

ASSESSMENT OF THE BUSINESS CLIMATE IN RUSSIA

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The Global Competitiveness Report 2013-2014 has been published. Its findings are virtually the same as in the report for the previous year which was analyzed in the Gaidar Institute's August Review. In the business climate, the most difficult situation for more than a single year has prevailed in such lines as weak protection of ownership rights, lack of independence of courts and corruption at courts, excessive state regulation burden, ineffective security of an individual, low level of corporate culture, weak competition, preservation of administrative barriers and high tax burden and inconsistent taxation. In other words, all the factors which make business feel insecure about the future and determine an underlying motive to withdraw capital abroad rather than invest in development of business in Russia still remain in place. A favorable situation is registered in macroeconomics (as long as prices on hydrocarbons do not fall) and quite a good one in the infrastructure (unless the situation with motor roads is considered a failure), secondary and higher education and retraining. Generally, Russia moved from the 67th place to the 64th place (the 63rd place in 2010 and the 51st place in 2008). It is to be noted that improvement also took place in the most painful aspects of the business climate though there were no explicit progress factors. The higher rating place can be explained by both expectations, including those not to change taxes and a certain lag of published materials from the statistical data and some information events in 2013. The Report fairly represents the realities of 2012 and, partially, till the middle of 2013.

The recently published Global Competitiveness Report 2013–2014 includes the updated data on **The Global Competitiveness Index**¹. The above research provides the most comprehensive evaluation of various aspects of the business climate. The latest Report covers 148 countries against 144 countries last year.

The analysis of the institutional environment with utilization of different ratings was provided in the August 2013 review by the Gaidar Institute². The main conclusion consists in the fact that in the present situation the private business is not confident in its future, primarily, due to unsatisfactory protection of ownership rights, lack of independence of courts and abuse

of power by the judicial system and pervasive corruption. The above factors cause mistrust of the authorities and apprehension to make large investments and prompt the business to withdraw its capital from the country. Also, the inhibiting factor is a weak competition, considerable administrative barriers faced by businessmen and inconsistent rules of regulation of the economy.

In the latest Global Competitiveness Report, the situation in Russia is assessed somewhat better than in the previous one though all the problems still prevail. Russia moved three positions upward from the 67th place to the 64th place. That rating is better than in 2011³ (the 66th place), but worse than in 2010 (the 63rd place). The level of the index itself rose insignificantly, too, from 4.2 to 4.25 (with the maximum value of 7, the highest value (5.67) was achieved by Switzerland). Switzerland was followed by Finland (5.54), Germany (5.51) and the US (5.48). At the bottom of the index, there are Sierra Leone (3.01), Yemen (2.98) and Guinea (2.91). Russia's best index level was registered before the crisis of 2008 when it occupied the 51st place.

Dynamics of the index of competitiveness and places occupied by Russia by the main blocks and groups of factors are shown in *Table 1*. As seen from the table, the most explicit advance took place (no matter how strange it might be) as regards the block which includes the factors of innovation and the quality level of doing business: from the 108th place to the 99th place

1 The Global Competitiveness Report 2013-2014. Full Data Edition. http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2013-14.pdf The Global Competitiveness Index is developed under the auspices of the World Economic Forum (WEF) on the basis of both the statistical data and the global survey of managers of enterprises with assistance of 150 partner-entities. The index deals with 114 aspects of competitiveness which are united into 12 major groups of factors (benchmarks) which are divided in their turn into three blocks: baseline conditions, efficiency factors, innovation and the quality of performance. About two-thirds of the aspects of competitiveness are determined on the basis of surveys. The index is determined in absolute terms and varies from 1 to 7 (from the low level of competitiveness to the highest one; the respondents in different countries are normally asked to use the above scale to evaluate each aspect of competitiveness and the obtained outputs are subsequently weighted in accordance with the adopted methods to determine the aggregate index) and the country rating is specified as its line number.

2 See. V. Starodubrovsky. The State of the Business Climate in the Country. The Economic Development of Russia. No. 9, 2013, pp. 55–62.

3 The first year – from among those specified in the reports – which the collected information actually refers to will be used.

which is nowhere near the place of honor, but, nonetheless, was an advance nine positions upward. It is to be noted that prior to 2012 Russia occupied higher places in the index. The index improved somewhat as well (from 3.2 to 3.3), but it remains rather low. The unit weight of that block of factors which determines the influence on the general competitiveness index amounts in accordance with the adopted methods to 23.1%. Baseline conditions – the 47th place against the 53rd place in the previous year with a great dispersion of estimates of the groups of factors inside that block – were evaluated somewhat higher, too. It is to be noted that that place was the best one for the years specified in the table.

The block's unit weight amounts to 26.9%. The block of efficiency factors whose unit weight amounts to 50% advanced three positions upward from the 54th place to the 51st place, though before the crisis its positions were better. Within the block, the difference in estimates of individual groups of factors is rather high, too.

Also, the table provides an idea of the dynamics of more favorable and backward spheres of the economy which competitiveness depends on. If the explicit advantage in the scale of the market is put aside – which advantage among other things is an attractive factor for foreign investments and makes many Western companies be ready to invest in the Russian economy should other conditions improve – the **macroeconomic environment** is worth paying attention to (as regards macroeconomic environment Russia is rated the 19th and has the highest index (5.9) among all the groups of factors). The estimate is entirely based on the official data and not on the surveys. The main advantages are related to the low level of the state debt in relation to GDP where Russia is rated the 10th (though in 2012 and 2011 it held the 9th place and the 7th place, respectively) and has quite a favorable balance of the state budget (the 23rd place against the 20th place in 2012). At the same time, the above example illustrates vulnerability of mechanical utilization of the statistical data as in conditions of dependence on hydrocarbons the soundness of the budget system is not quite reliable and actually remains rather strained. The above is pointed to by a reduction of expenditures – that reduction is planned in the 2014–2016 budget – which measure though a delayed one is still very important. As regards the credit rating, Russia is rated the 39th though before the crisis it was rated the 10th. When exiting the crisis, Russia moved downwards to the 49th place. The worst thing in that group – evaluation of the rate of inflation – was the 91st place; it is to be noted that in 2012 the inflation rate (December on December) was par-

ticularly low and amounted to 5.1%. In 2011, Russia held the 111th place, while in 2010, the 125th place.

The next one in the group of factors is **infrastructure** where Russia is rated the 45th though it is the best result in the years under review. Russia's standing in that group suffers due to a poor quality of motor roads: the 136th place and the worst index (2.5) from among the entire 114 factors of competitiveness. The quality of the railway infrastructure is rated better – the 31st place – however, as regards infrastructure of ports and airline service it is rated the 88th and 102nd, respectively. So, as regards the general quality of infrastructure Russia is rated 93rd with a low index of 3.8. However, in the past three years the situation was even worse. The entire group is propelled to a higher level thanks to the extent of density of mobile phones (the 6th place) and seat capacity of airline service (the 11th place).

The secondary and higher education and retraining is rated 47th with the index of 4.7. The above position is primarily ensured by a large number of students at higher education establishments (the 14th place), availability of the Internet at schools (the 54th place) and the quality of mathematical and science education. As regards other factors of that group, Russia's positions are worse than generally in the Global Competitiveness Index. It is to be noted that as regards retraining of personnel and the quality of management schools Russia is rated the 88th and even the 113th, respectively. Interestingly, as regards the **education and primary education** group of factors Russia's index is much higher (5.7) than that of the secondary and higher education and retraining, however the 71st place is the worst one in the years under review. It means that a larger number of countries is more successful and quick at making progress in that area. However, in that group evaluations of specific aspects of competitiveness are almost entirely based on the statistics data and the zero incidence rate of malaria – which permits to share the first place as regards that factor with a number of other countries – plays a particular role. However, as regards child mortality, the TB incidence rate and life expectancy Russia is rated the 58th, the 94th and the 101st, respectively. The quality of primary education is evaluated on the basis of surveys and Russia is rated the 61st with the index of 4.1, that is, lower on average than that as regards the secondary and higher education and retraining.

Now, let us discuss factors related directly to the institutional environment and the business climate. The parameters of individual aspects of that environment are included in different groups of factors. Let us begin from those which are included in evaluations of the **efficiency of the commodity market**. As regards the above criterion, Russia is rated the 126th of all the

Table 1

CHANGES IN THE GLOBAL COMPETITIVENESS INDEX AND THE MAIN GROUPS OF ITS FACTORS FROM 2007 TO 2013

	2007–2008 (131)*		2008–2009 (134)		2009–2010 (133)		2010–2011 (133)		2011–2012 (142)		2012–13 (144)		2013–14 (148)	
	Place	Index	Place	Index	Place	Index	Place	Index	Place	Index	Place	Index	Place	Index
Global Competitiveness Index	58	4.19	51	4.31	63	4.15	63	4.24	66	4.21	67	4.2	64	4.25
Baseline conditions	68	4.4	56	4.5	64	4.4	65	4.5	63	4.6	53	4.8	47	4.9
Institutes	116	3.1	110	3.3	114	3.2	118	3.2	128	3.1	133	3.1	121	3.3
Infrastructure	65	3.5	59	3.7	71	3.6	47	4.5	48	4.5	47	4.5	45	4.6
Macroeconomic environment	37	5.4	29	5.6	36	5.2	79	4.5	44	5.2	22	5.8	19	5.9
Healthcare, education and primary education	60	5.5	59	5.6	51	5.6	53	5.9	68	5.7	65	5.7	71	5.7
Efficiency factors	48	4.2	50	4.3	52	4.2	53	4.2	55	4.2	54	4.3	51	4.3
Secondary and higher education and retraining	45	4.3	46	4.4	51	4.3	50	4.6	52	4.5	52	4.6	47	4.7
Commodity market efficiency	84	3.9	99	3.9	108	3.7	123	3.6	128	3.6	134	3.6	126	3.8
Labor market efficiency	33	4.7	27	4.7	43	4.7	57	4.5	65	4.4	84	4.2	72	4.3
The extent of development of the financial market	106	3.6	112	3.6	119	3.3	125	3.2	127	3.2	130	3.2	121	3.4
Technological efficiency	72	3.0	67	3.4	74	3.4	69	3.6	68	3.7	57	4.1	59	4
Market scale	9	5.5	8	5.7	7	5.8	8	5.7	8	5.7	7	5.8	7	5.8
Factors of innovation and quality of doing business	77	3.5	73	3.6	73	3.5	80	3.4	97	3.2	108	3.2	99	3.3
Quality of doing business	88	3.7	91	3.7	95	3.6	101	3.5	114	3.3	119	3.3	107	3.6
Innovations	57	3.3	48	3.4	51	3.4	57	3.2	71	3.1	85	3	78	3.1

* The number of countries researched is specified in brackets.
Source: <http://www.weforum.org/>

groups of factors (with the index of 3.8). The above low position is determined primarily by institutional conditions. **The level of competitiveness.** As regards the extent of competitiveness on the domestic market, Russia is rated the 113th with a fairly good index of 4.5 against the 124th place in 2012 and 2011 and the 106th place in 2009, as regards the extend of domination on the market, it is rated the 93rd with the index of 3.5 though a year before it was rated the 107th, as regards the efficiency of anti-trust policy it was rated the 116th (the index of 3.5) against the 124th place and the 111th place in 2012 and 2011, respectively. Despite the occasionally favorable dynamics, the level of competitiveness is still estimated at a very low level. **Taxation.** As regards the effect of taxes on motivation of investments, Russia is rated the 125th (the index of 3), while as regards the general level of taxation in relation to profit Russia backtracks to the 124th place against the 105th place and the 88th place in 2012 and 2009, respectively. **Barriers faced by the business.** The situation with a start-up of business is somewhat better, though it is still far away from being favorable. As regards the number of procedures required for starting business, Russia holds the 88th place against the 97th in 2012, though it was rated the 27th in 2007. As regards the number of days spent on execution of documents, it is rated the 78th against the 104th place and the 57th place in 2012 and 2007, respectively. As regards the extent of foreign trade barriers it is rated the 124th against the 132nd place in 2012, as regards the level of customs tariffs – the 103rd place against the 106th place in 2012 and as regards the burden of customs procedures, the 124th place against the 132nd place in 2012. Even some improvements in the foreign economic regulation related, probably, with Russia's accession to the WTO do not ensure progress which can be assessed as normalization of the situation. As regards the extent of foreign property, Russia occupies the 132nd place against the 133rd in 2012.

In the group of factors related to the **labor market efficiency**, the estimate of the effect of taxation on labor motivation was introduced. As regards that criterion, Russia is rated the 122nd with the index of 3, that is, the worst value from the entire group of factors. Not surprisingly, if the situation with insurance contributions, including those for individual entrepreneurs is taken into account.

The group of factors related to **development of the financial market.** As regards availability of financial services Russia moved upwards from the 117th place in 2012 and the 119th place in 2011 to the 91st place in 2013. As regards availability of loans, it shifted from the 86th place to the 68th place (the 91st place in 2011 and the 107th place in 2010). However, as regards, reli-

ability of banks Russia is rated the 124th with the index of 4, which is better than the 132nd place with the index of 3.8 in 2012 and the 129th place in 2011 and 2010, but still regrettable.

And, finally, the group of factors related to **institutes.** As regards **protection of ownership rights**, as in 2012 Russia is still at the disappointing 133rd place with the lowest index which rose, however, a bit from 2.8 to 3, while as regards protection of intellectual property Russia moved from the 125th place to the 113th place with the index of 2.9. As regards **independence of courts**, the country moved from the 122nd place to the 119th place with the index of the mere 2.7. As regards **corruption**, particularly, illegal payments and grafts, the thing which one can hardly call the progress is expressed in Russia's advance from the 120th place to the 109th place (the index of 3.2), while as regards siphoning-off of state funds, an advance from the 126th place to the 113th place (the index of 2.5 is the lowest in that group of factors). **The state and state regulation of the economy.** As regards people's confidence in politicians, Russia is rated the 84th (the index of 2.7), while a year earlier – the 86th place; as regards, favoritism in decisions of government officials – the 111th place (2.6) against the 127th place earlier, as regards squandering of state funds – the 99th place (2.8) against the 103rd place; as regards transparency of the state policy – the 101st place (3.8) against the 124th place in the previous year (the 101st place is the best place in the years under review); as regards efficiency of the debate support system the 118th place (3) against the 124th place and as regards the burden of state regulation – the 120th place (2.9) against the 130th place. All the above aspects point to the fact that the situation has improved, but remains sensitive which factor reflects high but not critical mistrust of the authorities on the part of the business. **Protection of an individual.** As regards business's losses from crimes and violence: the 80th place with the index of 4.5 against the 90th place in the previous year, as regards business's losses from terrorism – the 112th place, 4.7 and the 119th place, respectively; as regards organized crime – the 111th place, 4.2 and the 114th place and as regards reliability of police services – the 122nd, 3 and the 133rd place. In accordance with the same scheme – parameters of the **level of corporate relations:** as regards companies' ethic behavior – the 101st place, 3.7 and the 119th place, as regards the level of standards of reporting and audit – the 107th place, 4 and the 123rd place, as regards efficiency of boards of directors – the 98th place, 4.3 and the 124th place, as regards protection of minority shareholders – the 132nd place, 3.3 and the 140th place and as regards protection of the interests of investors – the 100th place,

4.7 and the 94th place. Estimates of efficiency of boards of directors improved, while estimates of protection of investors' interests became worse.

As a result, it can be repeated that the most acute problems related to the business climate still remain the same for more than a single year: weak protection of ownership rights, lack of independence of courts and corruption at courts; corruption, excessive burden of state regulation, inefficient protection of an individual, low level of corporate culture, weak competition, maintenance of administrative barriers and high and inconsistent taxation. In other words, all those factors which make business feel unsecured about its future and determine the dominating motive to withdraw the capital abroad, rather than invest it in Russia are still in place.

The estimates of the main factors which impede doing business have changed a little. In all the years under review (from 2008), corruption was on the top of the list. In 2012, it accounted for 20.5% of the answers of managers of enterprises (it is to be noted that only one factor was asked to be named). It is followed by inefficiency of state bureaucracy (half as many answers) – 11.9%, availability of funding (10%) and the level of taxation (9.3%). In 2013, corruption accounted for 19.1%. It was followed by the level of taxation (13%), tax regulation (10.7%) and inefficiency of state bureaucracy (9.8). So, the business has started to experience more dramatically tax-related problems which situation is not surprising due to a short-sighted and inconsistent policy as regards insurance contributions.

Though the estimates of the main aspects of the business climate are quite disappointing, there is a question what factors were behind the explicit improvement of those estimates despite the fact that they are still far from those Russia used to receive in the recent past. The outputs of surveys of managers of enterprises used in formation of the index provide an idea about the opinion of those managers, but not the factors that opinion is justified with. So far, there is no explicit evidence of improvement in the institutional environment. One may suggest the effect of a number of factors. It is primarily hopes and expectations which play an important role in the economy. For example, an authoritative statement was made that the tax system was not going to be changed in the foreseeable future. The above statement is important not only in connection with explicit growth in a devastating tax burden on business, but also in broad terms: it is believed that business may adapt to any conditions provided that they are stable. Some hopes may be related to identification of large-scale corruption crimes (though investigations of those cases sooner raise more questions than provide answers) and the work

on road maps aimed at reduction of barriers which impede doing business.

However, discussion of the work on road maps at the government meeting on September 23 showed that the progress was far from being satisfactory. Only 83 measures (less than a half) out of 173 measures in respect of which the deadline took place were carried out, 37 measures were still in progress, while 52 measures (about one-third) failed to be fulfilled¹. The above road maps are aimed at upgrading of procedures which are reflected in the rating of the World Bank and *Doing Business*, an international financial corporation. As was shown in the previous report, though making of those procedures simpler is of utmost importance they do not cover the most painful aspects of the business climate related to protection of property, the state of the judicial system, corruption and other, so, even a breakthrough in that sphere may not be sufficient enough to have an effect on the situation.

Surveys on competitiveness were carried out earlier than important developments of the recent past took place: a verdict to A. Navalny was regarded by many as another abuse of power by the judicial system which situation resulted in a huge spontaneous meeting in the center of Moscow, election results of the Mayor of Moscow and the low voting turnout in regions where elections were held. The above developments reflect the extent of the risk of explosion of the sociopolitical situation in the country which situation cannot but affect the business climate. But the above developments were left beyond the frameworks of the Report in question. However, rational processes such as reduction of expenditures of the state budget and limitation of growth in prices of natural monopolies take place simultaneously.

With an insignificant number of managers of enterprises surveyed in Russia – about 100 – the dynamics of estimates can be influenced both by a relatively small change in their composition or a change in the opinion of a relatively small number of those managers.

Finally, though it is announced that in global competitiveness reports a year following the year of publication is analyzed, they actually reflect the reality with a delay. For example, if the 2013-2014 report came out in 2013 there was no statistical data available for that year, so the 2012 statistical data was utilized. That delay is explicitly shown in *Table 1*. The year 2009 was the most difficult crisis year in Russia, but apparent worsening of such aspects of competitiveness as the macroeconomic environment, the state of institutes and efficiency of the main markets started in 2010. So, the realities of 2013 can be adequately judged after the next report is published in 2014. ●

1 <http://government.ru/news/5951>