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February 1, 2021

Statement by Ms. Mannathoko and Mr. Jappah on Russian Federation (Preliminary)
Executive Board Meeting
February 3, 2021

We thank staff for the well written report and Mr. Mozhin for his informative Buff Statement. Russia continues to tackle the health and economic effects imposed by the COVID-19 shock, which comes against the backdrop of anemic growth performance realized in recent years. We commend the authorities for the decisive and coordinated fiscal and monetary policy response which moderated the impact of the pandemic on firms and households. Looking ahead, the effectiveness of the vaccine rollout in overcoming the delay caused by the second wave, alongside improved consumer and business confidence will be important in paving the way to a recovery in 2021. The outlook is also susceptible to significant risks stemming from geo-political tensions and an overheated mortgage market. We broadly concur with staffs' appraisal and offer the following comments.

Fiscal policy: While we commend the authorities for the strong countercyclical fiscal policy response to the crisis, we see scope to further support vulnerable populations through increased means-tested social spending and unemployment benefits. While noting the authorities' intention to phase out the stimulus and return to the fiscal rule, as stated in Mr. Mozhin's Buff statement, we consider that low public debt and sizeable buffers, including the sovereign wealth fund (National Welfare Fund) and international reserves afford fiscal space that can be used to relieve declines in welfare and associated social tension. We welcome measures taken to counter the increase in poverty in the wake of the pandemic; but given the rise in unemployment and its poverty effects, we encourage the authorities to stand ready to intervene if poverty levels are elevated by further income shocks. We note World Bank reporting that the goal of halving the 2018 baseline poverty rate has now been deferred six years to 2030; however, given ongoing impacts on various populations, we would encourage doing more sooner rather than later. With this in mind, among other things, we support staff's call to retain unemployment benefits at post-March 2020 levels until a meaningful employment recovery takes hold. We also note that the World Bank (Russia Economic Report, December 2020) reports that while the federal budget increased its transfers to regions in response to the crisis, some regions were unable to augment this as they face borrowing restrictions under state debt restructuring regulations. *Could staff* *elaborate on measures used by these regions to cope, relative to those that don't have borrowing restrictions?*

Monetary policy: We consider a sustained accommodative monetary policy stance appropriate within the context of weak aggregate demand. While we understand the authorities' emphasis on a data driven policy stance, we concur with staff that inflation may well subside as the pass-through from exchange rate depreciation abates and encourage the authorities to monitor inflationary drivers and expectations closely before deciding to reverse the accommodative stance. We also encourage the authorities' intention to only use foreign exchange operations in exceptional circumstances. This is appropriate to allow the exchange rate flexibility needed in response to current shocks. *Could staff elaborate on authorities' views regarding staffs' inflation forecast on page 14?*

Financial sector policies: Though capital remains largely adequate across the banking sector, we agree that balance sheet stress may be currently masked and could become more evident once regulatory forbearance especially on impairment recognition, is rolled back. High NPLs may be exacerbated beyond current expectations once support to firms is rolled back. Given the potential for masked weaknesses, we encourage the continued delay of dividend payments to allow banks to strengthen their balance sheets. We also urge the authorities to monitor the volume and treatment of restructured loans closely.

Structural reforms: We welcome progress in implementing structural reforms, including the approval of two bills aimed to improve the business climate, the ongoing review of all existing rules and regulations for business, the new Investment Protection and Encouragement Law, and the 2020/21 Economic Recovery Plan which aims to promote exports and expedite customs procedures through digitalization. At the same time, we encourage the authorities to foster competition by instituting reforms to engender a level playing field for new entrants by removing restrictive barriers. In addition, timely reform of SOEs would help limit their heavy fiscal burden on the national treasury. We commend the authorities for establishing policies and laws to address AML/CFT deficiencies identified in the 2019 mutual evaluation report. This notwithstanding, we encourage the timely implementation of recommendations of the Interagency Action Plan on the AML/CFT framework.