2015, the Russian Government considered a three-year budget plan for 2016–2018 (the Urals crude was projected at \$60–65–70 a barrel respectively).<sup>2</sup>

As early as the fall of 2015, the 2016 federal budget parameters were updated seriously from the original version approved as part of the law on the federal budget for 2015–2017. The resource base of the federal budget was reduced substantially by 1.5 percentage points of GDP (to 17.5% of GDP) below the parameters that were set originally. Federal budget revenues

<sup>1</sup> <http://www.minfin.ru/ru/#ixzz3yTTiNNKR>

<sup>2</sup> <http://government.ru/news/17821/>

dropped in response to expectations for further decline in oil and gas budget revenues to 7.7% of GDP (against 9.7% of GDP) as a result of falling crude oil prices globally. Federal budget revenues for 2016 were estimated on the assumption that the crude oil price is \$96 a barrel in the original version of the mid-term forecast and \$50 a barrel in the single year version. The approved volume of expenditure reached 20.5% of GDP, nearly 1 percentage point of GDP above the originally set targets. As a result, federal budget deficit increased to 3% of GDP against that of 0.6% of GDP in the original version. However, given that in Q1 2016 the crude oil price was way less than \$50 a barrel, it is highly likely that even the single year budget parameters will have to be updated within the fiscal year.

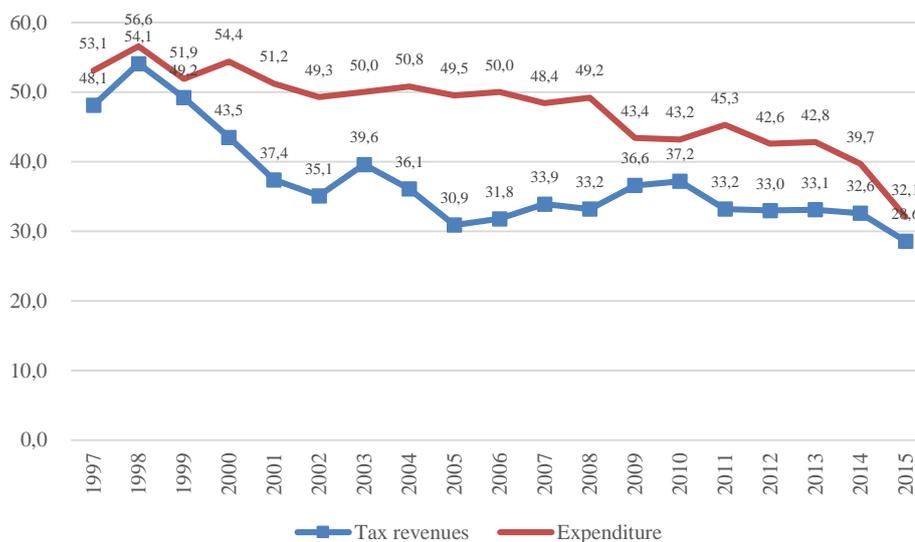
The complexity of the situation is that, on the one hand, a balance between searching for new sources of the resource base and cutting back on inefficient commitments has to be reached, and, on the other hand, the possibility of recovering Russia's economy and entering a new growth path should not be undermined. Budget deficit may double in 2016 and the Reserve Fund may be fully depleted in the absence of government's adequate measures of tactical response (for 2016) and strategic response (for 2017–2019) towards optimizing the 2016 budget expenditure, and if the current crude oil prices remain the same in the medium term,.

In terms of adjusting their expenditure commitments in 2016, the Russian government plan to cut back on the approved volumes of budget expenditure. For instance, plans to optimize federal spending may include a 10% cut-back on all the unprotected budget line items, thereby saving about Rb 500–700bn, as estimated by the Russian government. Budget holders are expected to analyze by themselves their own budgets and to decide on cutting back on inefficient spending thereof (in a volume of 10%). Officially, this is not just cutting volumes in all the expenditure items, this is cutting the inefficient component thereof. This is where the major challenge resides. Each of the federal budget expenditure contains expenditure that may be recognized as inefficient by an audit, as evidenced by audits conducted by Russia's Chamber of Accounts. However, does it suggest 10% cuts on all the expenditure?, especially on the "protected sectors" such as defense and social policy, as well as the "protected items" such as wages of public employees in every expenditure item. Further technical cuts of expenditure for educational and medical institutions may result in some institutions running short of funds and being unable to cover even their current expenses (other than wages). As a result, just mere cuts on financing are exposed to high risks if the budget institution network undergoes no reform. Therefore, while introducing new updates to budget expenditure, it is very important to avoid new "technical cuts" (although this is relatively easy to do) and to identify budget expenditure that are really inefficient. Additionally, it is significant that a variable approach is introduced into the practice of budget planning (like in New Zealand or Austria), predefining beforehand the expenditure to be cut if the macroeconomic context happens to be worse than the forecast (in the Russian practice this could be done as part of state programs, specifying "mandatory" and "supplementary" parts in each program).

## 2.3. Intergovernmental fiscal relations and subnational finance<sup>1</sup>

### 2.3.1. Analysis of principal parameters of consolidated budgets of subjects of the Russian Federation

The revenues and expenditure structure of consolidated budgets of the Russian Federation reflects main trends in relations between various levels of public administration. *Fig. 22* presents data reflecting the share of tax revenues and expenditure of subjects of the Russian Federation, that are expressed as corresponding indicators of Russia's consolidated budget.



*Fig. 22.* Share of tax revenues and of subnational budget expenditure of Russia's consolidated budget in 1997–2015

**Note:** No calculations were made for regions of the Crimean Federal Okrug.

*Sources:* Russia's Federal Treasury, Gaidar Institute's own calculations.

In 2015, the share of subnational budget expenditure of the Russian Federation consolidated budget dropped considerably from 39.7% in 2014 to 32.1% in 2015 (excluding expenditure for the Crimean Federal Okrug). The share of tax revenues shrank to a lesser extent, from 32.6% to 28.6%, during the same period. The decline in the share of subnational budget expenditure of the total volume of Russia's consolidated budget expenditure is explained largely by faster-than-normal growth of the federal budget expenditure (by 5.6% in nominal terms). The federal budget expenditure increased first of all for 'General National Issues' (by 18.6%), 'National Defense' (by 28.3%), 'Housing and Utilities' (by 20.5%), 'Social Policy' (by 23.5%), 'Municipal and Public Debt Servicing' (by 24.8%). Subnational budget expenditure increased in the period under review by 1.4% (excluding expenditure for the Crimean Federal Okrug).

Let us analyze in detail the revenue side of subnational budgets. The dynamics of principal components of consolidated budget revenues of subjects of the Russian Federation are shown in *Table 18*.

<sup>1</sup> Authors of this section: Authors of this section: Alaev A. – Gaidar Institute for Economic Policy, Mamedov A. – Gaidar Institute for Economic Policy, Fomina E. – Gaidar Institute for Economic Policy.

Table 18

**Consolidated budget revenues of subjects of the Russian Federation  
in 2008–2015**

	Volume of revenues (in nominal terms), rubles in billions								Growth in real terms, %			
	2008	2009	2010	2011	2012	2013	2014	2015	2009/ 2008	2015/ 2008	2014/ 2013	2015/ 2014
<b>Revenues, total</b>	<b>6.196</b>	<b>5.924</b>	<b>6.537</b>	<b>7.644</b>	<b>8.064</b>	<b>8.165</b>	<b>8.743</b>	<b>9.191</b>	<b>-12.1</b>	<b>-17.2</b>	<b>-3.8</b>	<b>-8.6</b>
<b>Tax and nontax revenues</b>	<b>4.912</b>	<b>4.243</b>	<b>4.980</b>	<b>5.827</b>	<b>6.385</b>	<b>6.588</b>	<b>7.141</b>	<b>7.585</b>	<b>-20.6</b>	<b>-13.8</b>	<b>-2.7</b>	<b>-6.4</b>
<i>Including tax revenues:</i>	4.384	3 792	4.520	5 273	5.800	5.967	6.461	6.890	-20.5	-12.3	-2.8	-6.0
profit tax	1.752	1.069	1.520	1.928	1.980	1.720	1.962	2.099	-43.9	-33.1	2.4	-5.2
personal income tax	1.666	1.665	1.790	1.996	2 261	2.499	2 679	2.788	-8.1	-6.6	-3.7	-7.9
Taxes on total income	161	152	179	215	272	293	314	346	-13.6	19.8	-3.8	-2.7
property taxes	493	570	628	678	785	901	955	1 067	6.1	20.7	-4.8	-1.3
excise duties	189	246	327	372	442	491	479	484	19.2	42.6	-12.4	-10.5
<b>Transfers</b>	<b>1.131</b>	<b>1.486</b>	<b>1.398</b>	<b>1.644</b>	<b>1.624</b>	<b>1.515</b>	<b>1.545</b>	<b>1.538</b>	<b>20.7</b>	<b>-24.1</b>	<b>-8.4</b>	<b>-18.5</b>
<b>Other revenues</b>	<b>153</b>	<b>195</b>	<b>159</b>	<b>173</b>	<b>56</b>	<b>62</b>	<b>57</b>	<b>68</b>	<b>17.4</b>	<b>-75.1</b>	<b>-17.4</b>	<b>4.8</b>

**Note:** No calculations were made for regions of the Crimean Federal Okrug.

*Sources:* Russia's Federal Treasury, Gaidar Institute's own calculations.

The data in *Table 18* show that in 2015 consolidated budget revenues of subjects of the Russian Federation dropped in real terms by 8.6% from the level seen in 2014. The 2015 decline in real terms in the total level of revenues was driven by a fall in retail trade turnover (a 10% decline below the level seen in 2014), in the volume of fixed investment (-8.4%), that is, an economic slowdown that was reflected in the 3.7% fall of GDP. Furthermore, inflation rate reached 12.9% in 2015, the highest since 2003, which affected inevitably the dynamics of fiscal indicators in real terms.

The above listed adverse factors dragged down in real terms all the principal sources of revenues of subnational budgets. The personal income tax fell the deepest among major types of taxes, driven by negative dynamics of revenues for two consecutive years (-3.8% in 2014, -7.9% in 2015). The structure of tax revenues was changed accordingly: the share of the personal income tax was down from 41.5% to 40.5%, whereas the share of profit tax – another source of budget revenues – increased slightly from 30.4% to 30.5%. Note that in 2015 profit tax revenues dropped by 5.2% in real terms, too. Revenues from aggregate income taxes and property taxes declined less, by 2.7% and 1.3% respectively. Subnational budget revenues from excise duties continued to fall at fast pace (a decline of 12.4% in 2014 and of 10.5% in 2015).

In 2015, nontax revenues dropped on an annualized basis (a decline in real terms of 9.5%). As a result, the share of this source of revenues of the total structure of consolidated budget revenues of subjects of the Russian Federation shrank inconsiderably from 7.8% to 7.6%. It is significant that intergovernmental fiscal transfers in 2015 decreased in real terms by 18.5% amid falling tax and nontax revenues of consolidated budgets of subjects of the Russian Federation.<sup>1</sup>

Let us analyze tax and nontax revenues at the regional level (see *Table 19*).

<sup>1</sup> Detailed analysis of the dynamics of federal budget transfers is made below.

Table 19

**Grouping Russia's regions according to changes in major types of tax  
and nontax revenues of consolidated budgets of subjects  
of the Russian Federation in 2015**

	Change in major types of tax and nontax revenues of consolidated budgets of subjects of the Russian Federation					
	growth by more than 25%	growth by 10 to 25%	growth by less than 10%	decline by less than 10%	decline by 10 to 25%	decline by more than 25%
<b>in nominal terms</b>						
Tax and nontax revenues, total	2	16	49	15	1	0
Profit tax	15	16	15	12	15	10
Personal income tax	0	4	56	23	0	0
<b>in real terms</b>						
Tax and nontax revenues, total	2	0	9	48	24	0
Profit tax	9	6	10	19	21	18
Personal income tax	0	0	2	41	40	0

**Notes:** 1. Arkhangelsk Region and Nenets Autonomous Okrug are presented as a single subject of the Russian Federation. 2. No calculations were made for regions of the Crimean Federal Okrug.

*Sources:* Russia's Federal Treasury, Gaidar Institute's own calculations.

The presented data show that the situation with own-source revenues of subnational budgets remained as much challenging as it was in 2013–2014 in most Russia's regions.<sup>1</sup> In 2015, 72 regions (71 regions in 2014) saw their own-source revenues of subnational budgets decline in real terms, including 48 regions facing a decline of about 10%. Profit tax revenues dropped across the country, and 18 regions saw their profit tax revenues fall by more than 25% in real terms. The deepest fall in profit tax revenues was recorded in the Republic of Tyva (-50.6%), Chechen Republic (-56%), Republic of Mordovia (-76.1%). Overall, the profit tax dropped in real terms in 58 regions. The rest 25 regions saw their profit tax revenues grow in real terms, and in nine subjects of the Russian Federation this tax increased by more than 25%, namely Tambov Region (29.3%), Republic of Karelia (50.1%), Murmansk Region (34.8%), Kirov Region (32.2%), Chelyabinsk Region (27.2%), Republic of Buryatia (108.6%), Magadan Region (49.1%), Sakhalin Region (64.0%), Chukotka Autonomous Okrug (81.1%). Profit tax revenues in the Sakhalin Region increased considerably as a result of implementation of oil and gas projects Sakhalin-1 and Sakhalin-2 as part of production sharing agreements. Profit tax revenues in the Republic of Buryatia soared due to large export-oriented manufacturing facilities (first of all, the Ulan-Ude Aviation Plant). Accordingly, depreciation of the Russian ruble pushed up currency proceeds, and the profit tax charged to the regional budget was on the rise accordingly. Only two subjects of the Russian Federation saw their own-source revenues grow up by more than 25%: Sakhalin Region (31.4%) and Chukotka Autonomous Okrug (28.3%). Revenues from the personal income declined in almost all the regions (81). A minor growth in the personal income tax was recorded only in Belgorod Region (3.7%) and Republic of Mordovia (8.2%).

Let us next analyze changes to the expenditure side of consolidated budgets of subjects of the Russian Federation in 2015 (see *Table 20*).

Overall, given a decline, in real terms, of both tax/nontax revenues and federal budget transfers, and with the debt accumulated by a few subjects of the Russian Federation, Russian subnational authorities conducted a conservative fiscal policy: total volume of expenditure increased only by 1.4% in nominal terms, resulting in a decline of 10.2%, as adjusted for inflation.

<sup>1</sup> In 2014, 71 subjects of the Russian Federation saw own revenues fall in real terms (51 subjects in 2013). Profit tax revenues dropped in real terms by more than 25% in four regions in 2014 and in 23 regions in 2013.

Table 20

**Consolidated budget expenditure of subjects of the Russian Federation  
in 2014–2015**

	As % of total		As % of GDP		Growth, %	
	2014	2015	2014	2015	in nominal terms	in real terms
General National Issues	6.2	6.4	0.74	0.75	4.5	-7.5
National Security and Law Enforcement	1.1	1.1	0.14	0.13	0.5	-11.0
National Economy Including:	18.8	19.7	2.26	2.32	6.1	-6.0
agriculture and fishery	3.0	3.3	0.35	0.39	13.1	0.1
Transport	4.1	4.2	0.49	0.50	4.2	-7.7
Public Road System (Road Funds)	7.6	7.8	0.91	0.92	4.3	-7.6
other issues related to the national economy	2.3	2.4	0.28	0.29	4.8	-7.1
Housing and Utilities	9.6	9.0	1.16	1.06	-5.1	-15.9
Environmental Protection	0.3	0.2	0.03	0.03	-12.7	-22.7
Education Including:	26.2	26.1	3.15	3.07	0.8	-10.7
pre-primary education	7.0	7.3	0.84	0.86	5.3	-6.7
general education	15.0	14.6	1.80	1.72	-0.9	-12.3
secondary vocational education	2.1	2.0	0.25	0.24	-2.1	-13.3
other issues related to education	1.4	1.3	0.17	0.15	-8.6	-19.0
Culture, Cinematography	3.4	3.3	0.41	0.39	-2.5	-13.7
Healthcare	13.9	14.3	1.66	1.69	4.6	-7.4
Social Policy	15.1	15.8	1.82	1.86	5.8	-6.3
Physical Culture and Sports	2.0	2.0	0.24	0.24	1.3	-10.3
Mass Media	0.5	0.5	0.05	0.05	2.9	-8.9
Municipal and public debt servicing	1.3	1.6	0.16	0.19	22.4	8.4
<b>Expenditure, total</b>	<b>100.0</b>	<b>100.0</b>	<b>12.01</b>	<b>11.79</b>	<b>1.4</b>	<b>-10.2</b>

Sources: Russia's Federal Treasury, Gaidar Institute's own calculations.

Analysis of changes in various line items of budget expenditure in regions reveals the following. In 2015, the annualized expenditure for 'Environmental Protection' (a decline of 12.7% in nominal and of 22.7% in real terms) declined the most. However, these expenditure left the total expenditure structure unchanged because the share of the former stood at 0.03%. The structure of expenditure was changed due to a decline in expenditure for 'Housing and Utilities' (down by 15.9% in real terms). Regions' policy aimed at cutting expenditure for 'Housing and Utilities' was a measure to counter fiscal disequilibrium, budget deficit and large debts. Note that the downtrend towards expenditure for the housing and utilities sector is likely to continue in the near term. For example, in 2016 federal budget allocations for the foregoing expenditure are planned to be cut by 47.2% from the value seen in 2015. Running short of their own-source revenues and facing cuts on federal co-financing, regions are unlikely to be able to spend more on 'Housing and Utilities'. Overall, the decline in expenditure in real terms can be seen for all the expenditure line items, except for 'Municipal and Public Debt Servicing'. These expenditure increased first of all because the volume of public and municipal debt rose by 11% and 9% respectively (see below for more details). However, the growth in expenditure for debt servicing slowed down inconsiderably as a result of replacement of a share of commercial debts with budget loans at an extremely low interest rate<sup>1</sup> (the volume of budget loans increased by 24.9% as of 2015 year-end). The 2015 year-end expenditure for 'Municipal and Public Debt Servicing' of the total expenditure structure rose from 1.3% in 2014 to 1.6%, by 0.03 percentage points of GDP: from 0.16% to 0.19% of GDP.

Overall, expenditure increased in nominal terms for all the line items, except 'Housing and Utilities', 'Environmental Protection', 'Culture and Cinematography'. Efforts were made to

<sup>1</sup> 0.1% per annum.

increase inconsiderably expenditure for ‘National Economy’ as a whole (6.1%) and the subitems related thereto. In particular, expenditure for ‘Transport’ and ‘Public Road System (Road Funds)’ increased by 4.3% and 4.8% respectively. ‘Agriculture and Fishery’ saw the biggest growth in expenditure not only in nominal terms (by 13.1%) but also in real terms (by 0.1%).

Let us next consider the dynamics of principal (not only expenditure) parameters of consolidated budgets of subjects of the Russian Federation, as a percentage of GDP (see *Table 21*).

*Table 21*

**Dynamics of revenues and expenditure of consolidated budgets of subjects of the Russian Federation in 2008–2015, as % of GDP**

	2008	2009	2010	2011	2012	2013	2014	2015
<b>Revenues</b>	<b>15.02</b>	<b>15.27</b>	<b>14.12</b>	<b>12.80</b>	<b>12.05</b>	<b>11.49</b>	<b>12.30</b>	<b>12.93</b>
Including:								
profit tax	4.24	2.76	3.28	3.23	2.96	2.42	2.76	2.95
personal income tax	4.04	4.29	3.87	3.34	3.38	3.52	3.77	3.92
Federal budget transfers	2.65	3.81	2.98	2.42	2.15	2.13	2.17	2.16
<b>Expenditure</b>	<b>15.15</b>	<b>16.12</b>	<b>14.33</b>	<b>12.86</b>	<b>12.47</b>	<b>12.39</b>	<b>12.97</b>	<b>13.17</b>
<b>Deficit (-) / Surplus (+)</b>	<b>-0.13</b>	<b>-0.85</b>	<b>-0.22</b>	<b>-0.06</b>	<b>-0.42</b>	<b>-0.90</b>	<b>-0.67</b>	<b>-0.24</b>
For reference: GDP, rubles in billions	41.277	38.807	46.309	59.698	66.927	71.055	77.893	80.413

**Note:** No calculations were made for regions of the Crimean Federal Okrug.

*Sources:* Russia’s Federal Treasury, Gaidar Institute’s own calculations.

2009 saw the biggest volume as a percentage of GDP of both revenues and subnational budget expenditure in the period of 2008–2015. Revenues rose in 2009 as a result of considerable growth (by 35.2%) of federal budget transfers, and expenditure increased due to the implementation of measures as part of an anti-crisis program (both at the federal level – using subsidies and subventions – and at the regional level). However, tax revenues in regions dropped in 2009 mostly as a result of declining profit tax revenues. It is therefore more appropriate to take the pre-crisis year of 2008 as the comparative base (recessionary trends in the fiscal sector were not visible until the last few months of 2008).

The data in *Table 21* show that in 2015 revenues from the personal income tax, profit tax, federal budget transfers did not reach levels recorded in 2008. Sources of revenues such as the profit tax and intergovernmental fiscal transfers were the farthest behind the 2008 levels. However, expenditure were much less in volume: 13.2% of GDP in 2015 against 15.2% of GDP in 2008.

In 2015, both revenues and expenditure increased as a percentage of GDP from 2014, by 0.63 and 0.2 percentage points respectively. The growth was observed for two consecutive years. Note that total expenditure and revenues increased in volume while they fell in real terms. The dynamics was observed amid slowing down GDP growth rates, with a 3.7% fall in 2015. The processes suggest that the economy is shrinking faster than changes in the principal parameters of subnational budgets of subjects of the Russian Federation. As a result, the deficit in 2015 was reduced in volume from 0.67% to 0.24% of GDP. Furthermore, in 2015, 36 regions reduced their expenditure even in nominal terms compared with the level recorded in 2014. Expenditure were reduced the most in the Amur Region (-13.8%), Yamalo-Nenets Autonomous Okrug (-13.2%) and Pskov Region (-10.6%).

Let us analyze in detail the situation with execution of consolidated budgets of subjects of the Russian Federation (deficit/surplus) in various regions (see *Table 22*).

*Table 22*

### Execution of (deficit/surplus) consolidated budgets of subjects of the Russian Federation in 2008–2015

Year	Number of subjects of the Russian Federation that executed their budgets	
	with a deficit	with a surplus
2008	45	39
2009	62	21
2010	63	20
2011	57	26
2012	67	16
2013	77	6
2014 <sup>1</sup>	74	9
2015 <sup>1</sup>	75	8

<sup>1</sup> Excluding regions of the Crimean Federal Okrug.

Sources: Russia's Federal Treasury, Gaidar Institute's own calculations.

The data in *Table 22* show that in 2015 consolidated budgets of subjects of the Russian Federation remained nearly as balanced in terms of quantity of regions as they were in 2014. Seventy five subjects of the Russian Federation ran a budget deficit in 2015 (74 in 2014). At the same time, five subjects (Lipetsk Region, Kaliningrad Region, Republic of Ingushetia, Yamalo-Nenets Autonomous Okrug, Republic of Altai) ran a budget surplus in 2014 and a budget deficit in 2015.<sup>1</sup> Three of the five regions increased their expenditure above the Russia's average level (1.4% in nominal terms).

Overall, in 2015 the parameters of consolidated budgets of subjects of the Russian Federation continued to be affected by adverse macroeconomic factors. Cost optimization opportunities continued to be sought at the subnational level. As a result, in 2015 expenditure were maintained at the year-earlier level, with a minor increase for 'National Economy'. The situation with revenues is more complex, first of all, because of the prevailing downtrend towards personal income and revenues from the personal income tax. Profit tax revenues were kept at a steady level largely due to export-oriented industries. The financial standing of Russia's regions is mixed in general. For instance, subnational budget deficit in 2015 dropped by 2.5 times due to a surplus of Rb 144.3bn in Moscow (a deficit of Rb 54.3bn in 2014) rather than because of financial rehabilitation across the regions. The downtrend towards federal budget transfers had an adverse effect on the volume of revenues in regions, too (see below for details).

#### 2.3.2. Financial support from the federal budget

In 2015, total volume of intergovernmental fiscal transfers to consolidated budgets of subjects of the Russian Federation (including the Crimean Federal Okrug) contracted both in nominal terms (-0.2%) and in real terms (-11.6%) from 2014 (see *Table 23*).

Overall, the volume of financial support shrank for almost all types of transfers, except 'Other intergovernmental fiscal transfers' (hereinafter – "other IBTs") that increased by 67.4% in real terms at 2015 year-end as a result of greater support for the development of the public road system as part of the Transport System Development State Program. In 2015, Rb 83.4bn (Rb 3.7bn in 2014) were allocated for this purpose.

*Table 23*

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<sup>1</sup> Excluding regions of the Crimean Federal Okrug.

## Federal budget transfers to subjects of the Russian Federation in 2009–2015\*

	2009		2013		2014		2015		Growth %, 2015 from 2014	
	rubles in bil-lions	as % of to-tal	rubles in bil-lions	as % of to-tal	rubles in bil-lions	as % of total	rubles in bil-lions	as % of to-tal	in nomi-nal terms	in real terms
<b>Transfers to regions, total</b>	<b>1.480,3</b>	<b>100</b>	<b>1.487,9</b>	<b>100</b>	<b>1.607,0</b>	<b>100</b>	<b>1.603,6</b>	<b>100</b>	<b>-0.2</b>	<b>-11.6</b>
<b>Grants</b>	<b>578.3</b>	<b>39.1</b>	<b>609.1</b>	<b>40.9</b>	<b>774.7</b>	<b>48.2</b>	<b>650.9</b>	<b>40.6</b>	<b>-16.0</b>	<b>-25.6</b>
Including:										
equalization transfers	374.0	25.3	418.8	28.1	439.8	27.4	487.7	30.4	10.9	-1.8
grants for measures to ensure budget balance	191.9	13.0	177.8	12.0	334.9	20.8	163.2	10.2	-51.3	-56.8
<b>Subsidies</b>	<b>530.0</b>	<b>35.8</b>	<b>515.6</b>	<b>34.7</b>	<b>409.9</b>	<b>25.5</b>	<b>400.2</b>	<b>25.6</b>	<b>-2.4</b>	<b>-13.5</b>
Including:										
subsidies to develop the national economy	214.3	14.5	268.3	18.0	241.9	15.1	258.2	16.1	6.7	-5.5
<b>Subventions</b>	<b>284.4</b>	<b>19.2</b>	<b>273.7</b>	<b>18.4</b>	<b>308.2</b>	<b>19.2</b>	<b>336.6</b>	<b>21.0</b>	<b>9.2</b>	<b>-3.3</b>
<b>Other intergovernmental fiscal transfers</b>	<b>87.6</b>	<b>5.9</b>	<b>89.5</b>	<b>6.0</b>	<b>114.2</b>	<b>7.1</b>	<b>215.9</b>	<b>13.5</b>	<b>89.1</b>	<b>67.4</b>

\* Unlike the previous paragraph, here volumes of transfers include the Crimean Federal Okrug.

Sources: Russia's Federal Treasury, Gaidar Institute's own calculations.

The structure of transfers was changed drastically due to considerable growth of other IBTs and cuts on other types of transfers. For instance, the share of other IBTs increased from 7.1% to 13.5% while the share of subsidies and subventions rose from 25.5% to 25.6% and from 19.2% to 21.0% respectively. In real terms, the volume of subsidies dropped by 13.5% while subventions decreased in volume by 3.3%. Overall, the decline in the volume of subsidies (both in nominal and real terms) was offset by a sharp hike of other IBTs. The volume of subventions is largely determined by the size of indexation of social benefits, and its growth rate tends to slow down. In fact, subnational budgets have not become less reliant in terms of exercising delegated powers. Although transfers have been reduced in volume, there is still a great number of subsidies with overdetailed spending of budget funds, as well as with considerably wide scope of delegated powers. For instance, 86 subsidies were planned for 2015 (92 subsidies in 2014). However, the 2015 year-end subsidies increased in number to 96 under the amended federal budget law. The mechanism of subsidization is more efficient to ensure proper spending of budget funds than to reach the target, a great number of subsidies facilitates growth of administrative costs on monitoring the spending of subsidies. Under the state sub-program called "Enhancing the system of allocation and reallocation of financial resources between the levels of the budget system of the Russian Federation", federal budget subsidies to budgets of subjects of the Russian Federation are to be reduced in number on a step by step basis, with their number set to be optimized (consolidated) to 70 at Stage I (2013–2015) and to 42 at Stage II (2016–2020).

Note that total number of subventions increased from 18 in 2014 to 21 in 2015. The number of subventions increased on the back of consolidation of nine subventions into a single subvention. The number of subventions increased partly due to delegation of certain powers to budgets of the Republic of Crimea and of the federal city of Sevastopol.

Reducing the share of targeted financial support is a priority of the fiscal policy.<sup>1</sup> The share of grants was formally reduced from 48.2% to 40.6% in 2015, which, however, corresponds to the target value stipulated in the Guidelines of the Fiscal Policy for 2016–2018 (41.2% in 2015,

<sup>1</sup> See, e.g., the Guidelines of the Fiscal Policy of the Russian Federation for 2016 and for the Planning Period of 2017–2018.

45.1% in 2016). In 2015, grants were reduced in volume because, first, financing under the state program called “Creation of conditions for efficient and prudent management of regional and municipal finance, enhancement of sustainability of budgets of subjects of the Russian Federation” was completed, whereby Rb 167bn were allocated in 2014 (excluding expenditure as partial compensation for extra expenditure to increase public sector wages). In 2015, as little as Rb 62.7bn were allocated for the implementation of the state program called “Development of federative relations and creation of conditions for efficient and prudent management of regional and municipal finances”. Second, in 2015 the volume of financial support as partial compensation for extra expenditure to increase public sector wages was cut in half to Rb 59.8bn, as a result of which the share of grants allocated in support of measures aimed at ensuring budget equilibrium in the structure of transfers shrank from 20.8% to 10.2% (by Rb 171.7bn).

In general, the decline in the share of grants allocated in support of measures aimed at ensuring budget equilibrium is a positive factor, because the grants are much less transparent than equalization transfers that in 2015 saw the least negative dynamics (-1.8%) compared with other types of transfers. However, the federal government’s policy aimed at a broader application of the budget loan instrument instead of equalization grants raises some questions, because regions will have to repay budget loans. Should Russia’s economy see no improvements in the years to come, there may be risks of regions being unable to repay their federal budget loans, in which case the federal government will have to extend new budget loans to ensure that old budget loans are repaid, or they will have to decide on writing off (or “freezing”) outstanding budget loans. Such a situation will deteriorate the transparency of intergovernmental fiscal relations, and it will inevitably deteriorate the fiscal discipline of regional government authorities.

Analysis of the process of allocation of federal government transfers to regions should consider the effect of federal support on differentiation of revenues of subjects of the Russian Federation, measuring the equalization performance of financial support from the federal budget (see *Table 24*).

*Table 24*

**Variation coefficient of consolidated budget revenues in regions  
(per capita, with consideration for budget expenditure index) in 2008–2015, %**

Year	Tax revenues	Tax revenues and equalization transfers	Tax revenues, grants, subsidies
2008	90.6	80.4	71.5
2009	78.3	66.5	54.5
2010	74.2	63.9	57.8
2011	77.8	68.4	61.6
2012	66.1	57.8	51.9
2013	63.7	55.3	48.1
2014	59.0	51.2	49.9
2015	66.1	60.3	56.0

**Note:** No calculations were made for regions of the Crimean Federal Okrug.

*Sources:* Russia’s Federal Treasury, Ministry of Finance, Gaidar Institute’s own calculations.

The data in *Table 24* show that differentiation of subnational budget revenues increased in 2015. The coefficient of tax revenues of consolidated budgets of subjects of the Russian Federation was up from 59% to 66.1%, reaching the level seen in 2012. With equalization transfers, the variation coefficient of budget revenues in regions increased from 51.3% in 2014 to 60.3% in 2015, and with all the allocated grants and subsidies, it increased in 2015 to 56% (49.9% in 2014). Differentiation of regional revenues in 2015 increased largely because the profit tax was up in a few subjects of the Russian Federation, which was related to export-oriented industries. For instance, the profit tax rose by more than 25% from 2014 in 15 regions (in nominal terms) and in 9 regions (in real terms).

### 2.3.3. Debt policy at regional level

*Table 25* shows data on the dynamics of volumes of public debt owed by subjects of the Russian Federation and municipal debt in 2010–2015. The Table shows that in 2015 the year-to-date growth in the debt owed by regional budgets was nearly 11% in nominal terms (for comparison: 28.2% in 2013, and 20.3% in 2014), excluding 14% in Moscow and Moscow Region (37.9% in 2013, 23.8% in 2014). The volume of debt owed by municipal budgets rose by 8.9% during the same period (17.8% in 2013, 8.4% in 2014). In December 2015, the debt of subjects of the Russian Federation was equal to or less than 6% over the volumes recorded as of December 1st, which differs notably from the practice of 2012–2014, when the year-end debt increased by 15–20%.

*Table 25*

#### Subnational budgets' public and municipal debt in nominal terms in 2011–2015, rubles in billions

	As of 2011 year-end		As of 2012 year-end		As of 2013 year-end		As of 2014 year-end		As of 2015 year-end	
	volume, rubles in billions	growth, %								
Total in regional budgets	1172	7	1355	16	1738	28	2090	20	2319	11
Total in regional budgets (excluding Moscow and Moscow Region)	832	28	1069	28	1474	38	1825	24	2079	14
Total in municipal budgets	216	27	245	13	289	18	313	8	341	9

Sources: Russia's Ministry of Finance, Rosstat, Gaidar Institute's own calculations.

Regional debt growth rates slowed down considerably in 2015, following the earlier downturn at the municipal level (municipal debt growth rates slowed down notably as early as 2014). 2015 saw debt growth rates slow down at the subnational level largely as a result of curtailing growth in expenditure that increased in nominal terms by mere 1.4% year-over-year (to compare, 5.6% in 2013 and 6.2% in 2014) amid favorable dynamics in nominal terms of tax and nontax revenues of regional consolidated budgets: a growth of 6.2% (however, a decline of 5.9% in real terms). As a result, subjects of the Russian Federation ran a consolidated budget deficit of 0.3% of GDP in 2015 against 0.6% of GDP in 2014 and 0.8% of GDP in 2013.

Overall, the dynamics of regional debt in 2011–2015 revealed a steady uptrend from 2.0% of GDP as of 2011 year-end to 2.9% of GDP as of 2015 year-end<sup>1</sup> (see *Table 26*). The volume of regional debt is estimated to be insignificant for the budget system and the economy as a whole. Given the slowdown in 2015, the regional debt does not yet pose a serious macroeconomic risk at the national level. However, a more correct assessment of the situation with the regional debt and with related budget risks requires analysis by subject of the Russian Federation.

*Table 26*

<sup>1</sup> The presented data rely on Rosstat's data calculated using a new method for GDP in 2011–2015.

**Volumes of public and municipal debt of subnational budgets  
in 2011–2015, as % of GDP**

	As of 2011 year-end		As of 2012 year-end		As of 2013 year-end		As of 2014 year-end		As of 2015 year-end	
	as % of GDP	growth, percentage points of GDP	as % of GDP	growth, percentage points of GDP	as % of GDP	growth, percentage points of GDP	as % of GDP	growth, percentage points of GDP	as % of GDP	growth, percentage points of GDP
Total to budgets in regions	2.0	-	2.0	0.1	2.4	0.4	2.7	0.2	2.9	0.2
Total for regional budgets (excluding Moscow and Moscow Region)	1.4	-	1.6	0.2	2.1	0.5	2.3	0.3	2.6	0.2
Total for municipal budgets	0.4	-	0.4	0.0	0.4	0.0	0.4	0.0	0.4	0.0

Sources: Russia's Ministry of Finance, Rosstat, Gaidar Institute's own calculations.

Note that previously only two subjects of the Russian Federation, namely Moscow and Moscow Region made up the major share of regional debt (as of January 1, 2011, they accounted for 40.7% of the total regional debt), whereas as of January 1, 2016 they accounted for about 10% of the total debt. This reflects the recently mounting problem with executing budgets at the regional level, which prompted not a few but many regions to raise funds to cover their current expenses rather than to finance investment.

The data on regions reveal that many subjects of the Russian Federation increased their debt volumes in 2015 (see *Table 27*). At the same time, it is significant that there was redistribution of regions towards growth in the number of subjects of the Russian Federation with a more moderate (less than 15% a year) growth in indebtedness, as well as the number of regions that reduced the volume of their debt increased notably (from 8 in 2014 to 16 in 2015).

The 2015 debt structure of Russia's regions was changed towards considerable growth in the volume of federal budget loans (see *Fig. 23*). The share of budget loans increased to 34.9%, by 3.9 percentage points above the value seen earlier in 2015. Outstanding budget debts increased as the share of commercial loans and government securities shrank by 0.9 and 2.5 percentage points respectively. In absolute terms, the volume of the commercial share of debts owed by subjects of the Russian Federation (government securities and commercial loans) shrank by about Rb 56bn. Thus, a trend unfolded towards replacing commercial loans with budget loans across regional budgets, reflecting region-focused priorities of the federal government's current policy.

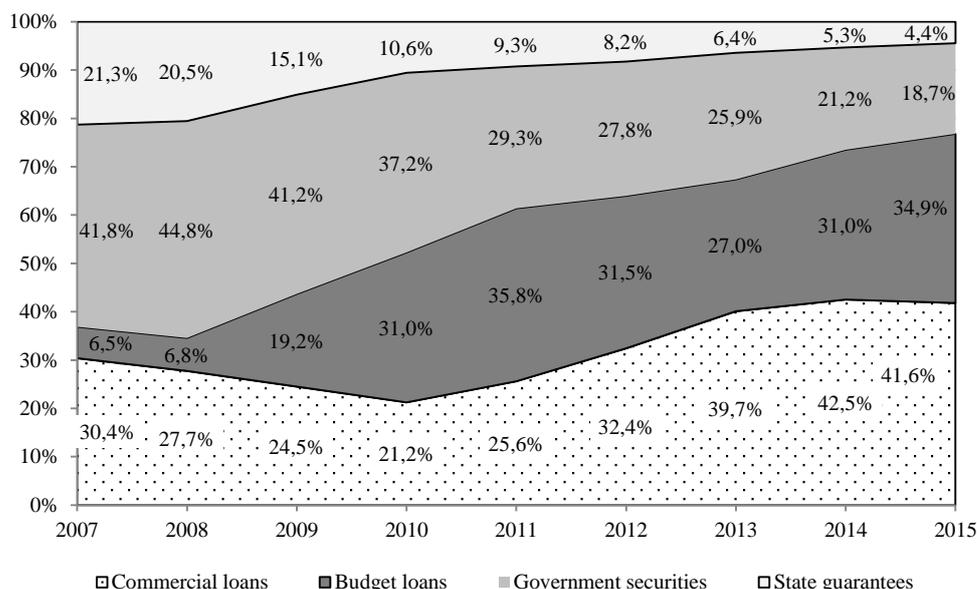
*Table 27*

**Dynamics of public debt owed by budgets of subjects  
of the Russian Federation in 2008–2015**

	Dynamics of public debt owed by subjects of the Russian Federation in a certain period (in nominal terms), number of subjects of the Russian Federation					
	growth by more than 50%	growth by 15 to 50%	growth by less than 15%	decline by less than 15%	decline by 15 to 50%	decline by more than 50%
2008	21	20	10	6	12	9
2009	37	18	11	6	4	2
2010	29	24	8	11	7	0
2011	21	27	13	14	6	0
2012	18	29	14	8	10	1
2013	31	36	8	6	1	0
2014	12	44	18	5	1	2
2015	7	27	31	15	1	0

**Note:** Arkhangelsk Region and Nenets Autonomous Okrug are presented as a single subject of the Russian Federation; the presented data exclude the Crimean Federal Okrug (to ensure full compatibility at various years).  
**Sources:** Russia’s Ministry of Finance, Gaidar Institute’s own calculations.

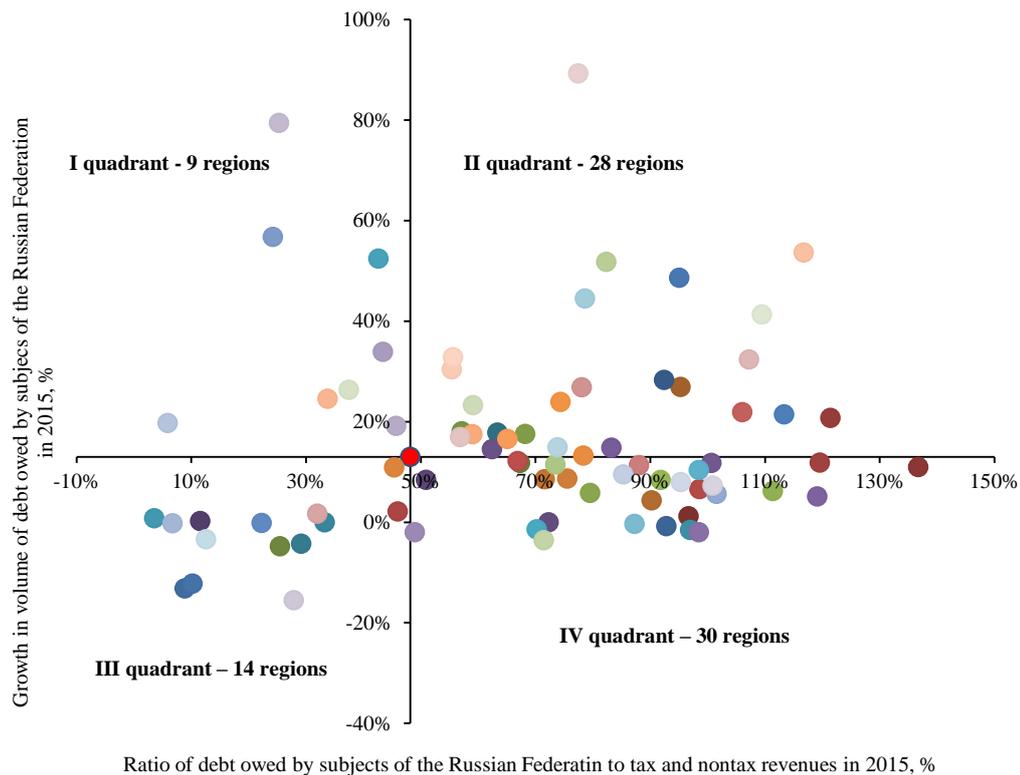
However, the situation differs largely from one region to another, which may necessitate further growth in the volume of budget loans (for regions that continue accumulating commercial debts). This creates risks of even heavier reliance of subjects of the Russian Federation on federal budget loans, which in turn would build up political pressure on Russia’s Ministry of Finance over making a decision on writing off or “freezing” repayments. Although such a measure seems to be simple in terms of tackling the problem of debts accumulated by some subjects of the Russian Federation, it can substantially undermine the fiscal discipline at the regional level and deteriorate the problem of soft fiscal constraints of subnational authorities in Russia.



**Note:** The presented data exclude the Crimean Federal Okrug (to ensure full compatibility at various years).

*Fig. 24. Structure of public debt owed by subjects of the Russian Federation in the period of 2007–2015*

*Fig. 23* shows a breakdown of subjects of the Russian Federation according to the dynamics of debt burden and growth rates in debt volumes in 2015. Subjects of the Russian Federation located in II quadrant are more vulnerable in terms of fiscal sustainability. This group includes 28 regions where the level of debt burden (the ratio of debt amount to the volume of regional budget revenues, excluding transfers) and growth rates of debt volumes in 2015 were higher than Russia’s average values (excluding Moscow). In terms of general values (excluding debt structure), the following regions faced the most challenging situation: Republic of Mordovia (in 2015, the debt volume increased by 26.2%, the level of debt burden was 182.5% as of January 1, 2016), Smolensk Region (+20.8% and 121.4%), Republic of Khakassia (+53.6% and 116.8%), Republic of Ingushetia (+21.5% and 113.3%), Jewish Autonomous Region (+41.3% and 109.5%), Zabaykalskiy Territory (+32.3% and 107.2%), Republic of Mariy-El (+21.9% and 106.1%).



**Fig. 24.** Debt burden and change in volumes of public debt owed by subjects of the Russian Federation in 2015

**Notes:** 1. The axes intercept at the point where debt burden and growth of volume of debt owed by subjects of the Russian Federation in 2015 take on Russia’s average values (48.2% and 13% respectively, excluding Moscow). 2. The figure shows Tyumen Region (0.89%, 256.9%), Republic of Mordovia (182.5%, 26.2%).  
**Sources:** Russia’s Federal Treasury, Ministry of Finance, Gaidar Institute’s own calculations.

However, to assess sustainability of regional budgets, it is important to consider not only the general dynamics of debt but also the structure thereof. Analysis of the structure of indebtedness of the subjects of the Russian Federation located in II quadrant shows that the most challenging situation unfolded in 9 of 28 regions, where commercial loans and bonded loans increased in volumes in 2015. The rest 19 subjects increased the volume of their regional debt due to budget loans and/or state guarantees. Note that in 2015 a few subjects of the Russian Federation increased their commercial debt despite considerable volumes thereof in the regional debt structure as early as 2015. Analysis of the 2015 data shows that six regions faced the most alarming situation: Magadan Region (in 2015, the outstanding commercial debt increased by 95% in nominal terms; the share outstanding commercial debt of the total regional debt was 88% as of the beginning of 2015), Republic of Khakassia (+73%; 71%), Republic of Mariy-El (+55%; 58%), Kurgan Region (+53%; 73%), Ivanovo Region (+52%; 75%), Novosibirsk Region (+38%; 74%).