July 2001
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Russian Federation: Post-Program Monitoring Discussions—Staff Report; and Public Information Notice on the Executive Board Discussion

In the context of the Post-Program Monitoring Discussions, the following documents have been released and are included in this package:

- the staff report for the Post-Program Monitoring Discussions, prepared by a staff team of the IMF, following discussions that ended on **March 23, 2001,** with the officials of the Russian Federation on economic developments and policies. The paper includes the authorities' statement on economic and financial policies for 2001 and outline of medium-term strategy. **Based on information available at the time of these discussions, the staff report was completed on May 17, 2001.** The views expressed in the report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Public Information Notice (PIN), summarizing the **views of the Executive Board as expressed during its May 29, 2001 discussion** of the report on issues related to the Post-Program Monitoring.

The policy of publication of staff reports and other documents by the IMF allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

RUSSIAN FEDERATION

Report on Post-Program Monitoring Discussions

Prepared by the European II Department

Approved by John Odling-Smee and Leslie Lipschitz

May 17, 2001

- A 17-month Stand-By Arrangement in an amount of SDR 3.3 billion (55.5 percent of quota) expired on December 27, 2000. Only one purchase, upon approval, was made under the arrangement. Outstanding obligations to the Fund at end-April 2001 amounted to SDR 8.5 billion (143.7 percent of quota). The staff will monitor the implementation of the authorities' macroeconomic and structural policies for 2001 in the context of the Post-Program Monitoring framework.

- The authorities' macroeconomic and supporting structural policies for 2001, as described in Appendix I, were the subject of intensive discussions during November 8–21, 2000, January 31–February 16, 2001, and March 3–23, 2001. The staff met with: Mr. Kasyanov, Prime Minister; Mr. Kudrin, Deputy Prime Minister and Minister of Finance; Mr. Khristenko, Deputy Prime Minister; Mr. Illarionov, Economic Advisor to the President; Mrs. Paramonova, First Deputy Chairperson of the Central Bank of the Russian Federation; Ms. Nabiullina, Deputy Minister of Economy and Trade; and other senior Russian officials.

- In one or more missions, the staff team comprised Messrs. Bélanger, Tiwari, Laursen, Roaf, Robinson, Spatafora, and Ms. Banerji (all EU2), Mr. Santos (PDR), Mr. Verhoeven (FAD), and Ms. van de Ven (assistant, EU2), as well as Moscow Office staff consisting of Messrs Gilman, Thomsen, Anderson, Barnard, and Välilä. Mr. Alam from the World Bank participated in the January–February mission. Mr. Mozhin, Executive Director for Russia, and Messrs. Lushin and Palei (OED) attended most of the policy discussions.

- Russia accepted the Proposed Fourth Amendment to the Articles of Agreement of the Fund on March 6, 2001.

- Discussions for the next Article IV consultation are expected to take place in September/October with a Board discussion in November/December 2001.

- This report is the product of a team effort led by Siddharth Tiwari.

Contents

I. BACKGROUND

1. **Macroeconomic outcomes have improved dramatically since the August 1998 crisis**. The large real depreciation provided a strong stimulus to growth and, assisted by a sharp increase in international energy prices, contributed to a massive strengthening of the external current account that permitted reserves to be rebuilt well beyond pre-crisis levels. Fiscal performance, a key contributing factor to the crisis, also turned around as a result of the strengthened macroeconomic environment, a significant improvement in the authorities' tax collection efforts, and control of the growth of expenditures. In particular, the government's decision to save a large part of the windfall tax gains (due to high energy prices) helped the central bank to manage the liquidity injection from the balance of payments, enabling inflation and the pace of the real appreciation of the ruble to be kept under control (Figure 1).

Key Macroeconomic Indicators, 1997-2000

	1997	1998	1999	2000
Real GDP (percentage change)	0.9	-4.9	3.5	7.7
Inflation (percentage change)	10.9	84.5	36.6	20.1
Federal government				
Primary surplus (in % of GDP)	-2.5	-1.3	1.8	5.3
Overall balance (in % of GDP)	-7.1	-5.9	-4.4	1.0
External current account ($ bn)	-0.4	-1.6	22.9	45.3
Gross official reserves ($ bn)	17.8	10.9	12.5	28.0
Russian oil price ($/barrel)	16.3	10.5	14.7	24.6
Real exchange rate (1997=100)	100.0	88.6	62.5	70.2

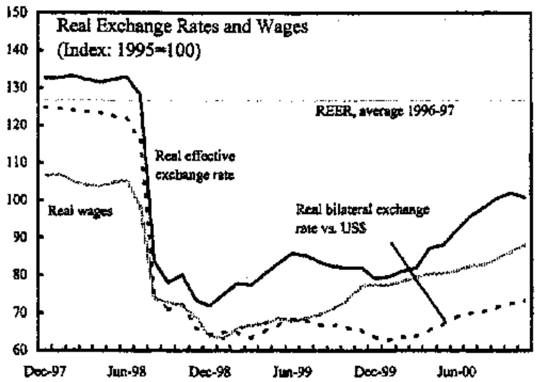
2. **While some progress has been made in tackling the structural weaknesses that contributed to the crisis, much remains to be done to sustain the improved macroeconomic performance**. Implementation of the structural reform programs under both the recently expired Stand-By Arrangement (SBA) and the canceled World Bank Structural Adjustment Loan (SAL3) was not as envisaged. In particular, the reforms in the banking sector and infrastructure monopolies slipped behind schedule. There have been no disbursements from the Fund or under SAL3 since mid-1999 though disbursements from the World Bank have continued under sectoral adjustment loans.

3. **Discussions with the Fund have evolved** from initially attempting to modify the SBA (approved in July 1999) to—since mid-2000—seeking agreement on a new SBA covering 2001 to, more recently, negotiations on a precautionary SBA. These discussions, particularly the specification of macroeconomic policies for 2001, were also influenced by the continuing uncertainty regarding energy prices and, thus, the strength of the balance of payments as well as the relationship between Russia and its Paris Club creditors. The authorities in late February made the policy decision to make full payments to Paris Club creditors in 2001, and the budget amendments necessary to make this effective have been passed.

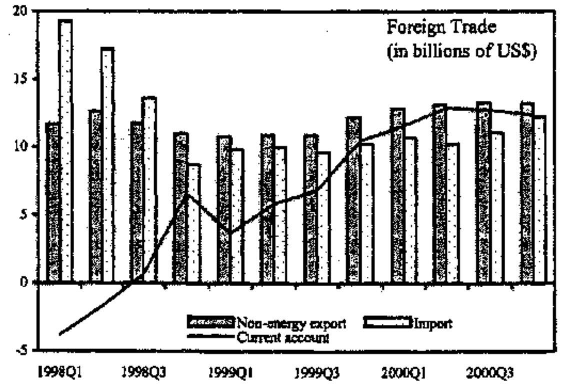
4. **In the end, after agreement had been reached on most aspects of a policy package, the authorities decided not to request a precautionary SBA. The staff will monitor the implementation of the authorities' macroeconomic and structural policies**

Figure 1. Developments Before and After the Crisis

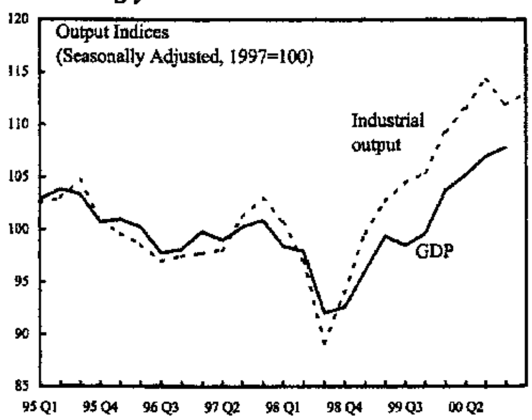
The crisis led to a sharp real depreciation and to sharp initial declines in real wages ...



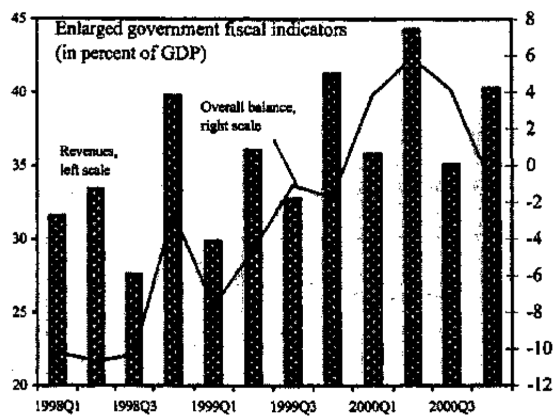
As a result, net export volumes increased significantly.



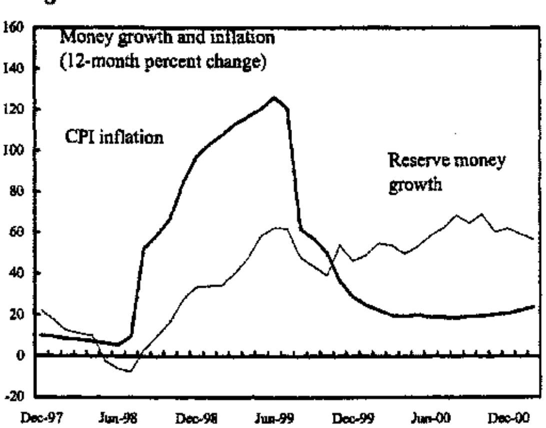
Output continued recovering strongly until late 2000 ...



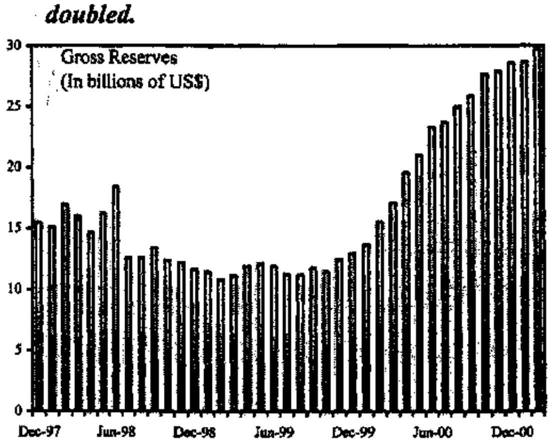
And the fiscal position improved considerably.



Inflation was reduced rapidly to moderate levels, well below money growth ...



Meanwhile, reserves more than doubled.



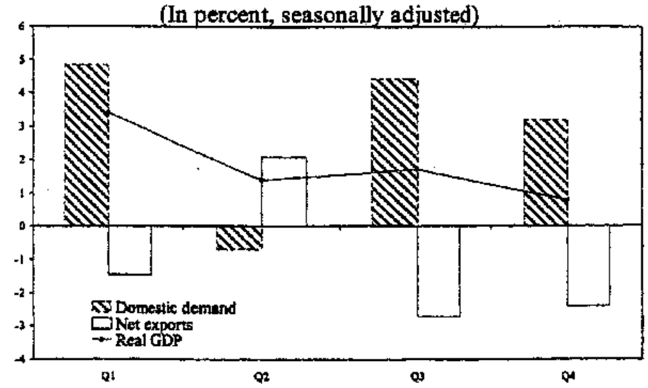
in the context of Post-Program Monitoring (PPM) procedures. The authorities' annual (and quarterly) macroeconomic targets for 2001 as well as the structural policy agenda (as described in the authorities' Statement on Economic and Financial Policies for 2001 and Outline of Medium-Term Strategy, attached to Appendix I)[1] are in line with those on which agreement was reached in the context of discussions on a precautionary SBA. However, some issues that would have needed to be addressed up-front in a new arrangement with the Fund have yet to be implemented though—with the exception of continuing to conduct, and make public, reviews of reserve management practices—they are included in the authorities' program to be implemented during 2001.

II. Recent Economic and Policy Developments

5. **Economic developments in 2000 were dominated by the strength of the balance of payments.** High international energy prices produced a strong current account surplus that permitted a large build-up of official reserves but also exerted pressure for a sharp appreciation of the ruble. Sterilized intervention by the CBR, assisted by a large fiscal surplus, moderated these pressures. However, a relaxation of the stance of both monetary and fiscal policies in the second half of the year heightened inflationary pressures and contributed to a sharp increase in capital outflows. The real exchange rate appreciated from the second quarter of the year, contributing to a slowdown in growth. On the structural reform front, the government has been able to put in place a far-reaching tax reform and continues to refine the agenda in other areas.

6. **Real GDP grew by 7½ percent in 2000, but the momentum slowed during the year.**[2] This expansion was supported by sustained growth in domestic demand, including both private consumption and investment, in response to rising wages and continued high levels of profitability.[3] However, the significant real appreciation from the second quarter

Real Demand Growth in 2000
(In percent, seasonally adjusted)



[1] A formal statement of policies is not a requirement for PPM, but the authorities' decision to provide, and publish, a clear statement of their program is a commendable step towards increased transparency.

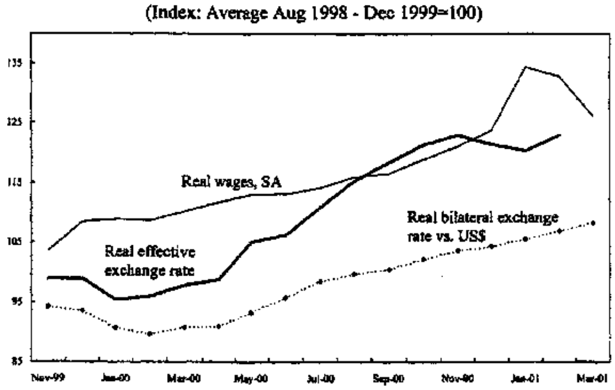
[2] Goskomstat has recently released revised national accounts data for 1999 and 2000 that indicate stronger growth than previously estimated.

[3] The sharp improvement in the external terms of trade resulted in significant (post tax) income gains concentrated in the energy sector, contributing to the acceleration in investment and capital outflows.

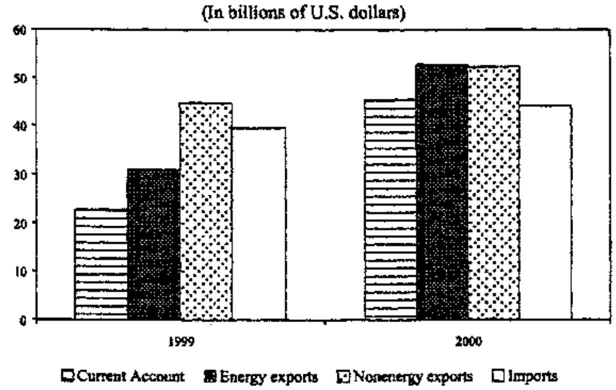
of 2000 led to a sharp decline in net exports. Industrial production data for the first two months of 2001 confirm the slowdown in growth. Concerns over this slowdown are reflected in consensus forecasts for growth in 2001, which have been revised downwards from 4 percent at the beginning of the year to around 3½ percent now.

7. **The external current account surplus is estimated at $45 billion (18 percent of GDP) in 2000, driven by the sharp increase in international energy prices and still compressed imports from the pre-crisis period.** Reflecting a two-third increase in the average price for Russian oil and natural gas exports, the energy sector accounted for the bulk of the over $20 billion (6 percent of GDP) improvement in the current account from 1999. Non-energy exports increased modestly during the year, while the combination of the real appreciation, rising incomes, and a fourth quarter fiscal loosening fueled a recovery in imports especially towards the end of the year.

Real Exchange Rates and Wages, 1999-2001
(Index: Average Aug 1998 - Dec 1999=100)



External Trade, 1999-2000
(In billions of U.S. dollars)



8. **The budget recorded a strong surplus in 2000, even though the fiscal stance was relaxed during the fourth quarter.** The primary balance of the federal government improved by 3½ percent of GDP over the previous year, largely on account of a strong increase in revenues driven by higher energy sector tax receipts and improvements in compliance. This surplus would have been higher had not a supplementary budget in December 2000 increased non-interest expenditures by more than 2 percent of annual GDP

Federal Budget Developments, 1999-2000
(Commitment basis, in percent of period GDP)

	1999	2000				
		Q1	Q2	Q3	Q4	Year
Revenues	13.2	16.0	18.4	14.3	16.6	16.2
Expenditures	17.6	14.1	15.2	12.1	18.8	15.2
Noninterest	11.4	8.7	9.9	8.2	15.7	10.9
Primary balance	1.8	7.3	8.4	6.1	0.8	5.3
Overall balance	-4.4	1.9	3.2	2.2	-2.3	1.0
Memorandum item:						
Enlarged government balance	-3.3	3.1	5.3	4.1	0.1	3.0

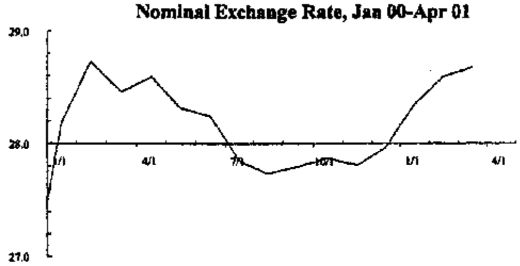
Sources of Changes in Enlarged Government Revenues, 2000 (In percent of GDP)

	2000
Enlarged government	38.8
Total change from 1995-97 pre-crisis level	4.1
Discretionary policy changes/adjustments	0.8
Real exchange rate movements	0.7
World price movements	1.6
Compliance and other changes (residual)	1.0

in the fourth quarter. The increased expenditures were allocated to transfers, budgetary wages, defense, and expenditures by budgetary funds. Other levels of government, particularly the Pension Fund, recorded a large surplus as expenditures remained restrained despite strong revenue collections. Further, interest expenditures declined significantly as a share of GDP reflecting the real appreciation of the ruble. As a result, the overall balance of the enlarged government improved by nearly 6½ percentage points of GDP. Preliminary data for the first two months of 2001 indicate a continued strong fiscal performance with revenues in line with projections and expenditures somewhat lower.

9. **For most of 2000, the strong support from fiscal policy and a sharp recovery in money demand reduced the burden on the CBR to sterilize a significant amount of the inflows from the balance of payments to keep inflation under control.** To limit pressures for nominal exchange rate appreciation, the CBR purchased substantial amounts of foreign exchange leading gross reserves to more than double by end-September.[4] The liquidity injection was partially absorbed by a build-up in balances at the CBR by all levels of government and some sterilization by the CBR. Nonetheless, base money increased

Nominal Exchange Rate, Jan 00-Apr 01



Sources of Base Money Growth, 2000-01 Q1
(In percent of beginning of year base money)

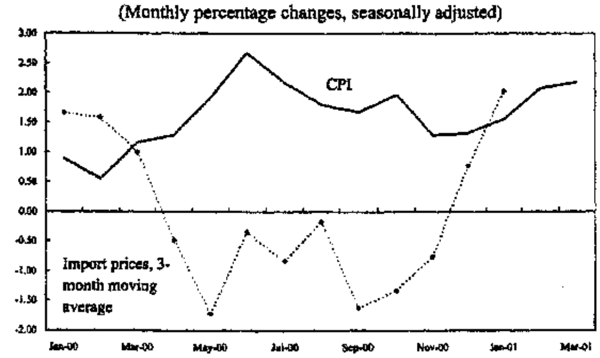
	2000 Q1	2000 Q2	2000 Q3	2000 Q4	2001 Q1
Base money	-1.7	24.1	12.4	25.3	-3.8
NIR	34.2	52.5	41.1	27.9	9.4
NDA	-35.8	-28.4	-28.7	-2.6	-13.3
Credit to federal government	-9.7	-11.4	-9.1	-3.5	-10.5
Credit to local government and EBFs	-11.5	-10.0	-8.9	-7.9	-3.4
Credit to banks	-13.9	-10.0	-6.6	5.3	4.0
OIN	-0.7	3.0	-4.1	3.5	-3.4
Memorandum items:					
CBR net intervention ($ bn)	4.2	7.3	5.3	2.6	3.4
(as percent of base money)	36.7	63.6	45.7	22.5	18.6
Gross official reserves ($ bn)	15.6	21.1	25.3	28.0	29.9

[4] The setting and monitoring of key components of the monetary authorities' balance sheet is complicated in the case of Russia by government and CBR transactions in non-gold precious metals. Such transactions are covered by the State Secrets Act, which constrains the authorities' ability to provide information to the staff as well as the staff's ability to monitor such transactions independently. Given the current very high market prices for some of these metals, such transactions can result in significant shifts in financial aggregates, including NDA and NIR, or, in the case of transactions between the government and the CBR, in net credit to the government. While the accounting and recording of these transactions in the fiscal and monetary data is fully consistent with previous program definitions as well as data provision requirements under the Articles of Agreement, such transactions give the authorities the ability to influence outcomes relative to targets independently of the implementation of usual financial policies. The authorities agreed with the staff that monitoring under future arrangements from the Fund would have to be modified to adjust for such transactions.

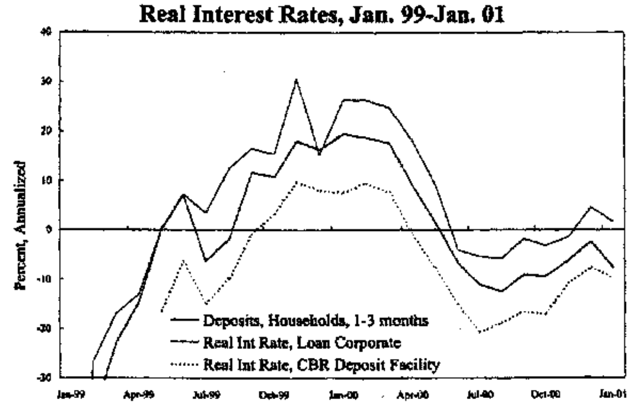
rapidly. The strong increase in money demand—driven by a combination of output recovery, the appreciation of the ruble, and the remonetization of the economy as the incidence of barter fell—limited the resultant inflationary pressures.

10. **The monetary policy stance eased during the second half of 2000, including by accommodating the fiscal relaxation at the end of the year, which resulted in a surge in capital outflows.** The CBR gradually reduced its sterilization from July onwards and CBR net interventions in the foreign exchange market declined despite the continuing strength of the current account. Current account earnings largely exited in the form of capital outflows as real interest rates on ruble deposits remained negative and there were few alternative financial instruments available within Russia.[5] For 2000 as a whole, more than half of the current account surplus was offset through net private capital outflows. In the first quarter of 2001, key monetary aggregates—base money, NDA, and NIR—were in line with projections, although the reduction in NDA has been achieved through stronger than anticipated fiscal performance rather than higher CBR sterilization.

Monthly Inflation Rates, Jan. 2000-Mar. 2001
(Monthly percentage changes, seasonally adjusted)



Real Interest Rates, Jan. 99-Jan. 01



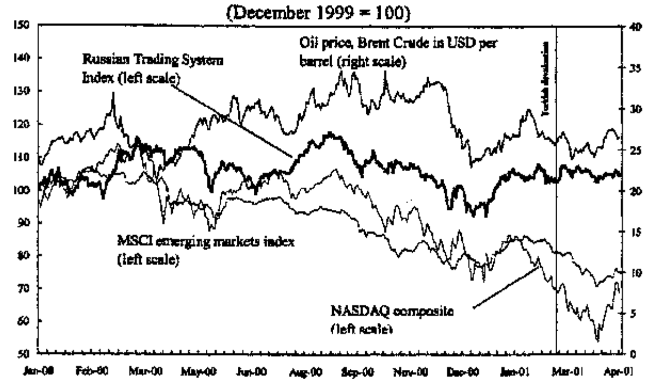
11. **Inflation also crept upwards during the year.** The initial uptick in April/May 2000 was related to administered price increases. The combination of rapid money growth and nominal wage increases maintained inflationary pressures during the remainder of 2000 though these were partially masked by falling import prices. Inflation increased further in early 2001 following the burst of fiscal expenditures, further increases in administered prices, and the nominal depreciation in late December 2000 and early January 2001.

[5] Net private capital outflows (including errors and omissions) increased sharply from an average of $5.8 billion per quarter during January–September to an estimated $9 billion in the fourth quarter.

12. **Russia has not suffered significant macroeconomic impacts from either the developments in Turkey or the decline in global stock markets.** Direct trade links with Turkey are modest—less than 4 percent of Russia's recorded external trade—and a significant portion of Russia's exports to Turkey are energy products which can be diverted to other markets. Spreads on Russian Eurobonds have increased modestly in 2001 along with those in other emerging markets in response to developments in Argentina and Turkey, but until recently remained higher than those in these two countries due to a higher risk reflecting past default. While reducing these spreads is important, their immediate impact is modest as the budget envisages no new access to international capital markets this year, and nonresident holdings of government ruble debt instruments are relatively small and subject to capital restrictions. As regards equities, the Russian stock market rose by 18 percent during the first quarter of 2001, in contrast with a decline in emerging markets as a whole. There has been little impact from the weakness in the Nasdaq, which in the past was closely correlated with Russian and other emerging markets. In contrast, oil prices continue to exert a significant impact on stock market values as oil and gas companies account for about two-thirds of total capitalization.

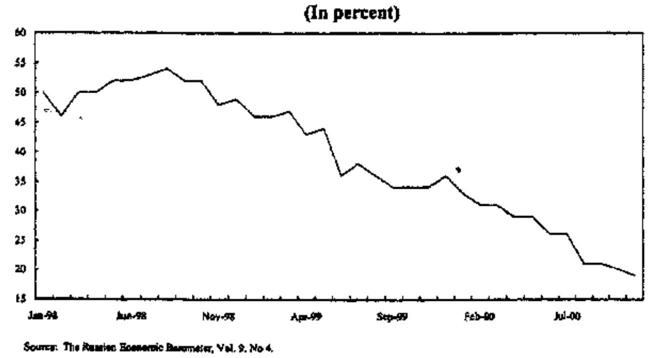
Russian Eurobond Spreads, May 2000-May 2001
(Basis points over U.S. Treasury Bills)

Stock market index, 2000-Q1 01
(December 1999 = 100)



13. **Shortly after assuming office in May 2000, the government formulated a comprehensive structural reform strategy.** This strategy was cast over a ten-year horizon, with a more detailed action plan for the period through 2001. Reforms in the fiscal area were the main achievements in 2000, with adoption of important tax legislation (i.e., passage of four of the five main chapters of Part II of the Tax Code), continued reform of the Treasury system, and rationalization of spending in the 2001 budget. Also, the nonpayments situation improved significantly in 2000, with the share of barter in industrial sales halved to about 20 percent by end-2000,

Share of Noncash Payments in Industrial Sales, 1998-00
(In percent)



Source: The Russian Economic Barometer, Vol. 9, No 4.

and cash collections in key infrastructure monopolies doubling in the course of the year. While much of the improvement was related to the strengthened financial conditions in the economy, the reduction in barter and nonpayments also reflected supporting policy measures, including the termination of offset operations by the federal government and stricter financial discipline in the economy, including at the subnational government level and in the energy sector. A number of other initiatives have been advanced, including a package of laws to streamline business regulations. On the other hand, reforms lagged in other key areas such as the banking system. While the financial review of Sberbank was completed, the passage of the long-pending legislative amendments to facilitate bank restructuring was postponed (see para 26). Plans to restructure the power and gas sectors were also delayed.

III. The Authorities' Program for 2001

A. Context of the Discussions

14. **The policy discussions focused on the macroeconomic implications of the strong balance of payments position and how to advance the structural reform agenda.** In particular, while a real appreciation and import recovery are consistent with a sustainable medium-term balance of payments position, the containment of risks to output growth from allowing too rapid a real appreciation of the ruble requires large-scale sterilization operations by the central bank. Maintenance of fiscal surpluses in the near term will help to reduce medium-term fiscal vulnerabilities. As regards structural policy, while the government's own reform agenda is broader in scope, the discussions focused on a streamlined set of issues that are of direct relevance for the sustainability of macroeconomic and financial stability—fiscal reform, the banking system, and nonpayments—and governance and transparency.

Key Macroeconomic Indicators, 2000-01

	2000 Est.	2001 Proj.
Real GDP	7.7	4.0
Inflation	20.1	14.0
Federal government, commitment basis (Percent of GDP)		
Primary balance	5.3	3.9
Overall balance	1.0	0.8
Current account ($ bn)	45.3	35.6
(Percent of GDP)	18.3	12.0
Gross official reserves ($ bn)	28.0	35.5
(Months of import cover)	5.5	6.0
(Ratio to short-term debt)	321.3	395.7
Russian oil price ($/barrel)	24.6	20.4

B. Macroeconomic Policies in 2001

15. **The authorities' macroeconomic program for 2001 targets a further decline in inflation and continued growth, albeit at a lower rate than in 2000.** Growth would be driven by domestic demand through a continued recovery of investment and consumption as well as some stimulus from a relaxation of the fiscal stance. The current account is likely to weaken, due to the fall in oil prices and the real appreciation of the ruble, but will remain strong and permit a further build-up of reserves (SEP, para 11). The resultant foreign exchange inflows would be sterilized by the CBR in order to achieve a further reduction in inflation and limit pressure for the exchange rate to appreciate.

16. **Fiscal policy targets a small overall surplus for 2001.** The relaxation in the fiscal stance relative to 2000 is largely due to the short-term impact of the tax reform introduced in the 2001 budget, which is projected to lower general government revenues by about 3 percent of GDP in 2001. Most of the revenue decline would occur at the lower levels of government, where expenditure would need to be reduced by about 2 percent of GDP to maintain a balanced position. The authorities noted that subnational governments faced hard budget constraints and that savings could be found through increased cost recovery in housing and utilities as well as reduced expenditures by regional Road Funds (SEP, paras 12–15). The staff expressed concern about the feasibility of realizing these savings without resort to arrears or unsustainable spending cuts.

17. **The external current account is expected to remain strong.** While the balance of payments is projected to weaken relative to 2000, a substantial current account surplus is still anticipated for 2001. Capital outflows are likely to remain high because a significant reduction can only be expected over the medium term as structural reforms advance. Nonetheless, gross reserves are expected to increase by $7½ billion, to a level equivalent to six months of import coverage at end-2001. On balance, pressures for a further real appreciation of the ruble are likely to remain strong.

18. **Monetary policy will be geared to a further reduction in inflation, which will require significant sterilization by the CBR to absorb the liquidity injections from the balance of payments.** The CBR has proposed a base money path for 2001 that the staff believe would be consistent with the inflation objective though there is considerable uncertainty about the continued speed of recovery in money demand. While it was willing to sterilize liquidity injections to meet this path, the CBR noted that the anticipated volume of sterilization was large and, in the event of a significantly stronger than projected balance of payments, the fiscal stance would need to be tightened. The conduct of monetary policy is to be strengthened by enabling the CBR to issue its own bonds and through a regularization of relations between the CBR and the Ministry of Finance, including a recapitalization of the CBR if necessary (as described in the SEP, paras 16–19). The adequacy of the CBR's instruments to effect the necessary sterilization and its impact on the CBR's income position will need to be kept under close review. Though inflation was higher than expected in the first quarter (by about 2 percentage points), the authorities cited the impact of administered price changes and hoped that with monetary aggregates on track the annual target for inflation could still be achieved or the excess kept small. The staff concurred that there was no reason for a significant revision of the target at this stage.

19. **The authorities disagreed with the staff's assessment that monetary policy had become too loose and that an early increase in interest rates was desirable.** Acknowledging that there were many factors underlying capital outflows, the staff argued that the apparent acceleration in capital outflows during the fourth quarter of 2000 indicated that monetary policy had become too loose, as evidenced by the negative real interest rates on ruble assets and the fact that more than half of the current account surplus had been offset through private capital outflows. Also, there is a clear risk that inflationary pressures were building, including through recent increases in real wages. The staff suggested that interest

rates be raised and sterilization be stepped up. The authorities shared the concern about the level of capital flight but saw little benefit from raising interest rates at the present time. While agreeing that interest rates might have to be raised to achieve the targeted level of sterilization, the CBR preferred a more cautious approach to monetary policy electing to monitor developments in liquidity and prices for signs of an acceleration in inflation before adjusting interest rates. In addition, an interest rate adjustment would increase pressure for a nominal appreciation of the exchange rate, and the authorities considered that the potential impact of a premature tightening of monetary policy on growth more than outweighed the inflation risk. The stronger than expected fiscal performance in early 2001 and build-up of government deposits at the CBR had also eased the need for sterilization by the CBR and, thus, for an early increase of interest rates.

20. **The government is pursuing further regional and global integration.** Renewed efforts are being made to regularize relations with all creditors, including non-Paris Club official creditors and uninsured suppliers. A preliminary agreement was reached in late April with uninsured suppliers, on similar terms to last year's London Club restructuring. In addition, the government is pursuing an accelerated schedule of discussions on entry to the WTO. Discussions with Belarus on a possible currency union are ongoing.

C. Structural Reforms

21. **The government's program recognizes that sustained growth depends critically on the steadfast implementation of a broad range of structural and institutional reforms.** The broad reform strategy aims at creating a favorable business and investment climate and reforming the structure and institutions of the economy. These reforms, which go significantly beyond those that are necessary for macroeconomic stability alone but are essential to support sustainable growth, include adoption of a Land Code, rationalization of the role of the government, reducing the regulation of economic activities, strengthening of judicial institutions and processes, development of the banking system and capital market, strengthening bankruptcy and anti-monopoly legislation, lowering barriers to entry to the Russian market, accelerating the restructuring of natural monopolies, and continuing privatization of state-owned enterprises. These priorities were reaffirmed in the President's address to the Duma on April 3, 2001. A medium-term program covering the period through 2004 is being finalized.

22. **The World Bank has been discussing with the authorities a framework for monitoring the implementation of the government's structural reform program though the government has indicated that it does not require further adjustment lending from the Bank at this time.** Where feasible, monitoring is to be based on quantitative performance indicators. The monitoring will focus on aspects of the structural reform program, including deregulation, corporate restructuring, hardening budget constraints and reducing implicit subsidies, streamlining administrative regulations, and enhancing the targeting of social assistance. The Bank is continuing its support for coal sector reform as well as fiscal and institutional reforms, the latter including through new loans to support the reform of intergovernmental relations, tax and customs administration, treasury

development, and public expenditure reviews. The Bank has streamlined its portfolio of project loans, which are now performing satisfactorily.

23. **The focus of structural reforms in the attached statement of the authorities for 2001 is on core areas critical to sustaining macroeconomic stability.** These include fiscal reforms, banking sector reform, dealing with nonpayments and barter, and enhancing governance and transparency in policy-making institutions.

24. **The government attaches high priority to advancing fiscal reforms on both the tax and expenditure side and in the financial relations between the different levels of government** (SEP, paras 26–37). Regarding tax reform, the focus in 2001 is to continue adoption of Part II of the Tax Code, notably the profit tax chapter, that would include phasing out of various special allowances, including the investment allowance, and exemptions. The bulk of the remaining chapters would be considered by the Duma in the spring of 2002. The staff expressed concern, however, that concessions in the Duma were sharply increasing the costs of the tax reform. From 2 percent of GDP initially envisaged as revenue losses for the overall tax reforms, passage of the first four chapters alone were estimated to result in revenue losses of 3 percent of GDP, while the compromise now under consideration for the profit tax could add 1–1½ percent of GDP more in 2002. Further steps are being taken to strengthen tax administration.

25. In the area of expenditure policy, most unfunded expenditure mandates have been suspended at both the federal and local levels for 2001, and are to be funded or eliminated as of 2002. The government is also preparing a reform of the pension system, including the creation of mandatory individual savings accounts. Expenditure policies will be further refined using regional and sectoral public expenditure reviews. At the same time, expenditure management is being strengthened, notably through extending the coverage of the Treasury to include the entire defense sector. Also, an inventory of budget entities is being completed with a view to separating commercial activities. Finally, the government is planning to eliminate all remaining federal budgetary payment arrears in 2001.

26. **The authorities acknowledge that accelerating banking sector reforms is critical for sustainable growth** (SEP, paras 38–46). A key step is to design a strategy for the development of the banking system that would increase the role of private, including foreign, banks and enhance competition. The CBR posted a draft strategy on its website in February and further refinement, in consultation with the government, is expected in the next few months. In this context, reviews of state banks, including notably Sberbank, are to be conducted, which will provide inputs into the design of the strategy for the reform of the banking system. The authorities also aim to improve the legal framework for bank supervision, and a package of amendments to the banking laws to facilitate bank restructuring was approved by the Duma in a third reading in April.

27. **Efforts will be made to sustain the recent improvement in the nonpayments situation and resolve remaining problems in this area** (SEP, paras 47–52). The problem has been largely solved at the federal level through avoidance of tax offsets and full funding

of energy consumption by budgetary entities. However, financial discipline needs to be strengthened at the local government level, and the government is considering supporting this with targeted subsidies for vulnerable regions. Also, it will insist on phasing out the acceptance of noncash payments and enforcing strict disconnection procedures for nonpaying customers by energy companies (including, in particular, Gazprom) to ensure that the recent improvements in cash collections are not reversed in the face of an economic downturn. Progress in this respect will be monitored relative to cash collection targets established for each company. Further, the government is undertaking an overhaul of the bankruptcy legislation to remove the current bias against liquidation of insolvent enterprises and accord more generally with current trends in insolvency law. In addition to the policy commitments contained in the SEP, the government intends to narrow the strategic list of energy consumers (who cannot be disconnected due to nonpayment) and abolish the list in its entirety by end-2001. In the oil sector, the government is developing a strategy to introduce appropriate market incentives to ensure adequate supplies of oil products to the domestic market without resort to domestic energy balance targets, while providing safeguards for vulnerable regions.

28. **The government and the CBR are also committed to further improving governance and transparency**, including strengthened steps against money laundering (SEP, paras 53–55). In this context, the Report on the Observance of Standards and Codes prepared as background for the 2000 Article IV consultation is being updated and will be published by the third quarter. In the area of fiscal policy, increased transparency will be mostly achieved through expanding Treasury coverage. The transparency of monetary and financial policies will be further increased through publication by the CBR of its audited 1999 accounts on an IAS basis and summaries of past quarterly reserve audits and an audit of reserve management practices that were prepared by the CBR's external auditor (PwC).[6] Later this year, the CBR intends to publish its accounts for 2000 on an IAS basis. The CBR and the government also plan to transfer the central bank's foreign subsidiaries to VTB by end-2001 and for the CBR to divest itself of its holdings in VTB by January 1, 2003.[7] Further, the authorities intend to provide reserve and foreign currency liquidity information to the Fund according to the SDDS template. Regarding money laundering, the European convention against money laundering was ratified in April, and the government has recently submitted new legislation on money laundering to the Duma.

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[6] The CBR does not, however, intend to have future quarterly reserve audits or audits of quarterly reserve management practices prepared by its external auditor.

[7] VTB (Vneshtorgbank) is a commercial bank in which the CBR holds 99.9 percent of shares.

D. Monitoring

29. Implementation of the authorities' macroeconomic program will be monitored on the basis of the quarterly outcomes for: the balance of the federal and enlarged governments (on a commitment basis, Table 2); and monetary authorities' net international reserves, net domestic assets, and net credit to the federal and enlarged governments (Table 4). Similarly, the progress in the implementation of the structural reform agenda will be assessed on the basis of meeting the goals that the authorities have established for themselves in the area of fiscal reform, the banking sector, nonpayments, and governance and transparency.

IV. Medium-Term Prospects and Vulnerability

30. **The staff's balance of payments projections—based on the assumption of a sustained implementation of structural reforms that would gradually improve the investment climate—indicate that Russia's medium-term outlook is favorable.** Output growth could average 4–5 percent per year, led by private investment but with room for a gradual recovery in private consumption as productivity and real wages improve further. Net exports are likely to contribute negatively to growth over the medium term as import growth would outpace exports in tandem with the real appreciation of the ruble. Some weakening of the terms of trade, as global energy prices are expected to decline, would further reduce the external current account, which should nevertheless remain in surplus owing to its current very high level. The capital account should also strengthen as the investment climate improves, through a reduction in capital flight, higher FDI, and renewed access to international capital markets. This would allow a further build-up of net international reserves. Thus, the baseline scenario does not suggest an immediate need for exceptional balance of payments support, although the staff recognize that the year 2003 in particular is vulnerable as large debt payments fall due in that year.

Key Medium-Term Macroeconomic Assumptions, 2002-06

	2002	2003	2004	2005	2006
			(In percent)		
Real GDP growth	4.0	4.0	4.5	5.0	5.5
CPI inflation (end of period)	11.1	8.8	7.9	7.0	7.0
Federal government overall balance / GDP	0.0	0.0	0.0	0.0	0.0
External current account ($ bn)	26.5	19.5	14.9	12.8	11.1
Change in Russian crude oil price (%)	-9.9	-7.8	-2.2	-1.3	0.0
Official reserves ($ bn)	40.0	40.2	43.3	47.0	56.8
(Months of import cover)	6.0	5.5	5.5	5.5	6.1
(Ratio to short-term debt)	284.3	484.6	438.4	551.8	581.3

31. **Even under the relatively favorable environment underlying the base-line scenario, there are likely to be significant fiscal pressures over the medium term.** While the authorities are committed to their objective of balanced budgets over the medium term, there is as yet no clearly articulated strategy as to how this will be achieved including how to respond to the volatility in revenues stemming from the current dependence of the economy on natural resource exports. The ongoing tax reform is proving to be very costly. The fiscal pressures arising from these revenue losses will be magnified by potentially significant reform-related expenditures, in particular in the social area. Additional resources are likely to be needed for health and education. In addition, there may be sizeable costs associated with

the restructuring of one-company towns and the Northern Territories. While fiscal pressures could be eased in the medium term through increased taxation of the energy sector as well as a larger capacity for domestic and external borrowing, it will be necessary to streamline expenditures (in line with the expenditure reform policies discussed above) and raise revenues through further strengthening of tax administration, broadening the tax base, and if necessary, raising certain taxes. The budget for 2002 needs to be placed in a comprehensive medium-term macroeconomic and fiscal framework consistent with the government's medium-term reform plans, which explicitly takes into account vulnerabilities associated with volatile oil prices.

32. **The government will also need to build on recent reforms of intergovernmental fiscal relations**. It will be necessary to reconcile revenue sources and spending needs at all levels of government, especially in view of the disproportionate loss of revenues from the tax reform at the lower levels of government. In this regard, a final solution must be found for the currently suspended unfunded mandates. Further, Treasury execution of expenditures should be extended to the subnational government level, which will require significant investments to augment data processing and communication capabilities.

33. **The dependence of Russia on volatile commodity prices, however, makes the medium-term outlook subject to considerable uncertainties** (Box 1). Notably, there is a risk that global energy prices may decline more rapidly than envisaged, putting pressure on both the fiscal position and the balance of payments. Further, normalization of financial relations with non-Paris Club bilateral creditors and uninsured suppliers could increase the debt service burden significantly by an annual average of about $2 billion. The main concern is for 2003 when large debt repayments fall due[8] and adverse external developments combined with large expenditure pressures could lead to a need for renewed exceptional balance of payments support. These risks, of course, would be further magnified if structural reforms are not pursued rigorously and high growth rates fail to materialize.

34. **Russia's external vulnerability has lessened and the capacity to repay the Fund has strengthened considerably over the last couple of years.** In the absence of any new disbursements, and with sizeable repayments, Fund exposure has declined dramatically, although it remains relatively high. At the same time, the very positive macroeconomic performance and commitment to prudent financial policies have markedly improved Russia's debt service capacity, and given the favorable medium-term prospects, Russia should be able to meet its obligations to the Fund.

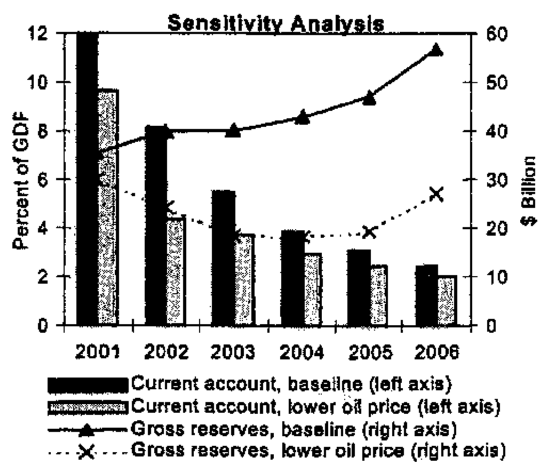
[8] The debt service as well as the debt service ratio (measured as a share of exports of goods and services) is projected to increase from $18 billion or 16 percent in 2001 and 2002 to $23 billion or 20½ percent in 2003 before declining in 2004 and beyond.

Box 1. External Vulnerability and Capacity to Repay the Fund

Russia's external vulnerability has greatly decreased since the August 1998 financial crisis. The current account has swung from a pre-crisis deficit to a surplus of 12 percent of GDP in 1999 and 18 percent in 2000, reflecting both the sharp post-crisis decline in imports and the continued significant growth in energy exports (driven by higher world prices for energy). A debt reduction on London Club debt and sizable repayments to the Fund led to a $15 billion reduction in public external debt, which stood at $141 billion (57 percent of GDP) as of end-2000. Gross official reserves have been replenished to $28 billion at end-2000.

The external position is expected to continue strengthening over the medium term. Under the baseline scenario (based on the latest WEO assumptions, and consistent with further real appreciation), energy exports will weaken significantly while imports recover, but the current account will continue to average significant surpluses of almost 6 percent of GDP over 2001–06. Further, as structural reforms take hold and confidence improves, net private capital outflows should decline sharply. Hence, gross reserves are projected to roughly double, from $28 billion (5.5 months of imports) in 2000 to $57 billion (6.1 months of imports) in 2006. Public external debt will fall to 30 percent of GDP in 2006. Given the structure of the debt repayment schedule, the debt service ratio (as a fraction of exports of goods and services) will at first rise, from 14 percent in 2000 to 21 percent in 2003, but it will then return to 14 percent by 2006.

This outlook, however, remains vulnerable to the risk of a sharp decline in oil prices. The staff have developed an alternative scenario, which assumes that oil prices fall to $15 per barrel already by end-2001 (instead of declining gradually to $19.5 per barrel by 2005, as in the baseline), with a corresponding decline in natural gas prices. Under this scenario, over 2001–06, the current account surplus will be on average almost 2 percent of GDP lower than under the baseline. As a result, gross reserves will decrease by over one-third (and import coverage by over one-half) between 2000 and 2003, with only a slow recovery afterwards. Lower energy prices will also weaken fiscal performance, reflecting both the direct impact on tax revenues from the energy sector and the indirect impact through lower output growth. Over 2002–06, enlarged revenues will be on average over 1 percent of GDP lower than under the baseline.



Russia: Indicators of Debt Service to the Fund, 2001–06 1/

	2001	2002	2003	2004	2005	2006
Debt Service ($ bn)	2.0	3.3	3.3	1.7	1.2	1.1
Charges	0.6	0.5	0.3	0.2	0.1	0.1
Repurchases	1.4	2.8	2.9	1.5	1.1	1.0
In percent of:						
Exports of Goods & Services	1.8	2.9	2.9	1.4	1.0	0.8
Total Debt Service	11.2	17.9	14.0	9.6	6.5	6.0
Gross Official Reserves	5.7	8.1	8.1	3.8	2.6	1.9

Sources: Based on data provided by the authorities, and staff estimates.

1/ Based on the latest WEO proj. for the $/SDR rate over 2001–06.

A sluggish pace of structural reforms would present a major source of vulnerability. Medium-term projections assume a significant improvement in the investment climate, in the absence of which there would be significant pressures on the balance of payments, through higher capital outflows and lower FDI.

Other potential shocks present far smaller risks. The additional impact on the current account of even a dramatic, prolonged weakening of global growth (above and beyond its impact through lower energy prices) would not exceed one-fifth of the impact of the above oil-price shock. Likewise, in the short run even a sharp increase in the risk premium on emerging market bonds, together with a significant weakening of FDI and portfolio equity flows, would present limited risks: Russia has not had access to international capital markets since the summer of 1998, it does not intend to tap the markets in the near future, it still imposes significant capital controls, and FDI is already very small. The effects would, however, be more severe in the medium term, as the baseline assumes that the improved business climate and confidence result in both stronger FDI, lower capital outflows, and improved market access.

Russia is expected to be able to meet its obligations to the Fund. Debt service to the Fund is projected to peak at an average $3.3 billion per year in 2002–03, accounting for 2.9 percent of exports of goods and services, 8.1 percent of gross reserves, and 16 percent of total debt service.

V. STAFF APPRAISAL

35. Russia's macroeconomic performance during 2000 was impressive with outcomes being the best since the dissolution of the former Soviet Union. Growth rebounded strongly, inflation was reduced to moderate levels, and there was a sharp increase in holdings of international reserves. These favorable outcomes were driven by the large real depreciation of the ruble (in 1998), the recent sharp increase in international energy prices, and the generally prudent fiscal and monetary stance in 1999 and 2000. However, recent trends—slowdown in growth and an uptick in inflation—highlight the difficulties in managing the strong balance of payments, and the authorities need to be vigilant in adjusting the policy stance as necessary to preserve recent macroeconomic gains.

36. In the staff's view, the authorities' macroeconomic program for 2001 appropriately aims at supporting growth, achieving a further reduction of inflation and building up external reserves. The staff also endorse those elements of the government's structural reform program aimed at strengthening the basis for sustained macroeconomic and financial stability—fiscal and banking reform, and elimination of nonpayments/barter—and to promote good governance and transparency in public policy making. While the implementation of many of these measures has been delayed in the context of programs with the Fund, their inclusion in the government's own program and the publication of that program points to a renewed commitment to ensure their implementation.

37. The principal challenge to economic management in the short run remains the strength of the balance of payments against the background of weakening growth prospects. The authorities face the difficult task of creating appropriately tight domestic liquidity conditions to prevent too rapid inflation and hence a real appreciation of the ruble that could threaten economic growth. The easing of the fiscal stance in 2001—stemming from adoption of the tax reform—now places the burden of sterilization squarely on the CBR. The large scale of sterilization that is likely to be needed emphasizes the need for the CBR to be endowed with an adequate income position as well as a range of instruments equal to the task. If the balance of payments is stronger than anticipated, the government should be prepared to achieve higher fiscal surpluses to help ease pressures for appreciation of the ruble. Uncertainties about the underlying strength of the recovery and the external environment, however, require that the targets and supporting policies be kept under continuous review.

38. The resolution to the macroeconomic challenges ultimately lies in a period of sustained growth led by gains in productivity and investment. The government's far-reaching structural reform program is appropriately aimed at improving the business and investment climate and the staff encourage the authorities to push ahead with the implementation of their agenda. Strong implementation would strengthen the stimulus to foreign direct investment and reduce capital flight, thereby ensuring sustained high growth and reducing vulnerability to external shocks.

39. The reform of Part II of the Tax Code initiated in 2000 is arguably the most important structural reform since the liberalization of prices and trade at the outset of the transition. The staff, however, are concerned that compromises to ensure the passage of this legislation in the Duma are turning out to be excessively costly. The revenue loss should be strictly

limited to ensure that fiscal sustainability is not threatened in the event of a cyclical downturn and given the uncertain costs of structural reforms.

40. The successful formulation of a strategy for the development of the banking sector is key to the much needed reform of the financial sector in Russia. The recent strategy paper developed by the CBR is a welcome first step in this direction. The staff urge the authorities to build upon this and design a forward-looking strategy that would increase the role of private, including foreign, banks, enhance competition, and move to international accounting standards. Their success will depend upon overcoming strong vested interests opposed to such reforms. In this context, the recent, much delayed, action to strengthen the legislative framework for bankrupt financial institutions is welcome, and the staff urge prompt adoption of the appropriate legal amendments.

41. Staff also strongly endorse the government's stated intention to eliminate the nonpayment/barter problem. While substantial progress has been achieved already, the authorities need to ensure that the underlying structural improvement is sufficiently strong to guard against a reversal in case of a cyclical downturn or worsening of the terms of trade. The identification of specific measures in this area, which would generate confidence that these objectives would be achieved, has been difficult. Close monitoring will accordingly be required and the search for new measures resumed in case of slippage relative to specified cash collection targets.

42. The implementation of the authorities' program for 2001 is to be monitored in the context of PPM procedures. The staff urge the authorities to implement their program resolutely to ensure a continuation of the recent strong macroeconomic performance and establish a strong record of policy implementation which would be a critical factor in considering a possible future request for Fund financial support for their policies.

Table 1. Russian Federation: Macroeconomic Indicators, 1998-2001

	1998	1999	2000	Q1 2001 Proj.	Q1 2001 Est.	2001 Proj.
			(Annual percentage changes)			
Production and prices						
Real GDP	-4.9	3.5	7.7	4.8	...	4.0
Change in consumer prices						
Period average (on previous period)	27.7	85.7	20.8	5.5	6.7	17.6
Within period	84.5	36.6	20.1	4.8	7.2	14.0
Change in GDP deflator	12.4	65.1	40.0	...	...	17.8
			(In percent of GDP)			
Public sector						
Enlarged government balance	-8.0	-3.3	3.0	1.2	...	1.0
Federal government						
Overall balance (commitment basis)	-5.9	-4.4	1.0	0.3	4.1	0.8
Primary balance (commitment basis)	-1.3	1.8	5.3	4.9	8.8	3.9
Revenue	11.0	13.2	16.2	15.7	16.6	15.6
Expenditure (commitment basis)	16.9	17.6	15.2	15.4	12.3	14.9
Interest	4.5	6.2	4.3	4.6	4.6	3.1
Noninterest	12.3	11.4	10.9	10.8	7.7	11.7
			(Within period percentage change, unless otherwise indicated)			
Money and credit						
Monetary authorities						
Base money	27.9	54.1	60.2	-1.8	-3.8	23.7
NIR (change in billions of U.S. dollars)	-12.1	5.6	19.1	1.4	1.7	9.0
Ruble broad money	21.1	57.2	62.4	4.9	0.5	26.9
			(In billions of U.S. dollars unless otherwise indicated)			
External sector						
Total exports, fob	74.9	75.8	105.2	26.0	25.3	105.0
Total imports, fob	58.0	39.6	44.2	12.1	11.0	52.4
External current account (deficit -)	-1.6	22.9	45.3	9.3	10.0	35.6
Gross reserves coverage (months of imports of GNFS)	1.8	2.8	5.5	5.5	6.1	6.0
Memorandum items:						
Nominal GDP (billions of rubles)	2,696	4,607	6,947	1,921	...	8,500
Exchange rate (rubles per US$, period average)	9.7	24.6	28.1	...	28.5	...

Sources: Russian authorities; and Fund staff estimates and projections.

Table 2. Russian Federation: Federal Budget Operations, 1999-2001
(In billions of rubles, unless otherwise indicated)

	1999 Year	2000 Year Est.	2000 Q1 Est.	2000 Q2 Est.	2000 Q3 Est.	2000 Q4 Est.	2001 Year Proj.	2001 Q1 Proj.	2001 Q1 Est.	2001 Q2 Proj.	2001 Q3 Proj.	2001 Q4 Proj.
Revenue	608.0	1126.9	221.8	285.9	275.5	343.7	1328.0	301.5	318.0	333.5	333.0	360.0
VAT	218.8	367.3	84.5	91.5	92.6	98.7	548.6	111.5	125.8	133.8	143.7	159.6
Excises	84.2	131.5	26.2	38.0	25.9	41.4	192.8	40.7	42.6	51.2	46.2	54.7
Profit and income taxes	98.9	210.1	31.9	56.9	51.3	70.0	192.0	36.4	36.8	53.3	50.4	51.9
Taxes on trade	86.3	233.1	48.2	55.3	58.5	71.1	254.6	80.2	76.6	61.2	55.1	58.1
Other	119.8	185.0	31.0	44.2	47.2	62.6	140.0	32.7	36.2	34.0	37.6	35.8
Expenditure 1/	670.6	993.3	180.8	219.5	220.3	372.7	1304.1	310.3	240.0	337.7	335.2	320.9
Interest	162.8	181.7	40.3	54.0	51.8	35.6	266.8	88.7	88.1	44.2	98.6	35.2
Domestic interest	73.9	71.3	15.6	21.5	20.2	14.0	62.6	16.4	18.4	12.8	20.0	13.4
External interest	88.9	110.4	24.7	32.5	31.6	21.6	204.2	72.3	69.7	31.4	78.6	21.8
Noninterest	507.8	811.6	140.5	165.5	168.5	337.1	1037.3	221.7	151.9	293.5	236.5	285.6
Wages	124.0	150.4	...	...	...	...	209.3	...	...	...	...	...
Transfers to regions and population	134.0	203.7	...	...	...	...	302.2	...	...	...	...	...
Transfers to population	...	97.4	...	...	...	...	115.5	...	...	...	...	...
Transfers to regions	...	106.3	...	...	...	...	186.6	...	...	...	...	...
Additional exp. for excess 2000 revenues	...	153.0	...	...	...	...	37.0	6.3	...	30.8	0.0	0.0
Additional wage exp. for excess 2001 revenues	...	...	...	...	...	...	27.0	0.0	...	0.0	6.8	20.2
Arrears clearance financed by securities	...	...	...	...	...	...	16.3	6.3	...	10.0	0.0	0.0
Other	249.8	304.5	...	...	...	...	445.6	209.2	151.9	252.7	229.7	265.4
Overall balance (cash)	-62.6	133.6	41.0	66.4	55.2	-29.0	23.9	-8.8	78.0	-4.2	-2.2	39.1
Rescheduled interest	124.8	114.1	34.9	27.5	22.6	29.1	0.0	0.0	3.0	0.0	0.0	0.0
Change in domestic arrears	16.9	-52.0	-20.0	-10.9	-10.6	-10.6	-41.4	-14.7	-3.6	-22.2	-2.2	-2.2
Primary balance (commitments)	83.3	367.3	101.3	131.3	117.6	17.2	332.0	94.5	169.7	62.2	98.7	76.5
Overall balance (commitments)	-204.3	71.5	26.1	49.8	43.1	-47.5	65.3	5.9	78.6	18.0	0.1	41.3
Financing (cash)	62.6	-133.7	-41.1	-66.4	-55.3	29.0	-23.8	8.9	-78.1	4.3	2.1	-39.1
Foreign	8.7	-61.1	-6.0	-32.5	-17.4	-5.2	-104.7	-28.8	-27.5	-3.1	-33.7	-39.1
Disbursements	55.0	39.5	9.8	6.5	10.0	13.2	33.5	7.7	3.8	11.6	7.2	6.9
Repayments	46.3	100.6	15.8	39.0	27.4	18.4	138.2	36.5	31.3	14.8	40.9	46.0
Domestic	53.9	-72.6	-35.1	-33.9	-37.9	34.2	80.9	37.7	-50.6	7.4	35.8	0.0
Bank financing	71.7	-44.2	-33.5	-22.8	-10.8	22.8	22.0	27.1	-49.5	-23.5	29.5	-11.1
Monetary authorities 2/	45.6	-117.9	-31.5	-37.0	-37.9	-11.5	3.6	20.9	-54.5	-11.8	14.3	-19.8
CBR credit (incl. VEB)	121.9	-34.2	-9.7	-10.9	-18.4	4.8	29.9	24.6	-34.5	-4.8	21.3	-11.2
Use of NIR	-76.3	-83.7	-21.8	-26.1	-19.5	-16.3	-26.3	-3.7	-20.0	-7.0	-7.0	-8.6
Commercial banks	26.1	73.6	-2.0	14.2	27.1	34.3	18.4	6.2	5.0	-11.7	15.2	8.7
Nonbank financing	-17.8	-28.4	-1.6	-11.1	-27.1	11.4	58.9	10.6	-1.1	30.9	6.3	11.1
Privatization	-4.4	27.2	1.1	1.6	3.4	21.1	35.0	0.5	0.7	3.0	12.5	19.0
Precious metals	15.9	47.5	10.3	6.3	7.6	23.3	3.0	0.0	3.6	1.0	1.0	1.0
Securities held by nonbank	-22.3	-103.1	-13.0	-19.0	-38.2	-32.9	4.6	3.8	-11.6	16.9	-7.2	-8.9
Plus new securities for arrears clearance	...	...	...	...	...	...	16.3	6.3	6.3	10.0	0.0	0.0
							(In percent of GDP)					
Revenue	13.2	16.2	16.0	18.4	14.3	16.6	15.6	15.7	...	16.3	14.9	15.7
VAT	4.7	5.3	6.1	5.9	4.8	4.8	6.5	5.8	...	6.5	6.4	6.9
Excises	1.8	1.9	1.9	2.4	1.3	2.0	2.3	2.1	...	2.5	2.1	2.4
Profit and income taxes	2.1	3.0	2.3	3.7	2.7	3.4	2.3	1.9	...	2.6	2.3	2.3
Taxes on trade	1.9	3.4	3.5	3.6	3.0	3.4	3.0	4.2	...	3.0	2.5	2.5
Other	2.6	2.7	2.2	2.8	2.5	3.0	1.6	1.7	...	1.7	1.7	1.6
Expenditure (cash)	14.6	14.3	13.0	14.1	11.5	18.0	15.3	16.2	...	16.5	15.0	14.0
Interest	3.5	2.6	2.9	3.5	2.7	1.7	3.1	4.6	...	2.2	4.4	1.5
Noninterest	11.0	11.7	10.1	10.6	8.8	16.2	12.2	11.5	...	14.3	10.6	12.4
Wages	2.7	2.2	...	...	...	...	2.5	...	...	...	...	...
Transfers to regions and population	2.9	2.9	...	...	...	...	3.6	...	...	...	...	...
Other	5.4	6.6	...	...	...	...	6.2	...	...	...	...	...
Primary balance (commitments)	1.8	5.3	7.3	8.4	6.1	0.8	3.9	4.9	...	3.0	4.4	3.3
Overall balance (commitments)	-4.4	1.0	1.9	3.2	2.2	-2.3	0.8	0.3	...	0.9	0.0	1.8
Primary balance (cash)	2.2	4.5	5.9	7.7	5.6	0.3	3.4	4.2	...	2.0	4.3	3.2
Overall balance (cash)	-1.4	1.9	3.0	4.3	2.9	-1.4	0.3	-0.5	...	-0.2	-0.1	1.7
Memorandum items:												
Potential debt service to COMECON and for FTO 3/	...	...	...	...	...	...	42.6	...	...	...	...	...
Principal	...	...	...	...	...	...	10.9	...	...	...	...	...
Interest	...	...	...	...	...	...	31.7	...	...	...	...	...
GDP	4,607	6,947	1,389	1,557	1,924	2,076	8,500	1,921	...	2,050	2,232	2,298
Russian oil price ($ per barrel)	14.7	24.6	23.8	23.4	24.9	26.2	20.4	21.4	...	20.6	20.0	19.5
Enlarged government balance	-150.7	205.9	42.8	83.1	78.1	1.9	86.6	23.7	...	35.8	-7.1	34.1

Sources: Russian authorities; and Fund staff estimates.

1/ Measured on a cash basis.
2/ Excludes valuation changes in treasury bill portfolios.
3/ Payments on certain COMECON debts and obligations to uninsured suppliers (FTO) that are currently under discussion are not included in these projections.

Table 3. Russian Federation: Enlarged Government Operations on a Commitments Basis, 1996-2001
(In percent of GDP)

	1996	1997	1998	1999	2000 Est.	2001 Proj.
Federal government						
Revenue	12.5	12.3	11.0	13.2	16.2	15.6
Expenditure	20.9	19.4	16.9	17.6	15.2	14.9
Interest	5.9	4.7	4.5	6.2	4.3	3.1
Noninterest 1/	15.0	14.8	12.3	11.4	10.9	11.7
Transfers to regions	2.6	2.2	1.9	1.5	1.5	2.2
Transfers to EBFs	0.5	0.9	0.4	0.4	0.4	0.4
Own expenditure	11.9	11.6	10.0	9.5	9.0	9.1
Health	0.4	0.6	0.4	0.4	0.4	0.3
Education	0.5	0.6	0.5	0.5	0.5	0.6
Defense	3.0	3.2	2.1	3.0	2.2	2.8
Other	8.0	7.3	7.0	5.6	5.9	5.4
Primary balance	-2.5	-2.5	-1.3	1.8	5.3	3.9
Overall balance	-8.4	-7.1	-5.9	-4.4	1.0	0.8
Local government 2/						
Revenue	16.4	18.5	16.2	15.6	16.0	13.4
Own revenue	13.4	15.2	14.2	13.9	14.3	10.9
Transfers from federal government	2.6	2.2	1.9	1.5	1.5	2.2
Other transfers	0.4	1.1	0.1	0.2	0.2	0.2
Expenditure 1/	16.7	19.4	17.4	15.7	15.4	13.4
Housing and communal services	4.2	4.3	3.5	2.7	2.3	2.0
Health	2.4	2.7	2.2	2.0	1.7	1.9
Education	3.4	3.7	3.1	2.7	2.3	2.5
Roads	1.4	1.7	2.0	2.1	2.3	1.3
Other	5.4	7.0	6.5	6.1	6.8	5.6
Overall balance	-0.4	-0.9	-1.2	0.0	0.6	0.0
Extrabudgetary funds						
Revenue	8.1	9.9	8.7	8.5	8.7	8.1
Own revenue	7.7	9.0	8.2	8.1	8.3	7.7
Federal transfers	0.5	0.9	0.4	0.4	0.4	0.4
Expenditure	8.2	9.8	9.6	7.3	7.4	7.9
Pension Fund	5.9	7.0	7.1	5.1	5.0	5.9
Employment Fund	0.3	0.3	0.3	0.2	0.3	0.0
Social Insurance Fund	1.2	1.2	1.2	0.9	1.1	0.9
Medical Insurance Funds	0.7	1.1	1.2	1.0	1.0	1.1
Overall balance	-0.1	0.1	-0.9	1.2	1.3	0.3
Enlarged government						
Revenue	33.5	36.5	33.4	35.1	38.8	34.3
Expenditure	42.4	44.4	41.4	38.4	35.8	33.2
Noninterest expenditure	36.5	39.7	36.9	32.2	31.6	30.1
Primary balance	-3.0	-3.2	-3.5	3.0	7.2	4.2
Overall balance	-8.9	-7.9	-8.0	-3.3	3.0	1.0

Sources: Russian authorities; and Fund staff estimates.

1/ Components of spending are shown on a cash basis prior to 1999, with arrears accumulation included in the "other" category.
2/ Consolidated with total territorial road fund budgets.

Table 4. Russian Federation: Monetary Authorities' Accounts, 1999-2001

(In billions of rubles, unless otherwise indicated)

	1999	2000					2001				
	Dec. Revalued	March Act.	June Act.	Sept. Act.	Dec. Act.	Dec. Revalued	March Proj.	March Est.	June Proj.	Sept. Proj.	Dec. Proj.
Base money	324.3	318.9	397.2	437.5	519.5	519.5	510.0	499.5	577.1	587.8	642.5
Currency issued	288.6	268.9	340.5	371.8	446.5	446.5	430.3	424.0	492.6	501.7	548.8
Required reserves on ruble deposits	35.6	50.0	56.7	65.7	73.0	73.0	79.7	75.5	84.5	86.1	93.7
NIR (at program rates) 1/	-76.5	34.3	204.7	338.1	428.6	457.8	497.1	506.8	600.5	623.3	711.3
Memorandum item: NIR in billions of US$	*-2.8*	*1.3*	*7.6*	*12.5*	*15.9*	*16.3*	*17.7*	*18.0*	*21.3*	*22.1*	*25.3*
NDA	400.7	284.6	192.5	99.4	90.9	61.7	12.9	-7.3	-23.3	-35.5	-68.8
Net credit to enlarged government	309.2	240.3	170.9	112.6	75.4	119.1	125.4	47.1	107.3	109.7	97.4
Net credit to federal government 2/ 3/	333.1	301.6	264.6	235.3	223.8	267.5	288.4	213.0	276.6	290.9	271.1
CBR net credit to local government and EBFs	-23.9	-61.3	-93.7	-122.7	-148.4	-148.4	-162.9	-165.9	-169.4	-181.2	-173.7
Net credit to banks	-45.9	-91.0	-123.4	-144.9	-127.6	-127.6	-180.5	-106.8	-197.3	-209.9	-230.6
o/w Correspondent account balances	-68.9	-74.8	-80.5	-92.1	-130.1	-130.1	-98.4	-84.0	-106.4	-115.7	-127.1
Other items (net)	137.4	135.3	145.0	131.7	143.1	70.2	68.0	52.4	66.7	64.7	64.4
Memorandum item:											
Gross reserves (US$ billions)	12.5	15.6	21.1	25.3	28.2	28.0	29.1	29.9	32.5	33.0	35.5

Sources: Russian authorities; and Fund staff estimates.

1/ At fixed accounting exchange rates (Rub 27/US$ and US$1.37/SDR for Dec. 1999 revalued and 2000, Rub 28.16 and US$1.30291 for Dec. 2000 revalued and 2001).

2/ Beginning December 1999, revalued, includes government securities held by the CBR's pension fund which amounted to Rub 4.1 billion at end-1999.

3/ From Sept. 2000, includes CBR holdings of MinFin Eurobonds issued during London Club restructuring in amount of Rub 8.6 bn to replace claims on VEB previously included in OIN.

Table 5. Russian Federation: Monetary Survey, 1999-2001
(In billions of rubles, unless otherwise indicated)

	1999	2000					2001			
	Dec. Revalued	March Act.	June Act.	Sept. Act.	Dec. Est.	Dec. Revalued	March Proj.	June Proj.	Sept. Proj.	Dec. Proj.
Broad money	994.9	1069.0	1235.1	1385.9	1547.0	1564.3	1637.0	1763.6	1804.7	1939.4
Ruble broad money	704.7	751.4	892.2	992.4	1144.2	1144.2	1200.1	1309.7	1333.9	1451.7
Currency in circulation	266.6	251.5	321.8	350.9	419.3	419.3	403.2	464.7	473.3	515.1
Ruble deposits	438.1	499.8	570.4	641.4	725.0	725.0	796.9	845.0	860.6	936.6
Forex deposits 1/	290.2	317.7	343.0	393.6	402.8	420.1	437.0	453.9	470.8	487.7
(Memorandum item: in US$ billions)	*10.7*	*11.8*	*12.7*	*14.6*	*14.9*	*14.9*	*15.5*	*16.1*	*16.7*	*17.3*
Net foreign assets 1/	71.5	230.8	412.6	561.2	646.9	685.6	724.8	828.2	851.0	939.0
NIR of monetary authorities	-76.5	34.3	204.7	338.1	428.6	457.8	497.1	600.5	623.3	711.3
NFA of commercial banks	147.9	196.5	207.9	223.1	218.3	227.7	227.7	227.7	227.7	227.7
(Memorandum item: commercial bank NFA in US$ bns)	*5.5*	*7.3*	*7.7*	*8.3*	*8.1*	*8.1*	*8.1*	*8.1*	*8.1*	*8.1*
NDA	923.4	838.2	822.6	824.8	900.1	878.8	912.2	935.4	953.7	1,000.4
Domestic credit	1132.4	1087.8	1101.1	1175.0	1,304.4	1,368.6	1,411.7	1,443.6	1,471.5	1,525.9
Net credit to general government	550.8	464.9	397.0	360.6	360.3	413.0	419.8	386.0	400.2	413.7
Net credit to federal government	574.8	541.4	518.6	516.4	539.2	591.9	619.0	595.5	625.0	613.9
Net credit from the monetary authorities	333.1	301.6	264.6	235.3	223.8	267.5	288.4	276.6	290.9	271.1
Net credit from commercial banks	241.7	239.8	254.0	281.1	315.4	324.4	330.6	318.9	334.1	342.8
Net credit to local government and EBFs	-24.1	-76.4	-121.6	-155.8	-178.9	-178.9	-199.2	-209.6	-224.9	-200.2
Credit to the economy	581.6	622.9	704.1	814.4	944.0	955.6	992.0	1057.6	1071.4	1112.2
Loans in foreign currency 1/	230.2	231.0	239.9	268.5	268.8	280.3	280.3	280.3	280.3	280.3
(Memorandum item: in US$ billions)	*8.5*	*8.6*	*8.9*	*9.9*	*10.0*	*10.0*	*10.0*	*10.0*	*10.0*	*10.0*
Other loans	351.5	391.8	464.1	545.9	675.3	675.3	711.6	777.3	791.0	831.8
Other items (net)	-208.9	-249.6	-278.6	-350.2	-404.3	-489.8	-499.5	-508.3	-517.8	-525.5
Memorandum items:										
Seasonally adjusted ruble broad money velocity 2/	7.8	7.9	7.4	7.2	7.0	...	6.8	6.6	6.2	6.1
Ruble broad money velocity (12 mnth change) 2/	9.3	4.7	-4.9	-9.2	-10.7	...	-13.4	-10.3	-13.7	-12.8
Real ruble broad money (rel. to CPI, 12 mnth change) 2/	11.8	29.6	30.7	40.1	39.1	...	31.9	24.3	16.4	11.1
Ruble broad money multiplier	2.17	2.36	2.25	2.27	2.20	...	2.35	2.27	2.27	2.26
currency-to-deposit	0.61	0.50	0.56	0.55	0.58	...	0.51	0.55	0.55	0.55

Sources: Russian authorities; and Fund staff estimates.

1/ At fixed accounting exchange rates (Rub 27/US$ and US$1.37/SDR for Dec. 1999 revalued and 2000, Rub 28.16 and US$1.30291 for Dec. 2000 revalued and 2001).
2/ December 1999 calculations exclude Rub 20 billion from broad money as an estimate for the temporary increase in liquidity associated with Y2K concerns.

Table 6. Russian Federation: Quarterly Balance of Payments, 1999-2001
(In billions of U.S. dollars, unless otherwise indicated)

	1999	2000					2001				
		Q1	Q2	Q3	Q4 Proj.	2000 Proj.	Q1 Proj.	Q2 Proj.	Q3 Proj.	Q4 Proj.	2001 Proj.
Current account	22.9	10.7	10.5	11.4	12.8	45.3	9.3	9.5	7.8	9.0	35.6
Trade balance	36.2	14.4	14.6	15.8	16.1	60.9	13.9	13.2	13.0	12.4	52.6
Exports	75.8	24.3	25.0	26.7	29.2	105.2	26.0	25.6	25.8	27.5	105.0
Non-energy	44.9	11.3	12.8	13.5	14.8	52.4	11.7	13.6	14.2	15.7	55.1
Energy	31.0	13.0	12.2	13.1	14.4	52.7	14.3	12.1	11.6	11.9	49.9
Oil	19.6	8.3	8.6	9.6	9.5	36.1	7.5	7.8	7.9	6.9	30.1
Gas	11.4	4.7	3.6	3.5	4.9	16.6	6.8	4.3	3.7	5.0	19.8
Imports	-39.6	-9.9	-10.4	-10.9	-13.1	-44.2	-12.1	-12.5	-12.7	-15.1	-52.4
Services (net)	-13.9	-3.8	-4.2	-4.4	-3.3	-15.6	-4.6	-3.6	-5.1	-3.3	-16.7
Nonfactor services	-3.9	-1.5	-2.0	-2.1	-2.5	-8.1	-1.9	-2.4	-2.4	-2.7	-9.4
Factor services	-10.0	-2.3	-2.2	-2.2	-0.8	-7.5	-2.7	-1.3	-2.7	-0.6	-7.3
Public sector interest	-8.8	-2.1	-2.1	-2.2	-0.9	-7.3	-2.5	-1.1	-2.7	-0.8	-7.1
Other factor services	-1.2	-0.2	-0.1	0.0	0.1	-0.2	-0.2	-0.2	0.0	0.2	-0.2
Current transfers	0.5	0.0	0.1	0.0	-0.1	0.0	-0.1	0.0	-0.1	-0.1	-0.3
Capital account	-16.3	-5.9	-2.7	-5.3	-8.3	-22.2	-7.9	-5.8	-7.0	-5.9	-26.6
Public sector capital	-1.6	-1.0	-0.6	-2.5	-0.9	-5.0	-1.0	-0.1	-1.2	-1.4	-3.7
Budgetary	-5.4	-0.6	-0.7	-1.5	-0.1	-3.0	-1.0	-0.1	-1.2	-1.4	-3.7
Disbursements	2.1	0.5	0.1	0.4	0.5	1.4	0.3	0.4	0.3	0.2	1.2
Amortization	-7.5	-1.1	-0.8	-1.9	-0.6	-4.4	-1.3	-0.5	-1.4	-1.6	-4.8
Non-budgetary	3.8	-0.3	0.0	-0.9	-0.8	-2.0	0.0	0.0	0.0	0.0	0.0
Private sector capital	-14.7	-4.9	-2.1	-2.9	-7.3	-17.2	-6.9	-5.7	-5.8	-4.5	-22.9
o/w Direct investment	0.7	0.1	0.3	0.3	0.6	1.3	0.4	0.5	0.6	0.8	2.3
Errors and omissions, net	-7.5	-2.7	-1.9	-3.0	-1.5	-9.1	0.0	0.0	0.0	0.0	0.0
Overall balance	-0.9	2.1	5.8	3.0	3.0	14.0	1.4	3.7	0.8	3.1	9.0
Financing	0.9	-2.1	-5.8	-3.0	-3.0	-14.0	-1.4	-3.7	-0.8	-3.1	-9.0
Net international reserves 1/	-5.4	-4.1	-6.3	-4.9	-3.3	-18.7	-1.4	-3.7	-0.8	-3.1	-9.0
Gross reserves (- increase)	-1.7	-3.2	-5.4	-4.2	-2.9	-15.7	-1.1	-3.4	-0.6	-2.5	-7.6
Net Fund liabilities	-3.6	-0.9	-0.9	-0.7	-0.6	-3.0	-0.3	-0.2	-0.2	-0.6	-1.4
Other liabilities	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valuation adjustment	0.1	0.1	-0.7	0.3	0.0	-0.4	0.0	0.0	0.0	0.0	0.0
Exceptional financing	6.3	1.9	1.3	1.6	0.3	5.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:											
Current account (in percent of GDP)	12.5	21.9	19.1	16.4	17.2	18.3	13.7	13.2	10.0	11.3	12.0
Gross reserves 1/	12.5	15.6	21.1	25.3	28.2	28.0	29.1	32.5	33.0	35.5	35.5
(in months of imports of GNFS)	2.8	3.6	4.3	4.8	4.8	5.5	5.5	5.6	5.4	5.3	6.0
Net private capital outflows (in percent of trade)	19.3	22.3	11.4	15.6	20.9	17.6	18.1	15.0	15.1	10.6	14.6
Russian oil price ($/barrel)	14.7	23.8	23.4	24.9	26.2	24.6	21.4	20.6	20.0	19.5	20.4
World oil price ($barrel)	18.0	26.6	26.8	29.8	29.7	28.2	25.5	24.6	23.9	23.3	24.3
External debt service payments	20.3	3.9	4.7	4.5	2.6	15.7	5.6	2.9	5.8	3.9	18.2
(percent of exports of goods and services)	23.9	15.0	17.1	15.4	8.4	13.8	20.0	10.4	20.0	13.0	15.8
Public external debt	154.6	...	...	...	...	140.7	...	...	...	...	137.1
(percent of GDP)	84.3	...	...	...	...	56.9	...	...	...	...	46.2
Potential Debt Service (COMECON/FTO) 2/	...	...	...	...	...	...	...	...	...	...	1.49
Principal	...	...	...	...	...	...	...	...	...	...	0.38
Interest	...	...	...	...	...	...	...	...	...	...	1.11

Sources: Central Bank of Russia; and Fund staff estimates.

1/ Quarterly data are calculated at constant cross exchange rates; annual data at end-period rates.
2/ Payments on certain COMECON debts and obligations to uninsured suppliers (FTO) are currently under discussion.

Table 7. Russian Federation: Medium-Term Balance of Payments Projections, 2000-06
(In billions of U.S. dollars, unless otherwise indicated)

			Projection				
	2000	2001	2002	2003	2004	2005	2006
Current account	45.3	35.6	26.5	19.5	14.9	12.8	11.1
Trade balance	60.9	52.6	44.0	37.5	33.6	32.5	31.7
Exports	105.2	105.0	103.0	102.2	104.4	109.3	115.3
Non-energy	52.4	55.1	59.0	63.0	67.1	72.5	78.9
Energy	52.7	49.9	44.1	39.2	37.2	36.8	36.4
Oil	36.1	30.1	27.1	25.0	24.4	24.1	24.1
Gas	16.6	19.8	17.0	14.2	12.8	12.7	12.3
Imports	-44.2	-52.4	-59.0	-64.8	-70.8	-76.8	-83.6
Services (net)	-15.6	-16.7	-17.2	-17.7	-18.4	-19.3	-20.2
Nonfactor services	-8.1	-9.4	-10.3	-11.1	-12.0	-12.8	-13.8
Factor services	-7.5	-7.3	-6.9	-6.6	-6.4	-6.5	-6.4
Public sector interest	-7.3	-7.1	-6.9	-6.8	-6.6	-6.8	-6.8
Other factor services	-0.2	-0.2	0.0	0.2	0.2	0.3	0.4
Current transfers	0.0	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3
Capital account	-22.2	-26.6	-19.2	-16.4	-10.4	-7.9	-0.3
Public sector capital	-5.0	-3.7	-0.8	-3.8	-0.5	-0.6	0.6
Budgetary	-3.0	-3.7	-0.8	-3.8	-0.5	-0.6	0.6
Disbursements	1.4	1.2	2.9	4.9	3.9	6.9	6.9
Amortization	-4.4	-4.8	-3.7	-8.6	-4.3	-7.5	-6.3
Non-budgetary	-2.0	0.0	0.0	0.0	0.0	0.0	0.0
Private sector capital	-17.2	-22.9	-18.4	-12.6	-9.9	-7.3	-0.9
o/w Direct investment	1.3	2.3	3.2	4.2	5.1	6.1	6.2
Errors and omissions, net	-9.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	14.0	9.0	7.3	3.1	4.5	4.9	10.8
Financing	-14.0	-9.0	-7.3	-3.1	-4.5	-4.9	-10.8
Net international reserves	-18.7	-9.0	-7.3	-3.1	-4.5	-4.9	-10.8
Gross reserves (- increase)	-15.7	-7.6	-4.5	-0.2	-3.0	-3.8	-9.8
Net Fund liabilities	-3.0	-1.4	-2.8	-2.9	-1.5	-1.1	-1.0
Other liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valuation adjustment	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional financing	5.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:							
Current account (in percent of GDP)	18.3	12.0	8.2	5.6	3.9	3.1	2.5
Gross reserves	28.0	35.5	40.0	40.2	43.3	47.0	56.8
(in months of imports of GNFS)	5.5	6.0	6.0	5.5	5.5	5.5	6.1
Net private capital outflows (in percent of trade)	17.6	14.6	11.3	7.5	5.6	3.9	0.5
Russian oil price ($/barrel)	24.6	20.4	18.3	16.9	16.5	16.3	16.3
World oil price ($barrel)	28.2	24.3	21.9	20.2	19.8	19.5	19.5
External debt service payments	15.7	18.2	18.2	23.3	17.4	19.2	18.0
(percent of exports of goods and services)	13.8	15.8	16.1	20.6	14.9	15.7	13.9
Public external debt	140.7	137.1	136.2	132.5	132.0	131.3	131.9
(percent of GDP)	56.9	46.2	42.1	37.8	34.7	31.8	29.2
Potential Debt Service (COMECON/FTO) 1/	...	1.49	1.70	1.99	2.09	2.12	...
Principal	...	0.38	0.35	0.67	0.82	0.91	...
Interest	...	1.11	1.35	1.32	1.27	1.21	...

Sources: Central Bank of Russia; and Fund staff estimates.

1/ Payments on certain COMECON debts and obligations to uninsured suppliers (FTO) are currently under discussion.

Table 8. Russian Federation: Indicators of Fund Credit, 1998-2008

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
	Outstanding Fund credit (in percent of)										
Quota	318.4	186.7	149.9	131.2	95.3	57.4	38.6	24.3	11.3	3.6	0.0
Exports	23.0	19.1	10.7	9.3	6.9	4.1	2.7	1.6	0.7	0.2	0.0
Gross reserves	183.7	130.1	43.7	30.1	19.4	11.6	7.3	4.2	1.6	0.5	0.0
Total external debt	10.9	8.7	7.0	6.3	4.6	2.9	1.9	1.2	0.6	0.2	0.0
Total official external debt	12.7	10.5	8.5	7.6	5.5	3.4	2.3	1.5	0.7	0.2	0.0
	Fund charges and repurchases (in percent of)										
Quota	27.9	61.0	45.6	26.3	42.1	42.0	21.4	16.1	14.0	8.1	3.6
Exports	1.9	5.8	3.3	1.8	2.9	2.9	1.4	1.0	0.8	0.5	0.2
Gross reserves	15.1	39.8	13.3	5.7	8.1	8.1	3.8	2.6	1.9	1.0	0.4
	(In billions of U.S. dollars)										
Total liabilities to the Fund	20.0	16.2	12.2	10.7	7.8	4.7	3.1	2.0	0.9	0.3	0.0
Fund purchases	6.2	0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fund repurchases	0.9	4.2	3.0	1.4	2.8	2.9	1.5	1.1	1.0	0.6	0.3
Fund charges	0.7	0.7	0.7	0.6	0.5	0.3	0.2	0.1	0.1	0.0	0.0
Memorandum items:											
Quota (SDR billion)	4.3	5.9	5.9	5.9	5.9	5.9	5.9	5.9	5.9	5.9	5.9
U.S. dollar/SDR exchange rate (period average)	1.4	1.4	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3

Sources: Russian authorities; and Fund staff estimates and projections.

Table 9. Russian Federation: Indicators of External and Financial Vulnerability, 1998-2001
(In units as indicated)

	1998	1999				2000				2001
	Dec.	March	June	Sept.	Dec.	March	June	Sept.	Dec.	March
External indicators										
Exports (12 month growth, US$) 1/	-23.9	-16.2	-9.9	4.9	25.6	56.2	46.9	40.3	20.4	7.1
Imports (12 month growth, US$) 1/	-55.8	-49	-41.8	-29.4	16.8	8.6	2.3	14.8	19.9	22.3
Current account balance (12-month, US$) 1/	-1.6	5.1	12.6	18.7	22.9	31.1	37.7	43.4	45.4	44.0
(percent of GDP) 1/	-0.5	1.9	6.2	10.4	12.3	15.7	18.0	19.2	18.4	16.5
Russian oil price ($/barrel)	8.7	8.7	12.1	17.1	21.3	23.8	23.4	24.9	26.2	21.4
Gross official reserves (US$ bn)	10.9	9.6	11.1	11	12.6	15.6	21.1	25.3	28.0	29.9
(in months of imports of GNFS)	1.8	2.5	2.5	2.5	2.6	3.6	4.3	4.8	4.8	5.5
(ratio to short-term debt) 2/	87.0	68.3	91.8	89.2	127.5	164.0	244.1	328.9	321.3	292.6
(ratio to reserve money) 3/	107.0	112.7	103.7	106.3	104.9	139.2	149.1	160.8	151.8	172.0
NIR of monetary authorities (US$ bn)	-8.4	-9.0	-7.3	-6.1	-2.8	1.3	7.6	12.5	16.3	18.0
NFA of commercial banks (US$ bn)	1.1	2.3	3.3	5.2	5.5	7.3	7.7	8.3	8.1	10.9
Total external debt (US$ bn)	189.9	...	...	...	185.7	...	...	...	171.8	...
o/w public sector	158.2	...	...	...	154.6	...	...	...	140.7	...
External debt/exports of GNFS	217.5	...	...	...	218.7	...	...	...	150.2	...
External debt/GDP	60.1	...	...	...	99.9	...	...	...	69.4	...
Total external debt service to exports of GNFS	27.6	32.8	33.3	11.1	21.8	15.0	17.1	15.4	8.4	20.0
Foreign currency debt rating	CCC- neg	Sel. Def.	Sel. Def.	Sel. Def.	Sel. Def.	Sel. Def.	Sel. Def.	B-	B-	B-
Spread of benchmark bond	n.a.	3,646	1,901	2,336	1,240	1,021	1,016	966	1,163	1,142
Exchange rate (per US$; end of period)	20.7	24.2	24.2	25.1	27.0	28.5	28.1	27.8	28.2	28.8
Real Effective Exchange Rate (1 year growth; period average)	-40.2	-43.6	-39.1	-26.2	6.4	6.7	6.6	12.2	23.1	27.8
Financial sector										
M2 growth (12 month growth)	20.9	31.4	54.0	63.3	57.2	58.6	57.1	66.1	62.4	53.0
Growth of credit to private sector	33.1	55.1	57.8	26.9	50.6	49.1	58.9	69.2	64.3	63.2
Share of foreign currency loans in total lending 3/	56.7	54.1	45.3	40.9	39.6	38.3	35.0	33.6	29.3	28.9
Share of foreign currency deposits in total deposits 3/	44.0	43.6	41.4	39.3	40.4	40.7	39.0	39.3	37.2	39.8
Share of ruble demand deposits in total Ruble deposits	61.6	58.9	59.5	58.3	60.1	59.1	59.7	61.6	63.0	60.5
Total domestic debt (Rub billion)	537.8	...	...	...	583.6	573.4	571	560.9	557.4	555.6
(percent of GDP)	19.9	...	...	...	12.7	11.1	10.1	8.9	8.0	7.4
Stock market index (US$ terms) 4/	58.9	80.4	125.7	83.1	150.0	231.9	171.4	199.1	143.3	169.5

Sources: Russian authorities; and Fund staff estimates.

1/ Data for March 2001 are projections.
2/ Short-term debt is estimated on official debt service falling due in the next 12 months.
3/ At end of period exchange rates.
4/ RTS index.

Table 10. Russian Federation: Macroeconomic Framework, 1999-2015

	1999	2000	2001	2002	2003	2004	2005	Average 2006-15
		Est.			Projections			
	(In percent of GDP, unless otherwise indicated)							
I. Savings-Investment Balances								
General Government								
Consumption	15.6	14.0	12.5	12.6	12.5	12.3	11.9	9.2
Gross investment	8.5	8.0	7.6	8.0	8.4	8.7	8.9	7.2
Net income from abroad	-4.6	-2.9	-2.4	-2.1	-1.9	-1.7	-1.6	-1.1
National savings	5.2	10.9	8.6	8.5	9.1	9.6	10.0	7.5
National savings - investment	-3.3	3.0	1.0	0.4	0.6	0.9	1.1	0.3
Private Sector								
Consumption	51.9	46.7	52.6	55.6	57.3	58.6	59.3	63.6
Gross investment	6.6	10.0	12.6	13.4	14.2	14.7	15.2	17.6
Net income from abroad	-0.4	-0.1	-0.2	-0.1	-0.1	-0.1	0.0	0.2
National savings	22.2	25.4	23.6	21.2	19.1	17.7	17.2	18.7
National savings - investment	15.6	15.4	11.0	7.8	4.9	3.0	2.0	1.1
Overall Economy								
Consumption	67.6	60.7	65.2	68.1	69.9	70.9	71.2	72.8
Gross investment	15.1	18.0	20.2	21.4	22.6	23.4	24.1	24.8
Net income from abroad	-5.0	-3.0	-2.6	-2.2	-2.0	-1.8	-1.6	-1.0
National savings	27.4	36.3	32.2	29.6	28.1	27.3	27.1	26.2
National savings - investment (current account)	12.3	18.3	12.0	8.2	5.6	3.9	3.1	1.4
	(In percent of GDP, unless otherwise indicated)							
II. Federal government accounts and debt indicators								
Revenues	13.2	16.2	15.6	16.8	18.1	18.2	17.8	16.8
Primary balance, commitments	1.8	5.3	3.9	3.0	2.6	2.3	2.1	1.2
Overall balance, commitments	-4.4	1.0	0.8	0.0	0.0	0.0	0.0	0.0
Foreign financing 1/	0.2	-0.9	-1.2	-0.3	-1.1	-0.1	-0.2	-1.0
Domestic financing 1/	1.2	-1.0	1.0	0.3	1.1	0.1	0.2	0.9
Total federal govt domestic debt	12.8	7.7	7.1	6.8	6.9	5.9	4.8	6.6
Total federal govt external debt	84.3	56.9	46.2	42.1	37.8	34.7	31.8	20.8
External federal govt debt service / revenues (%) 2/	35.1	25.9	28.0	22.0	27.5	18.4	20.9	10.2
External federal govt debt service / expenditures (%) 2/	31.8	29.4	28.5	22.0	27.5	18.4	20.9	10.2
	(In billions of U.S. dollars, unless otherwise indicated)							
III. Balance of payments and external debt								
External current account	22.9	45.3	35.6	26.5	19.5	14.9	12.8	8.5
Change in external terms of trade (%)	14.4	40.7	-1.3	-4.6	-4.1	-2.0	-0.4	0.7
Change in Russian crude oil price (%)	40.5	66.9	-17.2	-9.9	-7.8	-2.2	-1.3	2.1
Change in export volumes (%)	9.4	5.1	0.5	1.6	2.5	3.1	4.0	5.8
Change in non-energy export volumes (%)	14.7	11.4	4.0	5.0	4.9	4.9	6.2	8.2
Change in import volumes (%)	-15.6	19.0	17.7	11.2	8.6	8.2	7.4	8.3
Private net capital flows (including errors & omissions)	-22.3	-26.3	-22.9	-18.4	-12.6	-9.9	-7.3	-2.8
o/w gross FDI inflows	2.8	2.8	3.8	4.8	5.8	6.8	7.8	8.6
Official reserves	12.5	28.0	35.5	40.0	40.2	43.3	47.0	81.6
in months of imports	2.8	5.5	6.0	6.0	5.5	5.5	5.5	5.8
External debt service / exports of goods and services (%)	23.9	13.8	15.8	16.1	20.6	14.9	15.7	12.5
Balance of payments: exceptional financing / financing gap 3/	6.3	5.0	0.0	0.0	0.0	0.0	0.0	0.0
	(In percent, unless otherwise indicated)							
IV. Growth and prices								
Real GDP growth	3.5	7.7	4.0	4.0	4.0	4.5	5.0	6.0
CPI Inflation, end of period	36.6	20.1	14.0	11.1	8.8	7.9	7.0	7.0
Real effective exchange rate, period average, change	-29.5	12.3	16.6	5.1	2.0	2.0	1.5	1.0
Real effective exchange rate, end of period, change	11.6	22.9	9.0	2.0	2.0	2.0	1.0	1.0

Source: Fund staff estimates and projections based on official data.

1/ Net Fund financing is included in domestic financing, as a component of CBR credit; foreign financing therefore excludes the Fund.

2/ From 2001 onward, before any rescheduling. Excludes debt service in kind ($1.2 billion per annum until 2010). Includes debt service to the Fu

3/ For 2000 and before, refers to the (identified) exceptional financing. For subsequent years, refers to the (unidentified) financing gap.

GOVERNMENT OF THE RUSSIAN FEDERATION

Moscow

Mr. Horst Köhler
Managing Director
International Monetary Fund
700 19th Street, N. W.
Washington, D. C. 20431 USA

April 23, 2001

Dear Mr. Köhler,

The Government of the Russian Federation hereby forwards for your information the Statement of the Government of the Russian Federation and the Central Bank of Russia on Economic and Financial Policies for 2001 and Outline of Medium-Term Strategy.

This Statement is based on the comprehensive program of medium- and long-term social and economic development approved by the Government of the Russian Federation, and is targeted at promoting economic growth and macroeconomic stability, improving the investment climate and raising people's living standards. Broad understanding was reached with IMF staff on the structural reform measures and economic policy objectives in 2001 and for the medium term contained in the Statement.

The Government of the Russian Federation and the Central Bank of Russia intend to continue their cooperation with the IMF and will take measures to enhance transparency in implementing fiscal and monetary policy. To this end, we will begin reporting to the IMF on international reserves and foreign exchange liquidity in compliance with the Special Data Dissemination Standard, continue the practice of providing information about the status of the economic program to the Fund, and continue consultations with Fund staff.

Sincerely yours,

A. Kudrin
Deputy Prime Minister
Minister of Finance
of the Russian Federation

Statement of the Government of the Russian Federation and the Central Bank of Russia on Economic and Financial Policies for 2001 and Outline of Medium-Term Strategy

I. Introduction

1. The period 1999–2000 saw a steady adjustment to the financial crisis of 1998. This reflects the marked improvement in external competitiveness, the prudent conduct of macroeconomic policies, and a significant improvement in the external environment. Real GDP expanded by 7.7 percent in 2000, the external current account swung into a large surplus of over 17 percent of GDP, there was a large build-up of international reserves, and inflation moderated to 20 percent. Large revenue gains resulted in a primary surplus of the federal government of 5 percent of GDP. However, growth slowed down during the closing months of 2000, and while inflation was subdued in 2000 there was a marked uptick in the beginning of this year.

2. While relatively high energy prices in world markets may continue to provide some breathing space in the short run, progress with securing growth and macroeconomic stability will require that the existing problems in the economy are tackled and structural reforms accelerated. Against this background, the government has formulated a comprehensive medium- and long-term economic and social reform program, and a short-term action plan for the period through 2001. The strategic medium-term objective of social and economic development is to achieve a significant increase in per capita incomes over the next ten years, a radical lowering of poverty, and a scaling down of income disparity. The program rests on four main pillars: (i) consolidating macroeconomic stability; (ii) creating a favorable business and investment climate; (iii) reforming the structure and institutions in the economy; and (iv) raising the efficiency of social support.

3. Our macroeconomic strategy is based on the achievement of sustainable growth, continuing the process of disinflation and strengthening our external position so as to reduce the vulnerability of the economy.

4. We believe that the basic elements in improving the investment climate include strengthening and protecting private property rights, reducing administrative intervention in economic activities, and developing financial markets and institutions. Key reforms in this respect include enacting a Land Code, strengthening the bankruptcy law and anti-monopoly legislation, lowering barriers to entry to the Russian market, and the continued privatization of state-owned enterprises. The strict enforcement of laws and strengthening of judicial institutions and processes will be essential to support this process.

5. In the enterprise sector, infrastructure monopolies will be reformed through restructuring and exposing them to competition, while the efficiency of government regulation will be enhanced. The process of restructuring the large number of enterprises,

especially in the state sector, that are not competitive and which rely on direct or indirect support from budgets at various levels will be accelerated.

6. In the area of social policy, the government intends to improve the targeting of social protection expenditures by moving from implicit subsidies and category-based benefits to means-tested social assistance by building on the existing system of housing allowances. Resource allocation to the education and health sectors needs to be improved, aimed at ensuring the provision of a basic package of services and increasing investment in these sectors.

7. The measures elaborated below comprise the main elements of our economic strategy targeted at ensuring the sustainability of macroeconomic and financial stability. The measures include the maintenance of prudent fiscal and monetary policies, a comprehensive fiscal reform, further progress in banking reform, and resolution of the nonpayments problem. We will also take further steps to enhance governance and transparency in policy-making institutions.

II. Macroeconomic Strategy

A. Medium-Term Strategy

8. We believe that firm implementation of the comprehensive program will support a strong economic performance over the medium term, with real GDP growth averaging 4-5 percent per year while inflation is reduced to 7–8 percent. Growth should be led by private investment as structural reforms take hold and the investment climate strengthens, with considerable scope for a significant increase in private consumption as productivity and real incomes improve. The external current account will weaken gradually as investment and imports pick up—reflecting in part the expected continued real appreciation of the ruble—but the balance of payments position should remain strong as foreign direct investment increases, private capital outflows decline, and access to international capital markets is gradually restored. This will allow us to build up our reserve position and settle our liabilities to external creditors.

9. In order to reduce Russia's debt burden and enhance fiscal and external viability, the government is committed to achieving balanced budgets over the medium term, taking into account a reduction in the tax burden and associated decline in government revenues as well as allocation of additional resources to reform-related expenditures, including on social safety nets. This will require a streamlining of public expenditure commitments and concentration of spending on priority areas, as well as measures to strengthen revenues through enhancement of tax compliance. The government will also continue to work toward more efficient and transparent systems of interbudgetary relations and management of state finances. The pursuit of these policies will enable the government to strengthen fiscal and external viability over the medium term, with the burden of public debt obligations falling gradually.

10. When formulating our medium-term economic strategy, we have taken into account various factors affecting our economic development. Notably, the economy remains dependent on volatile commodity exports most of which are primary goods, which have a direct impact on the balance of payments and fiscal position. The year 2003 will be particularly vulnerable as large external debt repayments fall due.

B. Macroeconomic and Financial Policies in 2001

11. Our key macroeconomic objectives for 2001 are to consolidate the recent favorable trends in output and financial stabilization. The main parameters of our macroeconomic program are: (i) real GDP growth of 4 percent in 2001; (ii) a decline in inflation to 14 percent by end-2001 (December to December); and (iii) a continued accumulation of net international reserves of $9 billion, with gross reserves rising to the equivalent of about six months of imports at end-2001.

Fiscal policy

12. Budget policies hinge on continued reform of the tax system, expenditure policies, and financial relations between the different levels of government, and a reduction in unfunded federal expenditure mandates. The federal budget approved for 2001, together with recently adopted amendments, foresees a primary surplus of 4 percent of GDP. The government intends to fully service its external debt in 2001, and is continuing consultations with official and other creditors on the regularization of its Soviet-era debt.

13. The tax policy reform initiated in mid-2000 entails a reduction in both the overall tax burden and the number of individual taxes, as well as streamlining of the tax system. This reform, together with changes in macroeconomic variables, will lead to a projected decline in enlarged government revenues of 3–4 percent of GDP in 2001. However, implementation of the tax reform should also provide for increased compliance and create incentives for the legalization of incomes, which should eventually reduce budget revenue losses.

14. At the same time, there will be a shift of spending toward the federal level reflecting in part increased transfers to regions to compensate for the decline in their own revenues and to finance remaining expenditure mandates. Other federal non-interest expenditures are to remain roughly constant as a percentage of GDP compared to 2000.

15. Most of the revenue decline will occur at the level of subnational budgets, which will require a streamlining of their expenditures in order to maintain overall balance. In this regard, local and regional governments are expected to reduce their spending by 2 percent of GDP. The government expects that savings could be achieved in 2001 from increased cost recovery in housing and utilities, and believes that there is scope to reduce expenditures in regional Road Funds. At the same time, federal transfer policies have been adopted to shift resources toward poorer regions in order to avoid recourse to unsustainable expenditure cuts or arrears.

Monetary and exchange rate policies

16. Monetary and exchange rate policies will be geared to achieving a reduction of inflation. While a modest further real appreciation of the ruble is consistent with our medium-term growth objectives, a significant real appreciation could threaten the recovery. Thus, the CBR will intervene in the foreign exchange market to smooth fluctuations in the exchange rate consistent with the targeted accumulation of net international reserves (NIR). Taking into account our assessment of the recovery in money demand, these interventions will be partially sterilized to achieve the assumed base money path. In doing so, we will closely monitor inflationary pressures and the evolution of base money and take appropriate measures to ensure that the programmed inflation target is met.

17. The monetary program is complicated by a combination of a relatively strong balance of payments and uncertainties about money demand. Should balance of payments developments be more favorable than assumed, putting excessive upward pressures on the ruble, the CBR will initially increase NIR above the programmed floor, and undertake equivalent sterilization to keep base money on the assumed path through the use of its market-based instruments. However, in light of the limitations on the CBR's capacity to use such instruments, continued balance of payments pressures would require contribution from fiscal policy through the government keeping budgetary revenues over and above program assumptions on deposit with the CBR.

18. The facilitate the conduct of monetary policy by the CBR, the government and the CBR will seek adoption of legal and regulatory changes exempting the CBR from taxation of its bonds. By end-June 2001, proposals to amend the Law on the Central Bank and the Law on the Securities Market will be submitted to the Duma in order to remove residual restrictions on the issuance of such bonds (both in terms of volumes and the period within which issuance is permitted). The CBR will make use of increased reserve requirements only in exceptional circumstances.

19. The government intends to regularize its financial relations with the CBR in order to strengthen the efficiency of monetary policy. On the basis of CBR financial statements for the year 1999, prepared in accordance with International Accounting Standards (IAS) except for the standards relating to consolidation and hyperinflation, the government will, if necessary, restructure a sufficient portion of its outstanding liabilities to the CBR into instruments carrying a market interest rate with a view to ensuring that the CBR is adequately capitalized. The interest payments on these instruments will be included in the 2002 budget. For its part, the CBR will continue to ensure adequate transparency of its activities, including the divestiture of its foreign subsidiaries according to the relevant legislation.

Balance of payments and exchange and trade policies

20. We expect that the strong balance of payments situation will continue in 2001. The external current account surplus reached a record high level exceeding 17 percent of GDP

in 2000, but is expected to decline somewhat in 2001 to about 12 percent of GDP. This reflects both an expected easing of energy prices and a continued recovery of imports, as well as a slowdown in non-energy export growth. Meanwhile, private capital outflows should decline somewhat as the investment climate firms and confidence in economic policies improves.

21. We will refrain from introducing any new exchange and trade restrictions. The government has drafted a law *On Counteracting Legalization (Laundering) of Income Obtained by Criminal Means* targeted against money laundering and has submitted it to the Duma. The government will seek the enactment of this law by end-June 2001. We will continue to cooperate with the members of the FATF.

22. In the trade area, the government will make preparations for WTO accession. As part of this process, the government has further harmonized and reduced import tariffs while streamlining exemptions. The number of tariff rates has been reduced from seven to four. Revised proposals on further custom tariff liberalization will be prepared by September.

III. Structural Reforms Aimed at Enhancing Medium-Term Stability

23. The main areas of structural reform in 2001 comprise fiscal reforms, banking system reform, and addressing the problem of nonpayments. Further, we will continue our efforts to improve transparency and governance.

A. Fiscal Reforms

24. In past years, the lack of a rational, market-based budget and taxation system at different levels of the budget system resulted in unrealistic expenditure commitments, variable and inequitable tax collections, and imperfect control over budgetary resources. The comprehensive program includes broad-based measures to address these problems, notably continuation of a tax reform and rationalization of budget spending, including a review of public expenditure efficiency and the elimination of unfunded budget expenditure mandates.

Priorities for 2001

25. Our priorities for fiscal reform are: (i) passage of the profit tax chapter of the Tax Code; (ii) further refining the provisions of Part I of the Tax Code; (iii) taking measures to improve tax administration; (iv) eliminating unfunded federal expenditure mandates; (v) targeting federal budget resources toward priority areas while reducing inefficient expenditures; (vi) establishing a clear relationship between expenditure mandates at the different levels of government; (vii) clearing all outstanding federal budget arrears; (viii) completing the coverage of the Federal Treasury system and encouraging treasury execution at the subnational government level; (ix) rationalizing the list of budgetary entities and budgetary recipients; and (x) ensuring transparency of all budgets and budgetary procedures.

Tax policy and administration

26. Reform of the tax system will be continued in 2001. The adoption of Part II of the Tax Code represents a substantial tax reform element targeted at providing incentives for economic growth. The Duma has already passed the four chapters covering the VAT, excise, income, and social insurance taxes, which have taken effect from January 1, 2001. These chapters provide for a broadening of the VAT base and the elimination of a number of unwarranted exemptions; movement to a destination basis of VAT and excises for nonenergy goods and services; increases in specific excise rates; unification of personal income tax rates at 13 percent; and a reduction in social security contributions from 39.5 to 35.6 percent of wage payroll. The federal law *On Making Effective Part Two of the Tax Code of the Russian Federation and Making Amendments in Some Legislative Tax Acts of the Russian Federation* also provides for a reduction in turnover taxes, which the government aims to phase out completely in 2003. Further, the government intends to submit the amendments needed to move VAT and key excises to an accrual basis from January 1, 2003.

27. During the first half of 2001, the government intends to seek enactment of the key profit tax chapter. Amendments to the profit tax will allow for deduction of all legitimate business costs and carry-forward of losses for ten years, and the phasing-out of various special allowances, including the investment allowance, and exemptions.

28. In 2001, the government intends to enact changes to Part I of the Tax Code that would allow the tax authorities to levy penalties and fines in accordance with established procedures without use of the courts (in cases when the taxpayer does not challenge the tax authorities' requirement to pay a fine); restrict the ability of taxpayers to knowingly channel tax payments through illiquid banks; and enhance the tax authorities' ability to counter tax evasion through transfer pricing and other transactions through connected parties.

29. We will also take a number of other steps to improve tax administration, including the reduction of the lag in providing VAT refunds to traditional exporters to less than two months in 2001, strengthening incentives for voluntary tax compliance, and promoting efficiency of local tax inspectorates including through their reorganization.

Budget expenditure and social policy

30. The government's expenditure strategy primarily aims to direct available resources to the basic functions of the government, including social assistance, health, education, and law and order, and to reduce inefficient spending, such as general subsidies to enterprises and households. The government will undertake regional and sectoral Public Expenditure Reviews during 2001, which will be used as inputs for the draft federal budget for 2002 and beyond.

31. The government's key objective for reforming the social system is to ensure effective protection for the most vulnerable households, including through providing adequate and sustainable pension benefits and social assistance and universal access to basic social goods,

notably in the area of education and health care. The rest of social services should largely be provided on a commercial basis.

32. As of January 1, 2001, most unfunded federal mandates were suspended. During 2001, the government intends to find a solution for the suspended unfunded mandates and eliminate or finance remaining unfunded federal mandates from January 1, 2002.

33. In 2001, we intend to further decompress pension benefits while raising the living standard of the poorest pensioners. In the coming years we also intend to carry a comprehensive pension reform that would include the creation of mandatory individual savings accounts.

34. Current housing policies are not efficient enough and result in substantial spending from regional budgets. In addition to a wide range of reforms aimed at ensuring ownership rights and creating a well functioning market for housing services, federal transfer policies toward regional budgets will be based on the assumption that the Federation member territories will follow the approved federal standard envisaging a phased transition to full cost recovery for financing housing and communal services by 2004. At the same time, low-income families will be compensated for the increased costs of housing and utilities, including through subsidies for housing and communal services.

35. In the area of industrial policy, the government will review the possibilities of subsidized redundancy payments and retraining and relocation assistance. This refers especially to one-company towns in the Northern Territories. The government will also take measures to improve labor market flexibility, including conducting a review of the unemployment benefit system and seeking to adopt by end-2001 a new code of labor laws that will improve the system of hiring and shedding of labor.

Budget expenditure management

36. Measures to improve the management and control of budgetary expenditures are a key element in the government's fiscal strategy for 2001. The government has instituted an inventory of all organizations financed from the federal budget, separating recipients into budgetary entities, for which the government has financial responsibility, and other recipients, financing for which has been converted from a line-item to allocation of amounts for payment for the state order so as to remove any residual claim on the budget. This inventory will be completed, and corresponding measures taken for the remaining recipients, during the preparations for the 2002 budget. All off-budgetary accounts of budgetary entities will be moved onto the Federal Treasury by end-2001. Beginning in 2002, the government intends to reorganize budgetary institutions that are primarily commercial in nature into commercial organizations. Finally, all allocations of funds to third-tier recipients of the Ministry of Defense will be executed through the Federal Treasury by end-September 2001, and the operations of the Ministry of Defense will be fully executed by the Treasury from January 1, 2002.

37. During 2000, most of the outstanding payment arrears of the federal budget recognized as of January 1, 2000, were cleared, and the federal budget for 2001 provides that the remainder of arrears will be paid and some securitized during the first half of 2001. To prevent the accumulation of new payment arrears, the threshold for recording of expenditure commitments by the Federal Treasury of budgetary entities' utility payments, which currently stands at Rub 20,000, will be eliminated by July 1, 2001.

B. Banking System Reform

38. The evolution of the banking system indicates a gradual recovery of banking activity after the 1998 crisis. At the same time, measures to further improve the legal framework of banking activity are required to improve the efficiency of the banking system. Our aims in this area are to develop a more efficient and competitive banking sector; promote its stability; minimize systemic bank risks; raise the efficiency of bank intermediation of household and corporate deposits on the one hand and loans and investments on the other; rehabilitate and promote investor confidence in the Russian banking system, including among foreign investors and depositors, and households; prevent cases of tax evasion through the banking system; and further improve the corporate governance of state-owned banks. To this end, we will take measures to adopt federal laws to protect the rights of creditors and depositors; enhance banking supervision; eliminate non-viable banks; and enhance business qualifications of banking supervisors. Measures will be taken to further develop transparent banking practices, improve banks' corporate structure, and establish a level playing field for banks regardless of their form of ownership.

39. We are committed to intensifying the pace of reforms in the banking sector and will develop the strategy of its development. The government policy in the banking sector will hinge on maintaining and promoting market principles in banking, avoiding direct methods of regulation of banks' operations. The government and the CBR will fulfill their role by improving the statutory framework for the operations of banks and ensuring compliance with regulatory and statutory acts. The state's direct involvement in the operations of the banking system through ownership of lending institutions will be reduced. In the course of conducting its policy in the banking sector, the government will ensure that: (i) third parties will not interfere in the operations of banks unless warranted by law; (ii) a uniform approach will be taken to individual banks or their clients; (iii) anti-monopoly regulation will be strictly enforced to promote competition in financial markets; (iv) the legislative framework for banking supervision will be further developed to prevent the use of the banking sector for illegal and suspicious transactions, including those targeted at money laundering.

Legal and institutional framework

40. Amendments to the Bank Bankruptcy Law, the CBR Law, and the Law on Banks and Banking Activity drafted by the government and the CBR was adopted by the State Duma in a second reading in April 2001. It is assumed that the aforementioned laws will become effective as of end-June 2001. These amendments establish capital adequacy as grounds for mandatory revocation of a bank's license and procedures for subsequent termination of the

bank's operations; compel banks to write down charter capital to be no greater than the CBR's determination of their equity capital; tighten bank licensing procedures, in particular by strengthening the criteria for "fit and proper" managers and owners (shareholders) of banks; and strengthen bank reporting. The aforementioned amendments are targeted at streamlining procedures for the termination of bank activities following revocation of their licenses, and facilitate the tackling of the most pressing corporate governance issues in the banking sector. One of the major issues of the banking sector reform is the adoption of amendments to the Law On Insolvency (Bankruptcy) and to the Civil Code targeted at improving the protection of secured creditors in bankruptcies (including bank bankruptcies). The government will seek to compile corresponding draft laws and take necessary efforts in order to have them adopted by the State Duma by end-December 2001. The government and the CBR will also take necessary steps in 2001 to amend the Law On the Central Bank of the Russian Federation to allow for the divestiture of the CBR's foreign subsidiaries.

41. The CBR and the government place special emphasis on improving the transparency of reporting and raising confidence in the banking sector in general. The CBR is developing a strategy and coordinating activities of loan institutions for moving existing accounting standards closer to IAS. For its part, the CBR will prepare financial statements for 2000 that are consistent with IAS, except for standards relating to consolidation and hyperinflation. The CBR's financial statements for 2001 will include additional improvements, bringing them closer to IAS. The CBR is closely monitoring a pilot project developed with the assistance of TACIS to reform existing systems of bookkeeping and reporting with a view to introducing enhanced reporting standards for banks from January 1, 2002. We will identify by end-December 2001 the legal and regulatory measures required for the full adoption of IAS reporting by banks and organizations, as well as develop a timetable for the removal of current impediments with a view to adopt IAS as of January 1, 2004.

42. Effective procedures for the liquidation of banks, whose licenses were revoked by the CBR, have not been established. In this context the government jointly with the CBR will draft measures streamlining bank liquidation procedures by end-June 2001, subject to the amendments of the banking legislation currently considered by the State Duma.

Dealing with problem banks

43. Following the adoption of the amendments to the Law on Bank Bankruptcy, the CBR Law, and the Law on Banks and Banking Activity, the CBR will work with bank owners to identify corrective actions to harmonize the authorized capital of certain banks with their equity capital, and if that proves impossible it will revoke licenses on the basis of the new banking legislation. The CBR will apply all actions allowed for under the federal legislation, including initiation of bankruptcy or liquidation proceedings against any banks, whose implementation of financial rehabilitation plans will be deemed unsatisfactory..

44. ARCO activities in bank restructuring and the placement of banks under its management will be conducted in accordance with Federal Law "On Restructuring of Loan Institutions." No banks have been referred to ARCO for restructuring since July 2000. The

major tasks for ARCO in 2001-2002 will therefore be to complete the restructuring of the banks already referred to it and prepare the banks currently being restructured under its ownership for re-privatization. The role of ARCO beyond this will be determined in the context of the common strategy paper for the development of the banking system.

Strategy for the banking sector

45. In the context of the implementation of a strategy for the banking sector, we will take measures to encourage recapitalizations and mergers and to remove obstacles to foreign participation in the banking system. Measures encouraging the adoption of IAS by enterprises, improving protection of creditor and investor rights will be undertaken over the medium term. By end-July 2001, the CBR will conduct a survey of banks with foreign share holding operating in Russia, on the basis of which the CBR jointly with the government will develop, by end-September 2001, measures facilitating their activities, including free repatriation of profits. We will not introduce restrictions on foreign participation in the banking sector.

46. Drawing in large part upon the CBR concept paper on the development of the banking sector, a common strategy paper will be approved by the government and the CBR by end-September 2001. The role of the major state-owned banks and measures to enhance the stability of private banks and competition will be taken into consideration during the development of the banking sector strategy. The government will refrain from creating new state-owned banks or conferring privileges to existing ones. A financial review of Sberbank by external consultants has been completed, and a strategic review with the participation of external consultants will be initiated in the near future. It is expected that this will be completed in the summer of 2001. As to VEB, the government has announced the intention to split its debt agency and banking functions. An action plan on how to do this will be formulated by mid-2001, and a strategic plan for the banking arm will be developed by end-September 2001. As to VTB, the terms of reference for a strategic review will be approved by the government jointly with the CBR by end-June 2001, with an interim report available by end-September 2001, and the review completed by end-November 2001. With the agreement of the CBR the government has resolved that it is expedient to establish January 1, 2003 as a preliminary target for the CBR divestiture of the VTB capital.

C. Nonpayments

47. Despite the achievement of financial stability the problem of nonpayments remains unresolved. The persistence of arrears and noncash payments has reflected the lack of progress in restructuring enterprises and banks and lingering fiscal problems, especially at the lower levels of government.

48. The government is determined to address this problem through a comprehensive strategy aimed at both tackling the underlying structural problems and enhancing financial discipline in the economy. The government will combine a tougher enforcement of timely cash payments of tax and utility bills with measures to restructure enterprises, promote

competition and improve corporate governance. Tight budget restrictions will be implemented, which will be an incentive for the improvement of cash collections. The government will seek to adopt a new Law on Insolvency (Bankruptcy) in 2001, removing the bias against liquidation and ensuring better protection of secured creditors to recover and liquidate collateral. The draft law will be prepared in accordance with the current international practice. One of the key elements of this strategy would be to restructure and better manage the natural monopolies. The government will formulate concrete plans for restructuring the electricity sector by end-June 2001.

49. The use of non-cash payments has been eliminated at the federal budget level and the government will ensure that there are no reversals in this area during 2001. The government intends to continue the practice of not permitting the use of tax offsets and, as in 2001, will ensure full financing of energy consumption by all federal budgetary entities in the draft budget for 2002. The government will provide for the solution of the problem of strategic energy users. It will take the required measures to ensure the full payment of consumed heat and electricity by non-budgetary organizations, while budget organizations will be financed appropriately. In the course of 2001, the government will seek passage of amendments to the Civil Code to remove any legal impediments to the disconnection of heat and electricity to nonpaying customers in the household sector.

50. Despite improvements, the problem of non-payments has not been fully resolved at the subnational government level. The problem is especially acute in specific regions of the Federation with one-enterprise towns. The government is considering complementing increased financial discipline with the provision of well-targeted budgetary subsidies to vulnerable regions.

51. The provision of full cash payments to RAO UES and Gazprom remains an important objective. The government will push, through its representation on the boards of these companies, for enforcing stricter financial discipline *vis-à-vis* energy consumers, including the following: strict implementation of disconnection of nonpaying customers, or, where this is not feasible, for a reduction in energy supply in line with payments received; full cash payment of all current payables by RAO UES and regional energy companies, including current tax liabilities and payments for all current shipments; the requirement on the part of Gazprom of payments from RAO UES as from any other commercial customer; and the sale of gas by Gazprom to all other distributors at a transparent price. Oil companies and all natural monopolies are now maintaining full cash compliance with statutory tax liabilities to both federal and subnational governments, and we will insist that they continue to do so. The government will seek to phase out the use of veksels and other forms of noncash payments in the energy sector during 2001. The government will insist on phased progress in improving cash collections, which shall equal by the end of 2001 (as assessed for the fourth quarter and excluding veksels) no less than 80 percent for Gazprom, 85 percent for RAO UES and 95 percent for Transneft and the Ministry of Railways.

52. The government has removed balance targets for the shipment of fuel oil to the domestic market and the related quantitative export restrictions on fuel oil. Balance targets

and associated export restrictions on liquefied gas will be abolished by end-June 2002. An action plan targeted at the balanced shipment of oil and oil products to the domestic market through economic measures, i.e. the preservation of relatively high export customs duties on oil and oil products, if needed, the timely and full disbursement of federal budget subsidies for the repayment of consumed fuel and energy at all levels of the budget system, and the creation of a reserve system, will be developed in the first half of 2001. The government will prepare a similar plan for liquefied gas. It will formulate a more detailed plan which addresses legal and budgetary concerns in this regard. The government will also take measures to improve the transparency of access to the export pipelines.

D. Governance and Transparency

53. We are committed to further strengthening governance and transparency in the conduct of economic policy. In this regard, we will be guided by the recommendations contained in the Report on the Observance of Standards and Codes (ROSC) in the areas of data dissemination, monetary and financial policies, and fiscal policy.

54. The CBR will continue the implementation of measures targeted at ensuring transparency of its operations. A plan has been agreed by the government and the CBR for the CBR to divest its foreign subsidiaries. The plan in the first stage is to transfer these subsidiaries to VTB by end-2001, in compliance with currently effective laws and requirements of supervisory authorities of respective countries, with two subsidiaries being transferred in the first half of 2001. In accordance with recommendations of foreign supervisory authorities, the CBR will maintain some equity stake in these subsidiaries. The CBR will prepare for publication its accounts for 1999 according to IAS, except for those on consolidation and hyperinflation. It will continue to compile such accounts. Further, the CBR will publish information as regards quarterly reviews of reserve management practices prepared with the assistance of its external auditor for 2000.

55. Our efforts to improve fiscal transparency will be directed at two broad areas. First, basic budget management processes will be developed further and the treasury system implemented within the framework of the Budget Code. Second, we will increase our focus on achieving general government fiscal targets and improving transparency at all levels of government.

Mikhail M. Kasyanov
Chairman of the Government
Russian Federation

Victor V. Gerashchenko
Chairman of the Central Bank
Russian Federation

Russian Federation: Fund Relations
(as of April 30, 2001)

I. Membership Status: Joined: 06/01/1992; Article VIII

II. General Resources Account:	SDR Million	Percent of Quota
Quota	5,945.40	100.0
Fund Holdings of Currency	14,490.33	243.7
Reserve Position in Fund	0.98	0.0

III. SDR Department:	SDR Million	Percent of Allocation
Holdings	2.57	N/A

IV. Outstanding Purchases and Loans:	**SDR Million**	**Percent of Quota**
Stand-By Arrangements	471.43	7.9
Extended Arrangements	4,929,47	82.9
Contingency and Compensatory	2,156.55	36.3
Systemic Transformation	988.42	16.6

V. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	07/28/1999	12/27/2000	3,300.00	471.43
EFF	03/26/1996	03/26/1999	13,206.57	5,779.71
Stand-By	04/11/1995	03/26/1996	4,313.10	4,313.10

VI. Projected Obligations to Fund: (SDR Million; based on existing use of resources and pres

	Overdue	Forthcoming				
	04/30/2001	2001	2002	2003	2004	2005
Principal		744.0	2,136.0	2,254.6	1,117.4	850.8
Charges/Interest		299.2	324.1	216.9	137.7	93.9
Total		**1,043.2**	**2,460,1**	**2,471.5**	**1,255.1**	**944.7**

VII. Exchange rate arrangement: Floating rate. The exchange rate of the ruble is determined in the interbank foreign exchange market, which was unified on June 29, 1999. The interbank market electronically links exchanges across the country. The official rate of the ruble is set equal to the previous day's weighted average rate in the interbank market.

The Russian Federation accepted the obligations of Article VIII, sections 2, 3, and 4 of the IMF Articles of Agreement with effect from June 1, 1996. The Russian authorities, however, presently impose a number of exchange measures that are subject to approval under Article VIII. Many of these were imposed in August 1998 in order to stem capital flight and stabilize the exchange rate. Russia's restrictions under Article VIII are as follows:

- **Suspension of conversion operations through nonresidents' S-accounts** (exchange restriction and multiple currency practice). These are special accounts used for GKO/OFZ-related transactions. Before balances arising from such transactions can be repatriated, funds have to be either transferred to a noninterest bearing transit account or invested in special short-term GKOs that are convertible at maturity. As a result, the repatriation of interest earnings and other current proceeds from GKO/OFZ investments would be made with possibly a long delay and at unfavorable terms. Fund approval granted on September 15, 2000.

- **Repatriation restrictions on ruble balances of nonresidents not participating in the GKO/OFZ novation** (exchange restriction and multiple currency practice). The rules governing the repatriation of ruble balances are similar to those described above with respect to the S-accounts. They apply to ruble balances arising from GKO/OFZ investments which matured before December 31, 1998. Fund approval granted on September 15, 2000.

- **Restrictions on nonresidents' T-accounts** (exchange restriction). These are nonresident bank accounts used for trade and some bond-related transactions. Existing restrictions limit the ability of nonresidents to effect moderate amounts of amortization from the proceeds of bond transactions. Fund approval granted on September 15, 2000.

- **Restrictions on advance import payments** (exchange restriction). The authorities do not freely permit the making of all advance payments that are required under valid import contracts. Fund approval not granted.

- **Restrictions on certain advance payments to Latvian residents** (exchange restriction). Fund approval not granted.

VIII. Article IV consultation: Russia is on the standard 12–month consultation cycle. The last consultation was concluded on September 15, 2000.

IX. Resident Representatives:

Mr. Poul Thomsen, Senior Resident Representative, since January 20, 2001.
Mr. Jonathan Anderson, Resident Representative, since August 24, 1998
Mr. Geoffrey Barnard, Resident Representative since July 17, 1999.
Mr. Timo Välilä, Resident Representative as of October 2, 2000.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

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July 18, 2001

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes Post-Program Monitoring Discussion on the Russian Federation

On May 29, 2001, the Executive Board of the International Monetary Fund (IMF) concluded a Post-Program Monitoring discussion on the Russian Federation based on information available through that date.[1]

Background

A 17-month Stand-By Arrangement with Russia expired on December 27, 2000. Russia's outstanding obligations to the Fund at end-April 2001 amounted to SDR 8.5 billion (US$10.8 billion), which amounts to 143.7 percent of Russia's quota.

Economic performance in 2000 was very strong. Output grew by 7½ percent, inflation was brought down to 20 percent, and official reserves increased sharply to 5½ months of import cover. Developments were dominated by the strength of the balance of payments. High international energy prices swelled an already large current account surplus to more than 18 percent of GDP, permitting a large build-up of official reserves despite continued high levels of private capital outflows. Sterilized intervention by the CBR, assisted by a large fiscal surplus and a strong recovery in the demand for money, moderated the ensuing pressure for a sharp real appreciation of the exchange rate. A relaxation of the stance of both monetary and fiscal policies in the second half of the year heightened inflationary pressures and contributed to a sharp increase in capital outflows, while the growth momentum slowed during the year as the real exchange rate appreciated.

Developments in early 2001 point to a slowdown in growth and some uptick in inflation. Even after regularizing payments to Paris Club creditors, the budget has run a strong surplus that has enabled monetary aggregates to be kept under control despite a further increase in official

[1] Post-Program Monitoring provides for more frequent consultations between the Fund and members whose arrangement has expired but that continue to have Fund credit outstanding, with a particular focus on policies that have a bearing on external viability. There is a presumption that members whose credit outstanding exceeds 100 percent of quota would engage in Post-Program Monitoring.

reserves. The economy has not, to date, been significantly affected by uncertainties in global financial markets with the spread on Russia's Eurobonds declining during the year and a strong increase in Russia's stock market index.

Structural reforms were conducted in the context of the comprehensive structural reform agenda adopted by the government in July 2000. Reforms in the fiscal area were the main achievements in 2000, with the adoption of important tax legislation (i.e., passage of four of the five main chapters of Part II of the Tax Code), and further strengthening of the Treasury. The nonpayments situation improved significantly in 2000, with the share of barter in industrial sales nearly halved to about 20 percent by end-2000, and cash collections at some key infrastructure monopolies doubling in the course of the year. While much of the improvement was related to the strengthened financial conditions in the economy, the reduction in barter and nonpayments also reflected supporting policy measures, including the continued absence of offset operations by the federal government and stricter financial discipline in the economy. On the other hand, reforms lagged in other key areas such as the banking system and restructuring of the power and gas sectors.

Executive Board Assessment

Executive Directors welcomed the completion of the first Post-Program Monitoring (PPM) discussion on Russia and agreed with the thrust of the staff appraisal. They observed that Russia's macroeconomic performance in 2000 had been impressive, driven by a combination of a favorable external environment—the large real depreciation of the ruble in 1998 and the recent sharp increase in international energy prices—as well as the generally prudent stance of fiscal and monetary policies. While welcoming important structural reforms, particularly the tax reform, they felt that the authorities had not taken sufficient advantage of the positive conditions to advance the structural reform agenda. Directors also noted that the recent slowdown of growth and an uptick in inflation pointed to the need to be vigilant and to adjust the policy stance as necessary to preserve recent macroeconomic gains.

Directors agreed that the authorities' macroeconomic program for 2001 appropriately aims at supporting growth, continuing the disinflation process, and building up external reserves. They also expressed their support for the government's broader structural reform program, noting that it addresses weaknesses in key macroeconomic areas—namely, fiscal and banking reform, the elimination of nonpayments/barter, and the promotion of good governance and transparency in public policy making. Directors noted that, while many of these measures had been part of Fund- and World Bank-supported programs in the past, their inclusion now in the government's own program, and its publication, signal stronger ownership and the likelihood of timely implementation.

Directors considered that the main challenge to short-run economic policy is to manage the strong balance of payments so that it does not weaken growth prospects or ignite inflationary pressures. They stressed that the authorities face the difficult task of creating appropriately tight domestic liquidity conditions to prevent an acceleration of inflation, while seeking to smooth the real appreciation of the ruble so as not to threaten economic growth. To achieve this, the Central Bank of Russia (CBR) would need to undertake large sterilization operations, and the authorities should ensure that the CBR has an adequate income position as well as a range of instruments for this purpose. In view of the rise in inflation and the need to generate domestic financial saving, many Directors were of the view that the CBR should tighten monetary policy. Some Directors, however, were concerned that raising interest rates could worsen the domestic liquidity management problem. In general, Directors cautioned that a greater contribution from fiscal policy will be needed to contain inflation and ease the burden on monetary policy. This would be all the more important if the balance of payments turns out to be stronger than anticipated. Directors also stressed the importance of better coordination between the CBR and the Finance Ministry in the area of debt management. They noted further that both accelerated trade liberalization and accelerated debt repayments would help Russia deal with the difficult policy trade-offs caused by the very strong current account and the accumulation of foreign exchange reserves.

Looking ahead, Directors welcomed the government's far-reaching structural reform program aimed at improving the business and investment climate. They urged the authorities to implement resolutely their program, as it would strengthen incentives for investment—both foreign and domestic—and reduce capital flight, thereby fostering growth and lowering vulnerability to external shocks. A few Directors commented on the probably negative impact of exchange restrictions on foreign investment in Russia and urged the authorities to review the capital control structure.

Directors stressed that improved governance and transparency would contribute to building public support for the government's reform program. In this regard, they strongly welcomed the government's commitment to further improving governance and transparency, including strengthening steps against money laundering and the publication of economic and financial policies for 2001 and the outline of the medium-term strategy. They also welcomed the authorities' intentions to publish the Report on the Observance of Standards and Codes modules on fiscal policies, monetary and financial policies, and data dissemination, as well as to provide reserve and foreign currency liquidity information to the Fund according to the Special Data Dissemination Standard template.

Directors commended the authorities on the significant improvements to the tax system introduced through the reform of Part II of the Tax Code initiated in 2000. However, they were concerned that revenue losses from the ongoing tax reforms could become too large, and emphasized the importance of maintaining Russia's hard-won fiscal sustainability in the face of the uncertain costs of the structural reform program and the revenue implications of possible future cyclical downturns. Directors welcomed the plans by the authorities to establish an oil stabilization fund and encouraged them to consider carefully its design and its connections to overall fiscal policy. They noted that such a fund could provide resources for structural reforms or debt servicing, while maintaining full financial transparency and accountability.

Directors commented that financial sector reform is essential for the expansion of private sector activity. They urged the authorities to build upon the strategy paper developed by the CBR and to design a forward-looking strategy that would increase the role of private banks—

including foreign banks—enhance competition, and move to international accounting standards. Directors urged the authorities not to be sidetracked in this process, but to set an appropriately ambitious timetable and to adhere to it. They welcomed the recent approval by the Duma of a package of measures to strengthen the legislative framework for dealing with bankrupt financial institutions. Directors emphasized that the success of the strategy would depend upon the authorities' ability to overcome strong-vested interests opposed to these reforms.

Directors welcomed the continuing decline in barter transactions and stressed that the authorities need to continue their efforts to strengthen payments discipline in the economy to ensure that the recent decline in barter/nonpayments is not reversed in the event of a cyclical downturn or worsening of the terms of trade. They stressed the importance of continued close monitoring of progress relative to cash collection targets and the implementation of new measures in case of slippages.

Directors considered it appropriate for the Fund to monitor the authorities' program in the context of PPM procedures. Noting that Russia will face large external debt payments in 2003, they urged the authorities to implement their program resolutely to ensure a continuation of the healthy recent macroeconomic performance, to minimize risks associated with volatile energy prices, and to establish a strong record of policy implementation. The latter will be particularly helpful in the event of any possible future need for Fund financial support.

A number of Directors encouraged the authorities to consider publishing the PPM staff report.

Russian Federation: Macroeconomic Indicators, 1998–2001

	1998	1999	2000	2001 Proj.
	(Annual percentage changes)			
Production and prices				
Real GDP	-4.9	3.5	7.7	4.0
Change in consumer prices				
Period average (on previous period)	27.7	85.7	20.8	17.6
Within period	84.5	36.6	20.1	14.0
Change in GDP deflator	12.4	65.1	40.0	17.8
	(In percent of GDP)			
Public sector				
Enlarged government balance	-8.0	-3.3	3.0	1.0
Federal government				
Overall balance (commitment basis)	-5.9	-4.4	1.0	0.8
Primary balance (commitment basis)	-1.3	1.8	5.3	3.9
Revenue	11.0	13.2	16.2	15.6
Expenditure (commitment basis)	16.9	17.6	15.2	14.9
Interest	4.5	6.2	4.3	3.1
Noninterest	12.3	11.4	10.9	11.7
	(In billions of U.S. dollars unless otherwise indicated)			
External sector				
Total exports, fob	74.9	75.8	105.2	105.0
Total imports, fob	58.0	39.6	44.2	52.4
External current account (deficit -)	-1.6	22.9	45.3	35.6
Gross reserves coverage (months of imports of GNFS)	1.8	2.8	5.5	6.0
Memorandum items:				
Nominal GDP (billions of rubles)	2,696	4,607	6,947	8,500
Exchange rate (rubles per U.S. dollar, period average)	9.7	24.6	28.1	...

Sources: Russian authorities; and IMF staff estimates and projections.