RUSSIAN FEDERATION: Country Assistance Strategy

I am fortunate to be among those EDs who had the unique opportunity of a trip to Russia and witness firsthand the tremendous process of transition with its achievements as well as challenges. On the basis of what we have seen, I can share the CAS document conclusions that the transition process has been "chaotic and wrenching", that a lot has still to be done on many fronts, and that the Bank Group active role should continue as long as the window of opportunity for accelerated structural reform that the document cites indeed remains open. I have the following comments:

1. Despite the progress achieved so far, performance is fragile, prospects remain difficult and many uncertainties lie ahead. Substantial achievements have been made in controlling inflation, expanding the private sector, improving the external balance and arresting the decline in output. Nevertheless, even if the expected 6 percent output growth materializes for the coming years, it will be only in the year 2005 that the 1991 output level will be reached (Annex 9). Yet output growth is the main hope for reducing poverty where the level is still very high at 25-35 percent of the population. This is coupled with political uncertainties, fragile economic performance and still weak institutional capacity. All this underscore the magnitude of the tasks that have to be tackled. The document is full of the actions to be taken by the authorities on numerous fronts and implementation is far from easy.

2. The area where insufficient progress has been achieved and where much needs to be done is private sector development. The CAS document and Annex 4 point out that the business environment in Russia is less supportive for the entry and expansion of private business than in most eastern and central European countries, and that foreign direct investment is also well below eastern European countries such as Poland and Hungary. What is particularly noteworthy in this respect is Russia’s inability to attract new foreign investment in oil production which is attributed by the document to ‘serious deficiencies in the policy framework for foreign investment”. Some measures have been taken in the past year to address this issue but, as noted in para 28 and elsewhere, a lot needs to be done on the policy front to attract foreign investment. The suggested Bank Group approach in top of page 24 is appropriate, although one would expect that emphasis will be placed on
improving policies to attract foreign investment rather than on further resort to Bank project financing.

3. One factor that has been acknowledged to have affected the business environment is crime and corruption. Unfortunately the documentation barely mentions this factor, with no analysis of the magnitude of the impact and ways of dealing with it. This is in contrast to the increasing attention that the Bank is giving to the issue of corruption, including in a section in the Strategic Compact and a paper on the subject coming for the Board in few weeks. This is also in contrast to the wide acknowledgment of the importance of this issue inside Russia to the extent that led President Yeltsin last April to pledge a “fight to the end” against graft and corruption. During our recent EDs group travel to Russia we had a frank and open discussion of the issue with officials and parliamentarians where we heard various views and analysis, including the hope that relationships with World Bank will not be strained because of corruption, especially when the Bank sends a consultant with a $25,000 monthly salary!

4. Finally, on the proposed Bank strategy, I note that going for the high case of $2-3 billion is based on the assumption that the government delivers on an accelerated program of structural reforms and that, as indicated in para. 54, the government would need to support reforms in all of the major areas identified as essential to a resumption of sustained economic growth. It is also well recognized that this is a high risk case and that close monitoring is required throughout. The triggers suggested seem to be quite elaborate and one would look forward to see how they will be actually implemented. On some specifics, I would underscore Bank regional operations, especially in disadvantaged and national minority areas. I also commend the close involvement of the EDI and wonder how far is this being done in other borrowing countries.