

Main Problems of Russian Macroeconomic Policy

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Introduction

The specific measures taken in the course of Russian economic reform are as follows:

1. Since the beginning of January 1992 the prices and the terms of commerce have been liberalized. As a result of this step January saw an increase of prices by 250%, February by 38%, March by 24% and April and May by 15% a month. This stock-type price jump has brought about a radical drop in the volume of purchases in the retail trade. In January 1992 the volume made up 37% as compared with the figure in January of last year, in February-59% and in March approximately the same figure. In April, May the volume of buying was boosted but not too significantly. At the same time the amount of production decreased only by 15 per cent.

2. New regulations of the foreign economic activity were put into effect on 1 January. Duty on exports has been set in the range from 20 per cent to 40 per cent of the world price on average. The export duties are paid in rubles. 40% of the currency earnings the exporters have to sell at the rate twice lower than that of the market, 10% at the market rate and the rest they can have at their disposal to effect or to sell at an exchange market.

The import of goods is not subject to customs duties, taxes and is free of VAT.

3. The budget and fiscal areas are the ones where one can see the most radical changes.

On January 1, 1992, a new tax system was introduced. The key element in the tax reform is the replacement of the turnover tax (levied primarily in the form of price differences in various amounts depending on the kind of product) with a uniform 28% rate.

At the same time the price-difference subsidies (the major part of which belonged to the agricultural sector) were eliminated. The introduction of this kind of tax is designed to

create a stable income basis of the Republican budget.

The profit tax rate is 32%. However, there are substantial preferences relating to the profit tax. That is why the real rate of exaction is 22-23%. The introduction of two base taxes (the VAT and profit tax) with one standard and with minimum level of preferences and exceptions makes a rather stable income base of budgets for all levels.

4. Initially the budget deficit was thought to be in the amount of 1% of the GNP. However, in the course of the budget executing the budget expenditures have been rectified which caused an increase of the approved budget up to 4.5% with reference to the GNP.

In real terms the execution of the budget promised a lower deficit. Thus the Republican budget was executed with about 0.3% deficit from the GNP, the revenues of the local budget exceeded the expenses by 1.7% of the GNP. Moreover, one should remember that the increase of the balance on the Pension fund accounts amounted to over 3% of the GNP.

Part of the Republican budget expenditures planned for the first quarter in real terms were finally financed only in April due to the credit obtained from the CBR. If we take into account the expenditures, then the consolidated budget deficit made up some 1.4% of the GNP, and if one takes into account the balance gains the accounts of the Pension fund-about 1.7% of the GNP (of the excess of the incomes over the expenses).

5. Further steps to improve the tax system will be reforms mainly directed to improve the tax collection system.

On July 1, 1992, a single ruble rate was introduced for all current and capital transactions. This will cause a drastic change in the budget. The imports due to the credits would require considerable subsidies for internal prices. This is connected with the fact that

due to centralized imports one can buy primarily the grain and food. Once the market rates are effected without any subsidies, you can have a price rise for bread 4-6 times, while the price on food may go up 2-3 times. The reduction of import subsidies will occur as the domestic prices in similar goods grow and in the course of the increase of the ruble rate.

As long as the domestic prices on goods go up, the export rate will go down and the energy tax will increase.

Under the conditions of free prices one can speak about a macroeconomic balance in the economy of Russia. With all that you can not call the situation stable. The trend is for a further growth of prices though it is primarily of a corrective nature. In the national economy the portion of non-payments already comprises some 20% of the GNP. The way to solve the problem is through a comprehensive approach: the settlements system should be improved, the credits should be increased, though this may take place under the conditions of high rates, there may be bankrupt enterprises, the pledge system should be developed and other steps should be taken now that the financial responsibilities of enterprises are becoming more and more pronounced.

I. Main Consequences of Economic Reform in Russia

The main step taken from the start of 1992 was a liberalization of prices. Table 1 shows a price dynamics for the first five months. The first index reflects an aggregate price measured on the basis of the selection of the main type of products. The third index shows a drop in the real production volume, while the fourth index is used to reflect the dynamics of the real volume of the turnover.

Table 1. Price Index in 1992(month to month)

Month	Price index	Consumer price index	Real production*	Real retail turnover
January	3.58	3.45	0.85	0.37*
February	1.39	1.38	0.88	1.21
March	1.23	1.30	0.88	1.08
April	1.15	1.22	0.88	0.95
May	1.16	1.13	0.85	0.94

* in comparison to previous period last year.

As one can see from the table, the primary price boost is for January-February, while in March-May the rates of price rise were gradually going down. Simultaneously under the circumstances one can speak about a drastic decrease in the volume of production, while most noticeable was the drop in the purchasing power of the population.

In the first months of price increases the main tool used to fight inflation was harsh restraint on financing for all kinds of budget expenditures. At the same time one could see a tough limitation on the granting of credits to enterprises. However, the drop in demand for more than half could lead to the same drop in production and in the standard of living of the population. Now, keeping in mind that the price rise was slowing in March-April, the credit-money policy was made more liberal and more financing was provided to cover the budget deficit. In May the price of energy resources went up 5-fold, as compared with the previous fixed-level set on January 1, 1992. In spite of all this the boost of consumer prices was the same as in April.

As to the rise of wages it substantially fell from the price rise in January. As a result, the real wages in January comprised 51% from the average level of 1991. In February-April the wage rise was far ahead of the price which caused an increase of its real level. The table 2 shows the boost of wages.

II. Major Changes in the Tax System

The major change in the tax system was associated with the introduction of the VAT.

The structure of the wholesale prices was always different from the structure of retail prices in the Soviet economy. This difference (if it happened to be positive) was deducted from the budget in the form of the turnover

Table 2. Wage Growth (ruble per month)

Month	Nominal		Real	
	in economy	in industry	in economy	in industry
January	1470	1801	0.51	0.63
February	1994	2400	0.56	0.67
March	2705	3464	0.63	0.80
April	3024	3769	0.58	0.71
May	3300	—	0.56	—

Table 3. VAT Collection

Month	VAT (bln. rbl.)	GNP (bln. rbl.)	VAT in % to GNP
January 1st half	1.4	} 372	} 2.9
2nd half	9.5		
February 1st half	14.2	} 513	} 6.4
2nd half	18.5		
March 1st half	19.8	} 668	} 8.2
2nd half	34.8		
April 1st half	28.1	} 777	} 8.1
2nd half	34.9		
May 1st half	22.0	} 969	} 5.4
2nd half	30.4		
June 1st half	30.5	} 1163	} 6.7
2nd half	47.0		
July 1st half	51.2		

Table 4. Profit Tax Collection

Month	in bln. rbl.	in % to GNP
January	18	4.8
February	32	6.3
March	46	6.8
April	116	14.9
May	98	10.1
June	71	6.1

tax, or it came from the budget (if it was negative). Actually, one can speak of thousands of kinds of tax rates and subsidies differentiated with reference to certain types of products and certain types of producers. With a switch over to free prices and the establishment of uniform rates in the form of VAT the wholesale and retail prices are set at proportionately the same level. For manufacturers consumer demand dynamics have become transparent.

In table 3 you can see the dynamics of tax collection on the added value. In January-February the amount of tax collected was rather low. One can speak about a considerable VAT only in the second half of March. In the April-May period VAT earnings stabilized, though that stabilization was at a rather low level. The entire gain in volume of the VAT is frozen through insolvency.

The highest rates of growth are represented by profits tax earnings. Table 4 shows the dynamics of this type of tax. In the 1st quarter the profits taxes are realized in the form of advances with a 3.5 coefficient. However, in reality the profits went up 6-7 fold. As a

result, if you do a recalculation for the first quarter (in April-May), the profits tax receipts would be approximately the same as the amount collected in the first quarter.

Very high rates are also characteristic of the excise earnings and of income tax earnings that come from the population. The gains that are obtained from these taxes are associated with the price growth and the boost of wages and other incomes of the population.

The most unlucky is the collection of export duties and export payments into the non-budget funds (except for the Pension Fund and Social Insurance Fund). Non-payment of export duties is due to two reasons: firstly, a low ruble rate (exporters lacked rubles and were granted a delay) and, secondly, many exporters were granted preferences in regard to paying the export duties. The lack of returns to the non-budget funds is associated with non-payments and because of the lack of responsibility for such non-payment analogous to the responsibility for non-payment of taxes.

III. The Results of the Execution of the Budget for 6 Months

The revenues and expenditures of the consolidated budget for a 6 month period are given in Table 5. Consolidated budget receipts for a 6 month period amounted to 1107.4 billion rubles out of which 1305.6 billion rubles were spent.

The situation with the Republican budget is as follows. Expenditure exceeded the receipts by 280.4 billion rubles, and in the case of local budgets the figure is +82.2 billion rubles. However, as to the Pension Fund receipts exceeded expenditures by more than 50 billion rubles.

The results of the budget execution for 6 months show that primarily what we have now is the principle of the non-inflationary budget. The Republican budget deficit does not exceed the gains on the accounts of the local budgets and non-budget funds. One can speak about the same prospect of budget execution for the entire year of 1992.

IV. Further Trends in Economic Reform

In Russia's economic reform the main trend, will be the introduction of a uniform

Table 5. Revenues and Expenditures of the Budget for 6 Months (bln. rbl.)

	Total	Including :	
		Republican	Local
REVENUES			
1. VAT	288.2	221.6	66.6
2. Profit tax	387.3	176.9	210.3
3. Income tax	93.5	—	93.5
4. Excise tax	44.1	19.4	24.8
5. Other	227.2	148.4	78.8
Total	1040.3	566.3	474.0
Grants to local budgets	67.1	—	67.1
TOTAL	1107.4	566.3	541.1
EXPENDITURES			
1. Expenditures to economy	386.9	215.7	171.2
2. Social, science and cultural expenditures	313.5	96.9	216.6
3. Military	215.2	215.2	—
4. Internal debt service	12.6	12.6	—
5. Other	310.3	239.2	71.1
Total	1238.5	779.6	458.9
Grants to local budgets	67.1	67.1	—
TOTAL	1305.6	846.7	458.3
Deficit (-)	-198.2	-280.4	
Surplus (+)			+82.2

rate and the introduction of the ruble convertibility. The 1992 budget is prepared with a uniform ruble rate for the second half of 1992. All the obligatory exchange sales will be for the CBR or for the authorized banks. The Government will buy currency from the CBR to make the necessary payments within the existing ruble revenues. The main direction of the policy of the Government and the CBR will be that of stabilizing the ruble rate and not the consumption of the currency in amount as large as possible.

As to the tax sphere, the main trend there will be a better collection of taxes. Import tariffs will be introduced. As to the profits tax, there will be relief for investments which are made by an enterprise for the expansion of its own production.

In addition there will be a reduction of the ultimate rate of the income tax from citizens.

V. Problem of Non-payments and the System of Bank Transactions

After the period of price liberalization and

Table 6. Amount of Non-payments

	Non-payments (by the end of month in bln. rbl.)	Gain per month (in bln. rbl.)
January	140	106
February	606	466
March	777	171
April	1855	1078
May	2056	201
June	2400	344

the initial jump of prices in January-February, the primary way that losses will be covered is the non-payments of enterprises.

The dynamics of growth of non-payments is shown in the Table 6.

The non-payments in the economy can be accounted for by two primary reasons.

It has been expected that the level of wholesale prices will be higher than that of retail prices so enterprises faced a restriction in final demand.

In the atmosphere of fixed prices the difference between the wholesale and retail prices was covered by a form of budgetary subsidies (primarily with reference to such primary products as raw materials, energy resource products).

Once the subsidies were removed, the wholesale price level turned out to be higher than the retail prices. The losses of manufacturers did not cover the credits that could be obtained under very tight terms and for high interest rates, however, they continued to ship their products without being paid.

An absolute system of bank transactions was a contributing factor in this case. The manufactured items were dispatched to clients without checking the availability of assets on their accounts. Documents for payments were sent to the payer's bank and were accumulated there because of the lack of assets in the account.

In addition the bank transaction system is absolute and does not provide for rapid transactions. It takes 2-3 weeks for assets to reach a receiver. That was a second reason for non-payments.

As a result, the mutual indebtedness of enterprises reached some 17-18% of the annual GNP.

Under the circumstances, the Government and the Central Bank have taken the follow-

ing decision :

—to offset the mutual indebtedness of enterprises. All debts of enterprises that are left and all debts that are due the enterprises are referred to the Agency for Management of Debts of State-owned Enterprises. Within 1.5 years the Agency will sell the debts of the enterprises and the sales' proceeds will be distributed between the enterprises having a favorable balance because of the offset proportional to the amount of the positive balance.

Simultaneously the transaction system is eliminated when goods are shipped without the seller checking whether the payer has the assets in his account.

VI. Ruble Zone and Ruble Stabilization

Actually, an economic reform in Russia was launched in conditions when there was no common issuing center. Fifteen Central Banks of the fifteen Republics were issuing money on an independent basis.

Without any independent payments on a clearing basis payments were made from one republic to another. The only check was the introduction of correspondent accounts in Russia to conduct transactions with republics.

During the first two months Russia's favorable balance in the settlements with other republics was rather small. That situation continued until May. In May the settlement balance (excess of payments in Russia over the payments out of Russia) amounted to about 100 bln. rubles which approximates the deficit of the republican budget. But in June the sum doubled.

Because the developments took this course, the Central Bank of Russia made a decision to stop direct transactions between the republics.

Now, to effect their transactions the Russia's commercial banks, as well as enterprises, are now free to open accounts in the banks of other republics. On another hand, banks and enterprises of other republics are welcome to open ruble accounts in Russia.

In essence, this decision means that a monetary reform has occurred in Russia. Direct settlements on a clearing basis are made only inside Russia. To obtain money from other republics it is necessary to sell the currency of the other republics for rubles. And following this way we can establish an exchange rate for all republican currencies.

Thus the movement of money would be possible only in the form of cash until the official custom borders are established. And it should be stressed that large banknotes are issued only in Russia and within a 1-2 years period all the banknotes may be replaced by Russian banknotes.

The survey shows that in the second half of 1992 Russia is going to pass over to a much tighter version of economic stabilization.

A single ruble exchange rate will be introduced and the newly adopted system of bank transactions will do away with the principle of the automatic payment for products, and the ruble zone will be closed for other republics. These fundamental provisions should bring about much tighter restraints for enterprises.

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