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The Global Growth Agenda
THE GLOBAL GROWTH AGENDA
Plenary Session

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Address by the President of the Russian Federation Vladimir Putin

Address by the Chancellor of the Federal Republic of Germany Angela Merkel

Moderator:

John Defterios, Editor, Anchor, CNN International

J. Defterios:

Good afternoon. Welcome to our keynote plenary session of this year's Forum. I am John Defterios, host of CNN's prime time global emerging markets programme, *The Global Exchange*, which runs here at 19:00 Russia time. First, let me introduce the President of the Russian Federation, Vladimir Putin, and the Chancellor of the Federal Republic of Germany, Angela Merkel. President Putin, Chancellor Merkel, thank you very much. This afternoon's plenary will explore the global growth agenda, and, unlike the long white nights that we are enjoying here in St. Petersburg in June, candidly, we have little visibility on sustainable growth, and this is further complicated, of course, by the likely shift of the Federal Reserve and its policy by the end of 2013. The latest World Bank forecast is pointing to an expansion, globally, of just 2.2% this year, with the OECD nations, the 34 that make up that group in Paris, a fraction over 1%. Collectively, the developing markets are earmarked for just over 5% growth, but interestingly, if you strip out China and India, that number comes down to just over 3.5%. So how well are the developing countries doing? The commodity-rich countries representing the first two initials of the BRICS, Brazil and Russia, are pegged for growth of below 3% in 2013. So obviously, this begs a crucial question for our plenary this afternoon. Is this the new normal: sluggish or nearly no growth in the eurozone, with record unemployment in the South, and sub-par growth in the rest of the world? We will answer that question and plenty more. Both leaders will give their keynote addresses, and we will have about a half hour for questions. Please expect at least half of them to come from the floor. We want this to be as interactive as possible in the time that has been allocated. We will also have special remarks from the Vice Premier, His Excellency Zhang Gaoli, who is in St. Petersburg. It will obviously be very interesting to hear his thoughts about the potential slowdown in China, with the context that its growth of 7.7% is perhaps not the 10% that we got used to in the last few years. He will join us after the first two keynotes this afternoon. Let us give a warm welcome to the President of the Russian Federation, Vladimir Putin.

V. Putin:

Good afternoon and welcome, ladies and gentlemen, friends.

Our moderator opened by talking about the global economy. In my speech I will, of course, say a few words about this. But I think you will understand if the head of the Russian state focuses on Russia's own issues and on how we propose to address them.

This year, the St. Petersburg International Economic Forum has a special meaning: it is one of the key events in Russia's chairmanship of the G20. Incidentally, I propose that we conduct next year's SPIEF on the eve of the G8 meeting, which will be chaired by Russia in 2014.

In our proposals for the G20 agenda, we are placing paramount importance on practical, systemic solutions that will heal the global economy and the global finance industry: heal it through development. This requires wide-ranging implementation of cutting-edge technologies that affect people's quality of life; investment financing (including, and especially, investment in human resources); social development; and the development of high-value-added industries, which will result in the creation of new, effective jobs. These are the high-priority issues of Russia's chairmanship of the G20. These are also the high-priority issues of our domestic social and economic policies.

The times call for resolve. It is no surprise that this phrase has become the slogan of this year's SPIEF. Our top priority in Russia is to create the conditions required for stable economic growth. For years, we have seen the price of our main exports rise rapidly and almost continuously. This has allowed domestic companies and the Russian Government to cover their high costs. We no longer have this advantage, just as we no longer have easy solutions: we cannot change the situation by waving a magic wand. The situation requires us to be highly disciplined, set the right priorities, and find a perfect balance between long-term goals and solutions to our current, often pressing issues.

Economic growth must stand on three pillars: increased productivity, investment, and innovation. We can only ensure progress in all three areas by cutting financial, management, and infrastructure costs; by developing human capital; and by creating competitive business conditions in the full sense of the word. Another condition required for growth is what I would call a favourable economic

environment: macroeconomic stability, further reduction of inflation, a responsible budget, and compliance with the budgetary rules we have introduced and which are in force today. I will clarify for our foreign guests: the essence of these budgetary rules is to channel the surplus funds which are flowing into our economy as a result of favourable global markets and high energy prices into the Reserve Fund.

Let me stress that our chosen strategic course will remain unchanged. This is especially important, and I would like to emphasize this point further. We will stay this course regardless of staff changes at the Central Bank or in the economic departments of the Presidential Executive Office and the Government. Today, incidentally, is Ms. Nabiullina's last day with the Presidential Executive Office: on Monday she will take up the post of Governor of the Central Bank. I would like to thank her for the work we have done together in the Russian Government and in the Presidential Executive Office.

Ladies and gentlemen, as a result of significant efforts, and thanks to responsible financial policies, we have managed to significantly lower inflation. In the past, as you well know, inflation in Russia sometimes exceeded 30%. Two years ago, it reached a historical low point of 6.1%. Last year, it increased slightly; this year, it increased again to 7.5%. Our economy can handle these numbers. But we still have a great deal of work to do in this area. We have to create basic conditions for the long-term investment required to rebuild the structure of the economy.

As I mentioned before, inflation is still high, and we intend to work towards reducing it further. Today, inflation and inflationary expectations are highly dependent on the so-called non-monetary factor: in other words, on the tariff component of inflation. Accelerated tariff increases have become an independent and significant factor in inflation growth, and have produced an economic slowdown, an increase in costs, and a non-competitive manufacturing industry. Obviously, tariffs cannot continue to rise at the same rate as before. In this respect, I would like to inform you that we have made a decision to limit increases in the regulated tariffs of infrastructure monopolies: they cannot rise above the past year's actual inflation rate. We will lock in this procedure for five years beginning in 2014.

We all know full well, however, that the end price paid by the consumer or by the consignor for things like electricity is determined by more than regulated tariffs. I have asked the Government to develop a mechanism for keeping the consumer end price at acceptable levels in line with established parameters and principles. Furthermore, when setting tariffs, we must take consumer opinion into account. To ensure that these are not simply empty gestures, the procedure must be stringently regulated. To achieve this, I propose the creation of consumer councils within the Federal Tariff Service, infrastructure monopolies, and regional energy committees. I have asked the Government to draft the appropriate proposals in conjunction with the business community.

I would like to emphasize that our infrastructure monopolies have ways to save money. Each of these companies must implement a programme to cut costs and increase productivity. We must invest wisely, and be intelligent about attracting financing for our investment programmes. But we must not allow a cap on tariffs to have a negative impact or reduce investment in infrastructure. Our key objective over the next few years is to remove the many infrastructure limitations which are literally choking our economy, preventing entire regions of the Russian Federation from unlocking their potential.

What are we proposing in this respect? We have long been discussing the option of using our financial reserves. We have several types of reserves. One of these is the National Wealth Fund. These resources must be used for the benefit of Russia's economy and future generations. We cannot spend them on minutiae or waste them on defunct programmes. We must use them for projects that will change the face of our country, and open up new possibilities for its development.

That is why we have made another very important decision: to invest RUB 450 billion in viable infrastructure projects, naturally on a repayment basis. We will invest up to half of the National Wealth Fund in domestic projects. The key condition of this investment is that the private sector must evaluate the viability and effectiveness of projects: in other words, the private sector must co-finance the project. I know that investor interest in infrastructure projects is very high,

especially if the Government is willing to offer guarantees, minimize risks, and serve as a co-investor.

My meeting with heads of the world's largest investment organizations yesterday served to confirm this. I see some of them are here today. Yesterday, we had a long, detailed discussion on this subject. Today, I am ready to invite you to act as our partners in the first three of these projects. As I mentioned before, these projects will involve investments by the National Wealth Fund.

I shall say a few more words about these projects. The first is a high-speed railway that will connect Moscow and Kazan. It will become, in effect, the pilot section of a railway line that will connect the capital with Volga Region and the Ural Economic Region. The second project is the Central Ring Road, which will be built virtually anew in Moscow Region and New Moscow. Sections of the highway will be built 30–70 kilometres from the Moscow Ring Road. The Central Ring Road is, in effect, a brand new project that will change the face of transport logistics within European Russia; link the country's central regions, giving them new impetus for growth; allow us to relieve Moscow's traffic congestion; and improve the transport system and the environment within the capital.

Friends and colleagues, the Russian participants in today's meeting understand what this means for people living in central Russia. Moscow and Moscow Region alone are home to approximately 20 million residents. If we add the nearby regions, which will also undoubtedly make use of this infrastructure, the number of people and economic players involved will increase manifold.

Finally, we intend – this is the third project – to drastically modernize the Trans-Siberian Railway in order to increase its carrying capacity. I should note that the Trans-Siberian Railway is one of the longest railways in the world: it is almost 10,000 kilometres long. Direct rail travel across Eurasia will become a key transport artery linking Europe and the Asia-Pacific region. It will serve as a powerful impetus for development in the Far East and Siberia. Our transport infrastructure is an excellent match for the fast-growing Asian markets.

All these projects are part of our vision for Russia's cooperation with these markets. Let me repeat: for our part, we are ready to invest in this, and are interested in finding dependable, strong, ambitious partners. I have asked the

Russian Government to develop the specific mechanisms we need to implement these projects in the nearest future. Let me stress again that these are economic projects: carefully designed documents, not empty gestures.

I would also like to add that the new Far East pipeline infrastructure, which links up with China and the Pacific Ocean ports, allows us to undertake large-scale projects on the Asia-Pacific markets. This infrastructure has already enabled one of our leading companies, Rosneft, to sign a large contract with the China National Petroleum Corporation to deliver up to 46 million tonnes of oil annually for a period of 25 years. Based on the current market conditions, the contract's estimated value stands at an absolutely unprecedented USD 270 billion. The media have mentioned a different amount: USD 70 billion. This is just the upfront payment.

Another important project that is opening the Asia-Pacific markets up to Russia is the construction of the Amur River railway crossing. We signed the corresponding agreement with our Chinese friends right here in the margins of the Forum. I will note that projected capacity of the bridge at the first stage of the project will be in excess of 5 million tonnes of cargo annually, with a future increase to 20 million tonnes.

Ladies and gentlemen, domestic investors must also provide a resource base for the country's development programmes. To meet this challenge, we need trust in the financial sector; for that, we need an adequate regulatory system. The mega-regulator will have the job of regulating all financial institutions: it will oversee the work of banks, as well as investment and retirement funds. This mega-regulator will function as part of the Central Bank of Russia.

In the near future, we will create a retirement savings insurance system within the Deposit Insurance Agency. Once we have a reliable system for securing deposits, we will be able to lift the current limitations on investing retirement funds in long-term projects. We must also determine what portion of pension funds will be used to invest in securities issued by self-sustaining infrastructure projects. I gave you the amount earmarked by the National Wealth Fund for three projects: RUB 450 billion. However, we realize that this is not nearly enough to implement these projects: this is only the startup capital. The second stage of the

projects will require the use of retirement savings, on the condition that they are secured; in addition to, as I have already mentioned, investor resources. As these projects grow, we will look for other sources as well.

We will continue to develop our stock market, bringing it into compliance with all international requirements. We are already taking concrete steps in this direction. Today, the Moscow Exchange is fully prepared to handle major stock flotations and privatization operations. I repeat: we will be privatizing state-owned assets using domestic platforms. When VTB issued its shares, it demonstrated that this is not only possible, but practical. The issue was quite successful: we were able to organize this process in the proper manner.

At the same time, we will be privatizing gradually, focusing on the quality of each transaction, and selling our assets at truly profitable, fair prices. At the same time, we will be increasing the transparency and openness of our public companies, regardless of their ownership structure. We will be creating mechanisms to protect financial shareholders, and improve the quality of corporate management.

I would like to talk separately about state-owned companies. Investors often use them to extrapolate the quality of management of the country as a whole. It is no secret that the results are not always favourable. We intend to strengthen the state's regulatory role in the companies it owns, and establish clear management effectiveness indicators, including company capitalization and returns. Based on how well these companies meet our target indicators, they will be either rewarded or penalized. I am now also talking about staff-related decisions.

Obviously, no amount of regulation, no number of effectiveness indicators, will replace the most important factor: competition. Regardless of the company's ownership structure, we cannot allow preferential treatment in a normal market economy. We must create a competitive environment on our product and services markets, both domestic and international, and apply it to both private and state-owned companies.

We propose to take the first step in this direction in a sector where competition once seemed impossible, and to begin to gradually remove limitations on liquid gas exports. The new opportunities awaiting us on the Asia-Pacific markets,

along with the fact that consumption of liquid natural gas (LNG) is expected to double, allow us to plan for the gradual liberalization of LNG exports. This will create the conditions necessary to fully tap our shelf and offshore gas extraction potential.

I am happy to note that we have signed LNG export agreements right here in the margins of the Forum. For example, one of our companies, Novatek, has signed a cooperation agreement with the China National Petroleum Corporation as part of the Yamal LNG project. Under this agreement, China will purchase a 20% share in Yamal LNG, and the parties will sign a long-term contract to supply liquid natural gas to China. Gazprom is also preparing to sign a contract to supply gas to Japan and China. These contracts will be followed by sweeping investments in shelf extraction, undertaken in conjunction with global oil and gas industry leaders such as Exxon, Statoil, and Eni, as well as investments in production localization and cutting-edge equipment, undertaken jointly with such global technology leaders as General Electric.

Ladies and gentlemen, taxes play an important role in determining the volume of investments, be it a choice between different countries or different economic sectors. Taxation policy must also work to promote development, encourage investment in the modernization of existing Russian manufacturing facilities and the creation of new ones, and stimulate the creation of high-quality jobs. Therefore, when we devise our taxation policies, we are guided by the fact that even strict budgetary limitations are no reason to increase the tax burden on private companies.

Over the past year, we have significantly improved our tax administration procedures. Russia has taken a dramatic step forward in the area of tax administration: we shot up 30 points in the global rankings, moving from ninety-fourth to sixty-fourth place and overtaking many OECD 'old-timers'. But we have no intention of resting on our laurels. For example, we must reconcile our tax and accounting procedures as far as possible. We have often discussed this with representatives of the business community, and I agree with their opinion that we must move in this direction.

We will continue to create tax incentives for investments, in both capital assets and securities. I am, of course, talking primarily about Russian companies, as well as about our Far East projects. I will add that new movable assets owned by legal entities have already been exempted from taxation.

It is no less important to draw individual investors into the capital market, and to create new tax incentives for personal long-term investments, allowing individuals to profit from our economic growth. We are working on these measures right now. At the same time, we will battle the erosion of our tax revenue caused by companies moving their assets offshore. This is being done on a national, as well as on an international, level. Yesterday, I met with representatives of the Y20 Youth Summit. The suggestions for tackling the offshore problem offered by these young people are original and quite strict. I believe we could use a great many of their ideas.

During the G8 meeting, we discussed this problem and the need to 'de-offshore' the global economy at great length with our colleagues. Ms. Merkel took part in these discussions. One measure we plan to implement to combat the use of offshore tax havens is a series of special bilateral agreements between Russia and offshore and low-tax jurisdictions, which will ensure a higher level of tax information exchange. More and more of these agreements are being signed around the world.

Our domestic legislation is already being brought into compliance with the requirements established by the OECD and the Financial Action Task Force (FATF). By the way, Russia will soon preside over this Task Force. The State Duma has already approved the relevant law, and it will be signed in the near future.

Significant changes are being made to criminal, banking, and taxation laws. These changes are designed to prevent the laundering of illegal profits. We are significantly strengthening monitoring of, and accountability for, these kinds of actions. Now, lending organizations will be required to identify clients, disclose information about their clients' account beneficiaries, and, if any violations are discovered, refuse to provide further banking services.

We are also introducing tax monitoring mechanisms for these operations. These mechanisms stipulate that information about personal bank accounts must be disclosed to the tax authorities. As you know, we have signed corresponding amendments to the Tax Code, and have agreed to provide this information to our foreign partners: naturally, on a reciprocal basis.

I have a few more words about the banking system. Accessible bank loans are key to an active business investment environment. This issue is especially vital for small and medium-sized companies. Here, we must also implement a wide range of measures: we need to improve refinancing of the banking system, take steps to foster competition in the banking sector, and expand state-backed guarantees for small and medium-sized companies. We must also allow banks to lower their own risks, costs, and administrative expenses, using methods such as the abolition of redundant reporting oversight procedures.

We must pay particular attention to the protection of creditor rights. Often, banks cannot recoup their funds when a borrower goes bankrupt; what is more, they also find themselves in the position of debtors. At the same time, we must provide reliable protection of consumer rights in the financial and insurance sectors. This applies first and foremost to people, many of whom do not always have a great deal of financial knowledge. I will mention that literally the other day, we established the People's Front for Russia social movement. I propose that this movement serve as the platform for the protection of borrower rights. I have also asked the People's Front to take charge of public oversight of purchasing by state and state-owned monopolies. It must ensure transparency regarding the way in which resources designated for high-priority objectives are being used.

Ladies and gentlemen, our key priority is to improve the country's business climate. Everyone has to work towards this goal: from small-town mayors to federal ministers; from rank-and-file police officers to the head of the law enforcement agency.

Today, the quality of management at every level of government is fast becoming a critical factor in our development. That is why we are setting goals and objectives for state agencies and for officials at every level of government. These goals and objectives are clear and easy for the public to understand. As in the

business world, the results of this work are evaluated on the basis of personal effectiveness indicators. I would like to stress that our domestic business climate, as well as the country's investment image as a whole, is entirely dependent on our joint efforts and motivation.

We do not divide people who set up companies and create jobs in Russia into domestic and foreign, into 'us' and 'them'. We place great importance on people who get the job done, and we strive to create not simply good, but the best working conditions for those people. We will do everything we can to ensure that working in Russia is profitable, convenient, and safe. We expect that the comprehensive set of agreed business climate improvement measures will be implemented in full.

We have done a great deal to eradicate the accusatory bias in the law enforcement and judiciary systems in order to eliminate the need to open criminal proceedings because of a business dispute. We have done extensive work in cooperation with the business community and Parliament to humanize our criminal laws. To ensure that disputes between individuals and organizations, as well as disputes with state and local government bodies, are treated equally, I am proposing that we merge the Supreme Court of the Russian Federation and the Supreme Commercial Court. This will require the introduction of amendments to the Russian Constitution. This is a serious issue. We must analyse and weigh things very carefully. I am asking the Presidential Executive Office, representatives of the judiciary, and members of Parliament to unite in working towards this goal. I would like to ask you to prepare to consider this issue during the autumn session. The draft of the bill will be submitted to Parliament in the near future.

The institution of the Ombudsman, who is authorized to protect the rights of entrepreneurs at the federal and regional levels, has been established in Russia. The business Ombudsman will have effective powers to advocate for the interests of the business community in its interactions with state agencies. These powers, including the power to suspend legislation issued by local governments, have been defined by law. By the end of the current year, public organizations, including business associations, will have the right to file class action suits on

behalf of an unlimited number of parties and their members. In effect, along with the institution of the state Ombudsman, we are creating an organization of public ombudsmen consisting of influential business associations.

I would like to tell you about another policy decision. A month ago, as you know, we met with representatives of the country's leading business associations. It was suggested during that meeting that perpetrators of so-called economic crimes receive amnesty, especially since Russian law has changed drastically in recent years, and many people would never have been convicted had they operated under current legislation.

Of course we should not be hasty in offering amnesty. We cannot allow armed robbers, counterfeiters, criminals who conned people out of their flats, and others who have committed actual serious crimes against the state, an individual, or property, to be released into society. We especially cannot acquit people whose crimes involved the use, or even the threat, of violence. The draft amnesty bill has been improved by the business community and by State Duma deputies. I think we can accept this draft. I have asked the State Duma to consider and approve it. I expect this to happen within a short time frame, before the summer break.

According to this draft, the amnesty will apply to first-time offenders who have committed a crime as part of their business activities, and who have already paid, or agree to pay, damages and losses to their victims. These individuals will be acquitted. I must stress that in addition to upholding justice, in addition to being a humanitarian act in relation to specific entrepreneurs, this decision to offer economic amnesty also offers an opportunity to 'reboot' many aspects of our social relationships, improve our law enforcement and judiciary systems, implement our plans to drastically expand opportunities for entrepreneurial activity, and reinforce our people's trust in business as an institution. I am convinced that our nation can only evolve if there is public respect for private property and for values such as economic freedom, entrepreneurship, and success.

Ladies and gentlemen, in closing, I would like to revisit the central issue: the issue of human capital. We are implementing a comprehensive project to save

our nation, investing resources in individuals and their development. We are paying particularly close attention to demographic and healthcare programmes. We are making significant improvements to social policies and to education at every level, including professional education. We expect to face demographic challenges in the next few years. But most importantly, we understand that the social dimension of our economy will play an ever-increasing role; therefore, abstract figures like GDP and manufacturing growth, important as they are, cannot be the be-all and end-all of our policies. We need to see real changes in the lives of each individual, each family. That is what we are working to achieve. I invite you all to join us in this work. Thank you very much for your attention.

A. Merkel:

Good afternoon President Putin, Ministers, ladies and gentlemen!

I am very happy to be participating in this Forum, which is an extremely important event connecting political leaders and the business community. The Forum raises questions about globalization that are of great interest to me. Five thousand participants from more than 70 nations have come to the Forum. This year, the Forum has a special meaning, presenting special events dedicated to Russia's G20 Presidency. We will be back in St. Petersburg for the G20 Summit. Ladies and gentlemen, our most important objective is a stable global economy. The 2008–2009 financial crisis taught us that the economies of various regions are closely interrelated. Heads of states and government leaders began to meet as part of the Group of Twenty. These meetings have allowed us to introduce political content into the globalization process. Globalization changes people's lives in every region of the world. And people, especially those who come up with innovative approaches and meaningful projects, can affect this process. We must create a political environment that will promote this, and the only way we can do that is through cooperation between the world's largest economies.

I place great value on the fact that Russia is paying such close attention, as part of its G20 Presidency, to promoting economic growth and developing international trade. When Russia joined the WTO, it expressed its commitment to the basic principles of international trade. The past has taught us all that

following these principles has not always been easy: all countries have played around with protectionism from time to time, instead of working to remove barriers to trade. Even today, some countries show a propensity towards protectionism. I believe that during the G20 Summit in St. Petersburg, we must demonstrate our belief in the principles of free trade.

All of us – I am speaking on behalf of Germany and the European Union – must actively foster a competitive environment. During the G8 Summit in Northern Ireland, we announced our readiness to enter into talks with the United States to create a free trade zone. It is crucial that we reach an agreement: the European Union is the world's largest domestic market, while the United States is the world's largest economy. But we know we are facing very difficult negotiations.

The EU also wants to advance in terms of removing barriers to trade with Russia. The President of Russia said today that Russia also wants the same thing, and that it intends to maintain a good relationship with the West, the European Union, and the Asia-Pacific region.

The Hannover Messe Trade Show gave us an idea of Russia's economic potential: at this year's event, Russia served as a partner country. Russia's economic development has a huge impact on trade between Germany and Russia. Germany is ready to assist Russia in achieving greater economic transparency and diversification. We want to be a reliable partner to Russia. In 2012, the volume of trade between our countries reached record levels: over EUR 80 billion. In other words, it has tripled in the last decade. We enjoy fruitful cooperation in such industries as mechanical engineering and the automotive industry in particular, with German investors making great strides in this area. In addition, Germany greatly values our energy partnership: with changes in our energy policies, natural gas will play a major role in our energy consumption for years to come. We recently opened two new branches of the Nord Stream pipeline: the pipeline of the future. Not everyone in the EU was in agreement on this at the beginning. But today, we can say that this pipeline is a joint project between the EU and Russia. Russian companies Gazprom and Rosneft are active within Germany. Our companies E.ON and Wintershall are playing a major role in developing the Yuzhno-Russkoye field: Germany is ready to offer its

technologies to support this project. We are also ready to work together on issues such as the exploration of new renewable energy sources and the promotion of better energy efficiency. These issues will be raised during the ongoing intergovernmental consultations between Germany and Russia.

I came here with a German business delegation. This underscores the importance of our economic decisions. Germany's Committee on Eastern European Economic Relations, chaired by Mr. Cordes, focuses a great deal on these issues. I was happy to hear the Russian President's words in this regard. Large German companies, as well as medium-sized companies which also sometimes occupy leading positions on the global market, are ready to play an active role in Russia. But this requires a strong legislative foundation, transparency, and all the other factors that have been discussed today. As was said earlier, every Russian mayor is asking the President to ensure that everyone follows free market principles. The economy can function well only when everyone is committed to the principles of private property, and only in the presence of a clear and strong legislative foundation.

Germany is also ready to invest in the human capital mentioned just now by the President. Russian young people need good education. Germany wants to partner with your country in this respect as well. As the Federal Chancellor of Germany, I place great importance on the fact that our country's economy is the largest in the EU. But our long-term success depends on the success of the EU's economy as a whole. When the European currency found itself in a critical situation, Russia confirmed its unequivocal faith in the euro. The EU countries, in turn, expressed a strong political will to save the euro. After the global financial crisis, some EU countries saw the confidence of global investors plummet: right now, they cannot be sure that those countries will be able to repay their debts. The reasons for this varied from country to country, and to deal with the fallout of the crisis, we had to find the specific reasons behind each individual case.

Germany, like many other EU countries, faces serious demographic challenges. To tackle the existing challenges, we will in future have to find a balance between economic growth and budget discipline; otherwise, foreign investors will have no confidence in the stability of our economy. Stable economic growth and

budget stability will be among the main topics on the G20 Summit agenda. All of the largest G20 countries need to address these issues. I do not believe budget discipline is incompatible with economic growth: economic growth makes it easier to eliminate budget deficits.

This is why the countries of the eurozone have adopted a range of measures, which I would like to briefly describe here. First, each country has made a commitment to carry out structural reform in order to maintain a competitive edge on the global market. Ten years ago, people referred to Germany as the 'sick man of Europe'. We carried out reforms, passed demographic and budget consolidation measures, and regained our competitive economic edge. In addition, we decided to invest a great deal of resources in education and science. We subsequently signed the European Fiscal Compact and created mechanisms to save the euro.

Mr. President said that the main condition required for further growth is more accessible credit for small and medium-sized companies. Some European Union and eurozone countries are facing major challenges in this respect. Therefore, we have decided to drive forward work on the creation of the Banking Union and the establishment of pan-European banking oversight agencies. This will help our banking institutions to regain the trust of our population. Only through these measures will we be able to create good credit conditions for the 'public economy'. I also believe that we must coordinate our economic activities better within the currency union, and have a clear understanding of the factors on which our competitive edge depends. We must not allow a situation in which some countries invest very little in science and education, while others make significant investments in these areas. We must not allow a situation in which the level of spillover costs of production differs greatly between EU countries. Cost control is also crucial to the EU's harmonious development.

High unemployment rates, particularly youth unemployment rates, present a serious challenge to eurozone countries. Young people have a harder time staying employed in difficult economic times. Germany wants to lead by example in terms of eliminating youth unemployment. But we must answer the question of how Europe proposes to earn money. EU member governments and the

European Commission must work towards reducing bureaucratic procedures and improving their competitive edge, and address the truly important issues. Some countries, Germany included, have a great need for labour, while others suffer from unemployment. If we truly want to build a strong union based on a single currency, we must ensure the mobility of our workforce.

Russia and the EU, as well as Russia and Germany, must build a close strategic partnership, which will help all of us to overcome these difficulties. I am happy to hear that the Russian Federation is ready to meet economic challenges. We will be a dependable partner to Russia. We have rich infrastructure and manufacturing experience: manufacturing accounts for approximately 25% of Germany's GDP. We are always ready to offer advice on investment and other economic issues.

Thank you for giving me this opportunity to visit the Forum. I wish Russia success in its G20 Presidency. We will continue our dialogue focused on economic growth. The EU is ready to play its part in this growth. We know that there is a great deal of work ahead of us, and we are approaching it with great resolve.

Thank you again.

J. Deferios:

Chancellor Merkel, President Putin, we look forward to the questions and answers, and the participation from the audience.

As I noted in my opening remarks, we have a special appearance from the Vice Premier of the People's Republic of China, Zhang Gaoli, to give us some insights on the Chinese economy at this stage; he will participate for a period of 10 to 15 minutes and go back into the audience and then we will have our question and answer session here as well. Please welcome the Vice Premier of the People's Republic of China.

G. Zhang:

President Putin, ladies and gentlemen, please allow me to congratulate you on behalf of the Chinese Government on the successful opening to the Forum. This

year's Forum provides a platform for a serious exchange of opinions on global economic stability. This is a very urgent issue.

This year has seen positive changes in the global economy. However, numerous factors are still giving rise to instability and uncertainty, and there are still not enough drivers of economic growth. That is why we must join forces as much as possible – expand cooperation, foster camaraderie – and do this as soon as possible, in order to rebuild and improve the global economy. I would like to propose several measures in this respect.

First, we must continue to coordinate our macroeconomic policies. We need to maintain macroeconomic policies aimed at economic stabilization, growth, and helping people to find jobs. We must take more effective steps by fostering constructive and open cooperation, seeking to avoid inflation, and maintaining international financial stability.

Second, we must take steps to create a fair, transparent, and highly organized global economy. Conditions that promote trade liberalization are in every country's interests. We must work together to combat various forms of protectionism, and we need to settle various disputes through dialogue and coordinated action, in order to ensure that international trade is governed by the principles of freedom, openness, justice, and rationality.

Third, we must more actively involve entities like the G20 in providing global economic regulation. We must implement effective reforms in the sphere of global economic management, and increase the presence of developing countries and emerging markets within international financial structures. As a result, the G20 will play an even larger role in stimulating global economic growth.

China and Russia, the world's leading emerging markets, are making great efforts to create a just and rational international economic order. President of the People's Republic of China Xi Jinping's visit to Russia in March of this year was of great significance for the stability of global economic development. During this visit, he and President Putin arrived at a mutual understanding on issues of bilateral cooperation. Currently, both countries are actively working on implementing the results of this meeting, with an accent on deepening and

expanding our cooperation on major projects and cooperation between the regions of our countries in areas such as energy, investment, finance, trade, agriculture, science and technology, and aviation and space exploration. This year, we have already reached agreement on additional oil deliveries from Russia to China. We are continuing to work together in the gas sector. All this will provide an additional boost to global economic growth.

Ladies and gentlemen, China is the world's largest developing country. China's stable and healthy economic growth has great significance for global economic growth as a whole. China has set itself the goal of building a strong middle class, thereby fulfilling the dream of a Chinese national renaissance. To do this, we will increase the transparency of our economy, aspire to create a unified market, establish clear and just market interaction rules which will apply equally to everyone, and create a favourable investment climate. We will stimulate natural selection among companies with various ownership structures, including international companies. We will boost market activity; look for internal incentives to economic growth; carry out the industrialization, informatization, urbanization, and modernization of the agricultural sector; and take measures to increase domestic consumer demand.

Our efforts will primarily be directed towards developing appropriate cooperation methods to transform the economy, which will allow us to increase the quality and rate of economic growth, and ensure stable and healthy economic development. Currently, China is experiencing steady economic growth. In the first quarter of this year, our GDP grew by 7.7%. Our prices are stable, and six million more people are now employed.

Although we experience difficulties and face challenges from time to time, China has a massive market and huge development potential. We expect our imports to reach approximately USD 10 trillion in the next five years. We have earmarked USD 500 billion for international investment. More than four million Chinese citizens travel abroad every year. We will remain steadfast on the path of global development. We will defend the legal rights and interests of foreign investors and in the process help to restore and advance the global economy.

We thank all countries and companies that support China. Thank you for listening.

J. Defterios:

That was Zhang Gaoli, the Vice Premier of China, with his remarks on the expansion of the economy and plans to continue the push forward. Before we get started here I would like to alert those with the microphones to see if we could have one in this aisle here, one right near the front even if you need to take a seat, and then one microphone right there down the aisle. I want to go to the questions on the floor as soon as possible. Mr. President, and host of the St. Petersburg Summit, your home town, that we need to recognize as well, I would like to ask the first question from the podium and then I will take a seat. Both of you, Chancellor Merkel and President Putin, addressed the meeting of the G8, you have the chairmanship of the G20 in September here in St. Petersburg. At the G8, there is a great deal of focus on global trade and the possible US-EU alliance, there is a great deal of discussion on offshore taxation, something you talked about in your opening remarks, and we know the differences on Syria. I would like to talk about foreign policy a little bit later. What is the key priority, though, for you at the G20 in September? There was an absence of discussion about how to boost global growth at this stage. Do you change that priority now for the G20 or do you have a different priority in mind, sir?

V. Putin:

As Madame Federal Chancellor will tell you, we spoke about continuity in our work when we met at the G8 Summit in the United Kingdom, building primarily on the achievements of our Mexican friends and partners at the last G20 Summit in Los Cabos. After our meeting in the UK, we focused our attention on specific aspects of global economic development, which will be reflected in the agenda for the St. Petersburg G20 Summit in September of this year.

What did we discuss? We discussed the creation of more favourable conditions for global economic development. What does this entail? It entails improving the tax system, which I have already touched upon today, and combating tax

offshoring within the global economy. As we know, offshoring is one of the negative factors which led to the financial, followed by economic, crisis of 2008–2009. We discussed the joint efforts we would need to make to increase the volume of global trade, taking into account the fact that it has shrunk somewhat over the last year. We discussed the harmonization of our positions on this and certain other issues that are fundamentally important to global economic development.

Of course we discussed the situation in each of our countries: the United States, the eurozone, and Russia. Each G8 leader talked about the steps his or her government is taking domestically. President Obama talked about improvements to tax legislation designed to confront the threat of offshoring. These factors have naturally cleared the ground for joint work and discussion of the most pressing issues which affect both parties.

We also talked about foreign policy issues: the situation in Syria and other problems. The current situation in Syria is probably one of the most pressing issues today. We had an open discussion on the subject, in which all those at the Summit took great interest. We reasserted once again – and this was reflected in the final declaration – our common concerns and goals: to end the violence as soon as possible; to create conditions for renewed political dialogue between all warring sides; and to bring the groups in active opposition to each other, including armed opposition, to the negotiating table. We agreed to convene the Geneva 2 Conference in the near future, based on the principles we developed during the last meeting in Geneva, in order to encourage the warring sides to enter into dialogue and work out a positive solution.

I want to stress that the discussion of this and other subjects were the focus of great interest and took place in an atmosphere of partnership. In the course of this discussion, participants voiced various opinions. But I was happy to see that despite the importance and complexity of the issues on the agenda, we always looked for ways to reach a compromise, and managed to come to a consensus on virtually every issue.

J. Deferios:

Mr. President, I was going to talk to you about foreign policy a little bit later, but since you brought up Syria, just a quick follow-up if I may and then I will go to Chancellor Merkel thereafter. Is it possible to have a Geneva 2 discussion taking place when Russia, on one side, is providing arms, and you are very clear about that, to the Assad Regime, the United States has chosen the other side, and we have division amongst the G7, overall, on where to proceed and what is the tactical way to go forward. So, is it possible to have a Geneva 2 when you have that sort of division? Arms going in, support from Iran on one side, and the United States picking the other side, sir?

V. Putin:

Let us get back to weapons. I spoke on this subject at a press conference in the UK, so I can only repeat what I said before. The Russian Federation has not violated a single international law. We supply weapons to the acting lawful government of Syria within the limits of current international law and based on open and transparent contracts.

As far as the opposition is concerned, I must remind you that it has long been receiving weapons from abroad. We will not mention the origins of these weapons. But obviously, without foreign weapons, the current situation in Syria would be simply impossible. The opposition is receiving money and weapons from abroad, and forming highly-trained, armed groups. I cannot claim that this is exclusively happening abroad, but it is occurring there to a significant degree. In the meantime, Europe and various international bodies, such as the UN, have adopted decisions banning the supply of weapons to non-government entities, especially those in conflict zones. On this issue, we do have certain differences of opinion with the United States, for example. But I can tell you that Russia and the United States are not the only countries which cannot agree on this subject. The US and Russia are not the only ones with a stand. All of the G8 members are independent states, and their leaders deal with politics on a global scale. Each has his or her own opinion on the current situation in Syria, as well as in other regions of the world. To present the situation as a standoff between Russia and the US is to oversimplify complex global processes.

In fact, I will repeat what I said in the UK. I have a hard time understanding why anyone would supply weapons to unlawful armed groups in Syria when we do not entirely know who they are. The US Department of State has designated one of the key Syrian opposition players, Jabhat al-Nusra, a terrorist organization, and officially recognizes its connection to Al-Qaeda. So why would anyone supply weapons to these opposition forces? Where will these weapons end up in the end? What role will they play? We know that at least 600 people from Russia and Europe are currently fighting on the side of the opposition. Where will these weapons end up? We have no answers to these questions at this time; and when we ask our partners, they have no answers either.

Therefore, things are not as simple as we might want to imagine. But we believe our position is justified and sound. We believe a long-term solution to the problems, which have certainly been accumulating in Syria for decades, can only come from the Syrian people. For our part, all we can do is create the conditions that will help to foster these agreements.

J. Deferios:

Thank you for your response. Chancellor Merkel, you talked about the tendency for protectionism, and we saw that during the financial crisis in the last three years. Is it realistic to suggest that the European Union and the United States could enter into serious, genuine talks with the resistance that we are seeing from France, in the media sector and the film sector, and the fact that we are not certain that the Conservative Party in the UK actually wants to stay in the European Union? It does not seem like the best conditions to form a concrete path forward for trade.

A. Merkel:

Thank you very much.

I would like to revisit the issue of Syria. During meetings like the G8 Summit, we try to present different viewpoints, and to show that different viewpoints exist: otherwise, things would be very difficult. Despite all our differences – for

example, the differences between Germany and Russia – the Summit yielded positive results, since we stated what was important to us.

First of all, we want to make sure that none of the parties supports terrorism; secondly, the UN must conduct an investigation into the use of chemical weapons; and thirdly, we want to see a transitional government supported by all sides. If we dedicate all our efforts in the coming weeks to reaching these objectives, we will have a chance to prevent and alleviate the pain and suffering of millions of people. We will be discussing this further.

Next, I am grateful to the OECD for presenting so many ideas on how to combat tax evasion at a global level. The G8 approved these ideas, and we hope that the G20 will also approve them during the St. Petersburg Summit in September. I believe that we should not have some people paying extra taxes because others take advantage of a situation to evade taxes: this creates social tensions within countries. We will not be able to convince people that everyone – not just a select few – benefits from economic growth.

When it comes to the US, the EU has already signed a great many free trade agreements, with Korea for example, which do not touch upon the issues of culture and the media. So for the EU, these clauses are not compulsory. When we began talks with the US, we kept in mind that the media and the film industry are important for the US. But France took a hard-line stance on this issue. Some people in Germany, as well as in the European Parliament, felt the same way. I think we were wise not to walk away from the negotiating table. Instead, we said we would have to face this issue when it came up.

When it comes to the UK, we unequivocally believe that it is part of the European Union, and that its presence enriches the EU. The UK sometimes criticizes the EU. I agree with some aspects of this criticism, and disagree with others. But when the EU becomes too slow and mired in bureaucracy, the UK is an excellent engine. At times, we have to compromise, and negotiate with our British partners on the points you mentioned. But I must also note that I completely disagree with the claim that the UK is stuck between the US and Europe.

J. Deferios:

Okay, I have one quick follow-up question for both of you because this is an economic summit so I need to ask an economic question to each, and then I am going to go directly to the floor. First, for President Putin: we saw a very serious reaction after the US Federal Reserve suggested that the policy may be adjusted by the end of 2013 in terms of the bond purchases. A very violent reaction in stock markets around the world, but particularly, in emerging markets. What counter measures are needed by Russia, with a new Central Bank Governor, to boost growth if there is that much worry about Federal Reserve Board policy, particularly, in a country like this?

V. Putin:

I talked in my speech about the steps Russia can and must take to drive economic growth. I do not think I need to repeat myself.

With regard to the reaction to Mr. Bernanke's statement, first of all, we fully expected it. A correction had to happen sooner or later. We cannot endlessly pump the economy full of liquidity while we fail to address the fundamental issues that are key to fixing the situation. President Obama managed to do a great deal of excellent work on the 'fiscal cliff'. This is undoubtedly a great victory for him on the domestic front, a great economic victory. But it is probably not right that the entire world should exist in constant fear of problems, living from fiscal cliff to fiscal cliff. Fundamental decisions must be taken. Sooner or later, the Federal Reserve had to make this correction. This is nothing unexpected: I think it was the right decision.

It is essential to move gradually away from the conditions we have seen over the past few years. Measures must be taken to lighten the debt burden on the US federal budget, and to reduce debentures. There are many other problems as well. President Obama spoke quite frankly about this at the G8 Summit. Overall, I think this was a wise decision. The market reacted in predictable ways. I think the correction will happen, especially once everyone realizes that the US and global economies are beginning to recover. In the end, we will all benefit from this.

J. Defterios:

Thank you Mr. President. Ms. Merkel, before I go to the floor here, you talked in your opening remarks about having to pursue a policy of growth in Europe right now, and that it is very important. You also added that it needs to be along with sound fiscal policies, as well. You know the criticism aimed at Germany, that, the policies that are good for Germany are not necessarily good for the southern half of Europe, with youth unemployment at above 50% in Greece and in Spain right now. Fiscal consolidation would mean greater competitiveness, but there is no growth in southern Europe. Is there a willingness on behalf of Germany to adjust those policies because of the pain that is being inflicted on those in southern Europe and, particularly, those in the next generation? Is there a change in policy that is necessary?

A. Merkel:

I would like to comment briefly on the previous topic. We cannot forget that high liquidity caused the major 2008–2009 financial crisis. We do not want to live through another one. I believe we have yet to reach the necessary balance: if all regions of the world were already enjoying stable development, banks of issue would not have so much influence over currency rates. We can see how closely the economy is linked to the actions of banks of issue. In a stable, predictable environment, this would not be happening.

Moreover, the high deficit gave rise to a rumour that people should no longer invest in European bonds. What did we conclude from this? We turned to the IMF and the European Central Bank, and developed programmes for problem countries. The best international experts took part in this work. These countries were not simply negotiating with Ms. Merkel: they were negotiating with reputable institutions. In Eastern Europe – in the Baltics, for example – some countries that are not part of the eurozone also adopted similar measures. They went through a difficult period, but eventually attained economic growth. I believe we can achieve the same results in Southern Europe.

I am not just talking about the economy. In Greece, for example, no one would buy government bonds anymore, and something had to be done about it. That is

why we are talking about sweeping structural reform. Greece needs an effective government, an effective taxation system, and a broader privatization programme. Baby formula, for example, should be sold in supermarkets, like it is in the rest of the world, not just in pharmacies. Of course the administration, which benefited from the existing system for so many years, is having a hard time bringing itself to undertake structural reform. But this reform is obviously needed.

Another question relates to how the burden of the reform is shared. This is difficult to control at a global level. As I said earlier, some shirk their share of the burden, and others have to carry it for them. So we have solidarity, but it is based on our unwillingness to hurt each other by telling the truth. Solidarity, yes, but 10–20 years from now, we will realize that we are no longer competitive.

In the meantime, China, Russia, and Brazil have already stated that they will not sit around and wait for Europe to move forward. They can make cheaper and more innovative products, and as a result, they will grow more competitive. The question is whether Europe's economy will still be innovative in 20 years, or whether Europe will turn into a tourist attraction for people who want to visit the first chemical factory or see where the first car was built. I want to see a competitive Europe. So we must be absolutely blunt with each other.

V. Putin:

I would like to return to your earlier question. The markets have slowed down a bit following Mr. Bernanke's announcement; and what is more, the value of gold has plummeted. Why did this happen? I think this was done to strengthen the dollar, to the great joy of the yuan, the euro, and certain regional currencies. But this will lead to changes on the commodities market that have to be taken into account when shaping economic policy.

To address your question to Madame Federal Chancellor, this issue is not only vital to the eurozone, but to us as well. You might have noticed that I mentioned in my speech that we must find a balance between addressing strategic issues and addressing ongoing operational issues. Theoretically, these are the same issues as those facing the eurozone: solving the unemployment problem in the

southern countries, and ensuring overall economic growth. The goals are somewhat similar, although today I am happy to say that we have a healthier situation: our unemployment is at 5.5%. Can you imagine? Our unemployment is at historically low levels. We have virtually no debt. Russia's foreign debt is 2.5% of our GDP, while in the US this figure is, I believe, 114%, and in the eurozone it is approximately 100%. Even if we take into account domestic debt, our figure is 10–11%. Our inflation is also near historic lows, as I have already mentioned. Inflation has increased a bit, but I think we can deal it a serious blow by capping the tariffs of natural monopolies. To sum up, we are at a satisfactory – I do not quite dare say good – starting point for further development.

But our problems are fundamentally similar to those facing Germany and other eurozone countries. I agree with Madame Federal Chancellor, and she knows how I feel. I believe this is the right approach for us: before we put something into the cask, be it honey or caviar, we must make sure the cask is in good condition. Otherwise none of our nice products will be going anywhere. That is the most important thing. Russia has a great deal to do in this respect.

Thank you.

J. Defterios:

Thank you very much. I want to open the floor to questions, I am looking for a quick question, in particular, on energy policy because the President talked about the softness we have seen in commodities and also economic policy. If we could have a microphone here into the centre of the room, Mr. Yergin, if you could stand up that would great. And then I am going to go to other side of the room, to the left in about the fifth row. Dan Yergin has got the floor.

D. Yergin:

Thank you, Mr. President and Chancellor Merkel for your addresses. A question for President Putin: major technological developments are unfolding in the oil and gas industry relating to tight oil and shale gas that are affecting the energy balance, supply, and potentially, price. How do you see these developments

affecting the Russian economy and what kind of strategies does Russia have for addressing these new developments? Thank you.

V. Putin:

Things are always changing. The world always adapts to them somehow, and so does our economy. The thing is that I do not see any fundamental changes. Shale gas has entered the American market. This is an economic fact in today's world, especially in the energy sector. But I have yet to see fundamental changes. First of all, the cost of shale gas extraction is several times higher than the cost of regular gas extraction. I am afraid to give you the wrong figures, but I believe the cost is USD 16 per 1,000 cubic metres. Meanwhile, Gazprom spends USD 1 per 1,000 cubic metres. Do you see the difference? That is the first point.

The second issue is environmental change. It is well known that people living close to shale gas mining sites often – not always, but often – have black sludge coming from their taps. Shale gas extraction requires huge expanses of land. It requires explosions. From one explosion to the next, and so on, and so forth. Huge plots of land are taken out of commercial circulation and are completely destroyed. I assume that the technologies will continue to improve. But today, if we want to produce shale gas, maybe followed by shale oil – this is also possible; it is already being done – then the end price for the consumer will be around USD 120 per 1,000 cubic metres. If we add the cost of liquefying, diluting, and transporting it, the European market price goes up to USD 350–400 per 1,000 cubic metres. This is, in effect, the same price Gazprom currently charges its major European customers for pipeline gas.

The American market benefits from this, at least today. But for now, I do not expect the global gas market to see serious changes. As I said earlier today when I met specialists from the energy industry, we must all now focus on fundamental technological changes in this area. If we can all change the technology together, we will reach a breakthrough. We must assume that cheap energy does not exist. We have to go after hard-to-extract resources which require high initial investment and new technologies. That will be a new step in global energy development.

J. Defterios:

Another question from the floor. I see someone here who would like to ask a question.

J. Turley:

John, thank you and both of you, thank you for your comments. This is for President Putin. Russia has, over the last decade, had a very well-deserved reputation for fiscal discipline and prudence, and you have touched on this a little previously, but if you could be a little more granular, as the economy has slowed here, how do you plan to balance the need for stimulating growth with the need to really maintain that discipline that you have earned so well over the last ten years?

V. Putin:

I would like to focus your attention on several issues. First, we want to significantly lower inflation and create the basic conditions to ensure the required level of economic growth. Second, we are going to improve the banking system, and as a result of having addressed the first issue, we will drive interest rates down and provide major, as well as small and medium-sized companies, with easier access to credit. We are going to reduce administrative barriers, streamline administrative procedures, improve the quality of management, and lower the corresponding costs. Finally, we are going to continue to develop our infrastructure.

These three issues are just the tip of the iceberg. We are also going to continue our work in the Russian regions, and take steps in other areas as well. Naturally, this will require resources. I repeat: although these objectives seem mutually exclusive, we will try to find a middle path of development that will allow us to maintain our basic conditions and find ways to finance the objectives, primarily in the area of infrastructure, that I mentioned earlier.

Finally, I have a few words about the main topic of the day: developing human capital and improving education and the healthcare system. On these issues, we

have prepared a sweeping programme based on cooperation with the relevant professional and public institutions.

J. Defterios:

Thank you, Mr. Putin. Another question from the second row, if you could, please identify yourself.

J. Wermuth:

Jochen Wermuth, German investor in Russia, a happy investor I have to say, over a billion invested and able to do it in a normal fashion. Thank you very much for the excellent reception here. Thank you very much for your indication of the great cooperation between the G8 heads of state and your commitment to Europe and Russian-European cooperation. So, my question to both of you is on Russian-EU strategic partnerships. In this room here, I think it was a few years ago in 2005, Herman Gref and Peter Mandelson negotiated the four common spaces between the EU and Russia. The question is, the pre-condition for the four common spaces, freedom, movement of goods, security, and education, to be implemented was that Russia would join the World Trade Organization. Now, eight years later, it has happened. Could we go back to the plans of 2005 and implement the four common spaces between Russia and the EU to come to a general and strategic partnership for growth for Russia and the EU? Thank you very much.

J. Defterios:

Thank you very much. Ms. Merkel, would you like to take that first?

A. Merkel:

The potential for partnership between the EU and Russia has not been fully tapped. I believe Russia's accession to the WTO was a very important step. As a result of intergovernmental consultations, we have noted that our cooperation in the energy sphere has progressed. I believe that the Prime Minister of the

Netherlands was here yesterday. Many countries, such as France, for example, are working very closely with Russia.

There are undoubtedly still challenges to be met. Russia is trying to address the visa issue as quickly as possible. I know people in Russia think we are too slow on this issue. We have discussed economic freedom and human rights: an area in which we have obvious differences. But when we talk about long-term prospects for cooperation, as a European, I can tell you that Russia plays an important strategic role. Despite certain setbacks – and the President of Russia is not always reticent about coming forwards to express his opinion on these issues; he sometimes talks about them very loudly – this does not stop us from cooperating further.

V. Putin:

I express myself in a way that will be heard. If I am too loud, I apologize.

But I do not understand why we should go back to 2005. Madame Federal Chancellor hit the nail right on the head when she mentioned Russia's accession to the WTO. When Ministers Mandelson and Gref worked on these issues, their main objective was to ensure that Russia joined the World Trade Organization. We have met this challenge. We still have many problems, many disagreements, and I believe this is quite natural. We must undoubtedly take these steps in the context of harmonizing our stance on humanitarian law, and in the context of a mutual understanding of the nature of human rights and how they should be upheld, as well as of the nature of shared values. We still have many issues to reconcile. But it is also crucial to treat each other with care and respect. This is extremely important. Russia is always ready to listen to its partners and adjust things, but only on the condition that no one condescendingly imposes their rules on us.

But I can tell you that I have not seen this go on, especially lately. It has not been happening, except perhaps in the media, where there are many emotional people who are not particularly well informed about what is going on in reality. They put forth various theories on the issue. By the way, this is the fault of our

governments: if we offered the public and the media timely and comprehensive information, we would not have to deal with all sorts of conjecture.

We are also seeing a great deal of debate on economic cooperation. But this is natural. Every country is always looking for the best way to address its problems. Here, as is the case with any kind of trade, sellers want to sell for a higher price, and buyers want to buy at a lower price. This is natural; it is to be expected. We have disagreements, but we do find solutions.

We have joined the WTO. The leader of another international organization is here with us today. He is a close friend, and we are working together towards Russia's entry into the OECD. We are also approaching this issue calmly, without rushing into it. Even if it does not happen tomorrow, we know that we must harmonize our domestic laws and regulations with OECD requirements. We are doing this quietly, without taking dramatic steps. I do not even want to put a specific deadline on our joining the organization. That is not important. What is important is that we hear and understand each other, that we are moving in that direction.

We disagree with the EU on the Third Energy Package. We have yet to reach an agreement in principle. But as Madame Federal Chancellor noted, we and our European partners still built the Nord Stream pipeline together, and it works. I believe we will continue to work in the same vein, because our work is based on deep mutual interest. I have already given you statistics on the growth of consumption in China. But consumption will also grow in Japan and other parts of Asia, and in Europe, despite its current problems.

I am convinced that the foundation of Europe's economy and the European leadership's sense of responsibility will drive the recovery of this region, which plays such an important role in the global economy and is currently Russia's largest trading partner. Our trade with the EU has topped USD 400 billion. We are moving towards the goals we set for ourselves just a few years ago.

J. Defterios:

A question for Ms. Merkel. A big decision last night overnight: EU finance ministers decided to recapitalize banks but there was a caveat put forward by

Germany that national governments need to share the burden. My question for you, Chancellor, is will this not shut out the economies that need it most? Because the state cannot afford this in Spain, Italy, Portugal, Greece, for example, the recapitalization of the banks. Are you satisfied that it will do what it is needed to do?

A. Merkel:

I believe we can attain our goals. When we talk about the EU, we must take into account that it is not a single national entity, but several states. The question of joint responsibility, as well as the ability to take joint action and make joint decisions, is very important to me and to Germany. So far, we cannot recapitalize banks Europe-wide. My position as Federal Chancellor does not allow me to influence the way banks are recapitalized in, say, Spain or Greece, since they are controlled by national governments.

We have to reconcile very different things: the majority of EU countries do not want to change the European Union Treaty because the process is too complicated. We must work towards expanding the rights of European institutions. But to do that, we have to change the Treaty.

As far as bank recapitalization is concerned, I have yet to see a written clause defining who will be responsible for bank recapitalization if any issues arise. We said that taxpayers, be they Germans or citizens of other European countries, should not always bear responsibility for the problems facing banks. We cannot create a 'too big to fail' situation. And to avoid that, we must devise a hierarchy of responsibility.

What do we do if a bank cannot save itself, if it does not have sufficient capital? The state must get involved. If the state cannot get involved, we have the European Stability Mechanism. But that is the last resort, and the state has to apply for the ESM to be implemented. Once the EU receives this application, it can dictate its conditions. My position as Federal Chancellor does not allow me to tell individual states, "You have to change the way you manage this bank", and so forth.

In other words, I am responsible for Germany's tax policies, and the heads of other states are responsible for tax policies in their own countries. We must bear responsibility for the way tax revenues are being spent. We can only do that in cooperation with our colleagues. There is another option: we could hand over the responsibility to the European Central Bank or another body. But that can only be done if each nation hands over the responsibility for its own banks. Germany promotes solidarity, but only in combination with responsibility, when the responsibility ends up on our shoulders. And Parliament has confirmed this.

V. Putin:

Madame Federal Chancellor has said she does not yet know who is responsible for the recapitalization of failing banks. At the same time, she has said that I sometimes express my point of view too loudly. Let me whisper this to you: I hope the burden will not be on the clients.

J. Defterios:

Before I go back to the floor, I would like to ask our host and your guest, Mr. President, I do not want to be accused of running over time, but there are a lot of questions from the floor, do we have ten more minutes, does that suffice for you? Madam Chancellor, are you OK as well?

A. Merkel:

Yes, I will have to speak with the President less, but I agree. Ten more minutes: no longer.

J. Defterios:

Thank you very much, I appreciate that.

Sir, a brief question if you can.

From the audience:

UniCredit Vita, Milan, and Axel Springer, Berlin. I have a question for Madame Federal Chancellor. You said something about the possibility of taking necessary

measures in Europe. When will we see a European political union? We have 27 different countries with 27 fundamental sets of legislation, 27 presidents and cabinets. This is a point of weakness. A union must be united to be strong.

A. Merkel:

I think a political union between all the government entities you just mentioned is possible if we form a single European government. But this requires a lot more time. Certain powers have already been handed over to the European Union: one example is the antidumping measures related to solar panel imports from China. In this case, I have to explain to the Chinese Government that I can only have so much influence over this situation, because this is the purview of the European Union, and it has to be addressed by qualified majority. I might be unhappy with the Third Energy Package, but Germany depends on the European Union's decision on this. I believe the European Union can only have the powers we hand over to it ourselves.

I think it is better to coordinate our actions: in other words, rather than hand over our powers, we must sign multilateral economic agreements which all EU members must abide by, while social issues must remain within the purview of national governments. Truly European solutions lie not only in handing over powers to the EU, but also in promoting coordinated action: the central administration is not always equipped to find suitable solutions to local issues.

I also think it is crucial that we know we are doing a good job. But I am not convinced we are. Whether or not we are doing a good job is determined by our competitive edge. We have been in the vanguard for years. But that does not mean we will remain in the vanguard forever. Globalization presents us with entirely new challenges. We can meet these challenges better if we are united, with each of us making a unique contribution. I do not oppose the new model. But we will not have a unified state.

V. Putin:

Madame Federal Chancellor has explained her position clearly. Please allow me to offer my opinion as an outsider. A single currency zone cannot be effective

without a single budgetary and fiscal policy and a single macroeconomic policy, especially when member countries operate at different levels of economic development. That is why we will either see a unified state, the United States of Europe, or a unification process based on individual agreements and accords. It does not matter: what matters are the results. I can think of many jokes on the subject. Whatever we do on our wedding night, the outcome must be the same.

J. Defterios:

One quick question for Ms. Merkel, one quick question for Mr. Putin, and then we will wrap it up. A very important decision overnight, Ms. Merkel, and that was a move to block the accession talks for Turkey into the European Union, after the protests that we saw and the government response, which, I understand affected you quite personally, you took it quite hard. Is this move irreversible? The accession talks with Turkey into the European Union, after what we saw?

A. Merkel:

Turkey's accession to the EU is hampered by many problems. We issued a mandate to conduct negotiations; the negotiations took place; page after page was turned. But in the last few years, we have not taken any steps forward on this issue. When all the preconditions are met, we will turn the next page. Right now, our decision has to be based on the following facts: Turkey has yet to fulfil the Ankara Agreement, which requires that Turkey have equal trade relations with all countries of the European Union. This brings up the particularly complicated issue of Cyprus. We are currently not taking any steps forward; however, we are not taking any steps back either. We will turn the next page only after Turkey fulfils the Ankara Agreement.

I have already mentioned the situation in Turkey. The government's treatment of the protesters worries me. The protesters are defending the rights and values we hold dear. Something strange is happening in Turkey. We will be discussing this further. Whether or not we turn the next page is a different issue. We will take a decision next week. I do not want to get ahead of things and reveal Germany's position too early.

J. Defterios:

Indeed. Thank you very much.

Mr. President, I would like to clear up one issue that came up in the last week or so. Let us roll back the clock eight years to the visit of Robert Kraft to St. Petersburg and his Super Bowl ring. There was a meeting here and shaking of hands, the ring passed from one person to the next. Was it a gesture that he gave you the ring? You thought it was a very nice ring, you said "Thank you very much and I will give a gift in-kind"? Let us clear up this international question of intrigue that has been circulating for the last 10 days. Thank you.

V. Putin:

You know, I cannot remember Mr. Kraft or the ring. But I do remember they were giving out souvenirs. If Mr. Kraft and his team place such high value on this, I have a suggestion. I will ask our manufacturers to create something really nice and striking: an obviously expensive item, made of high-quality metal, with a stone; something that could be passed down from generation to generation within the team whose interests Mr. Kraft represents. I think that would be the smartest solution to this complex international issue in the true spirit of partnership.

J. Defterios:

Let me extend my thanks to President Putin for allowing me to host the key note address. Chancellor Merkel, thank you very much also for your words of wisdom in terms of your speech, and for taking questions.

I wish we could take more questions from the floor, but we have had an issue with the time allocation.

Thank you very much for the invitation. I wish you success for the rest of the summit.

V. Putin:

I would like to ask everyone to thank Madame Federal Chancellor for finding the time to come to St. Petersburg and take part in our discussion.