

RUSSIAN FEDERATION

Real GDP growth in 2007 is likely to remain close to the levels of 2005-06, before moderating in 2008 as the impulse from recent terms-of-trade improvements dissipates. Growth will still be primarily consumption-driven, but the contribution of fixed investment to growth should increase. Inflation is likely to fall further, owing mainly to shrinking external surpluses, further de-dollarisation and slower growth of utilities tariffs and other regulated prices.

The easing envisaged by the revised medium-term fiscal plan will limit the speed of disinflation. It will also make it harder for the authorities to hold down the rate of real effective exchange-rate appreciation. Nevertheless, this short-term relaxation of fiscal policy has accompanied steps to create a better rules-based fiscal framework. In the medium-to-long term, the key will be the effective implementation of plans to improve the management of oil windfalls and reduce the non-oil budget deficit.

The economy continues to grow strongly

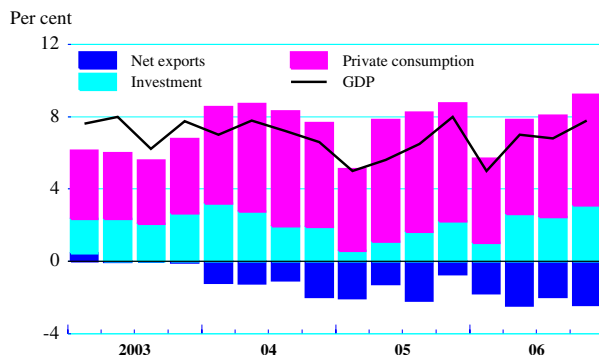
GDP growth reached 6.7% in 2006, slightly higher than in 2005. Fixed investment rebounded strongly, compensating for a moderate slowdown in the still-robust growth of household consumption and the increased negative contribution of net exports. On the production side, market services accounted for somewhat over half of the increase in real GDP. Resource-extraction sectors grew modestly, recovering from the sharp slowdown of 2005, but non-resource tradables continue to struggle with the pressures generated by rouble appreciation. Manufacturing growth slowed for the third year running, falling to 4.9%. Investment gains were concentrated in resource extraction, services, the public sector and agriculture, which benefited from an influx of federal support under the "Priority National Project" for the sector. Fixed investment in manufacturing grew relatively slowly. This may reflect forward-looking assessments of the profitability of domestic manufacturing in Russia.

Inflation has fallen further

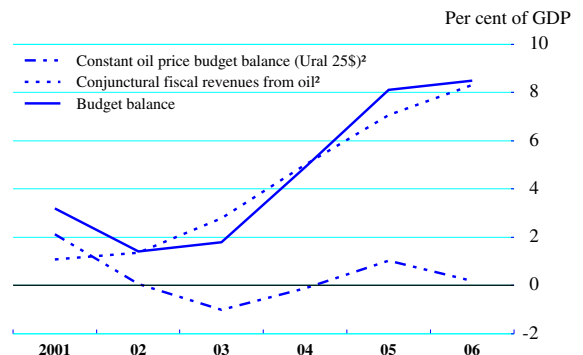
Despite money-supply growth far in excess of central bank guidelines, headline inflation has continued its gradual decline and is

Russian Federation

Growth remains strong¹



Fiscal slippage has been minimal



1. Year-on-year percentage change.

2. The constant-oil-price budget balance and oil windfalls are estimated on the basis of the average dollar price of Urals crude in 1992-2006 (\$ 25/bbl).


Source: Economic Expert Group and Russian Federal Service for State Statistics.

Russian Federation: Macroeconomic indicators

	2005	2006	2007	2008
Real GDP growth	6.4	6.7	6.5	5.8
Inflation	10.9	9.0	7.5	6.5
Fiscal balance (per cent of GDP) ¹	8.1	8.5	4.0	2.0
Current account balance (per cent of GDP)	10.9	9.8	6.2	3.8

1. Consolidated budget.

Source: Data for 2005-06 are from national sources. Data for 2007-08 are OECD estimates and projections.

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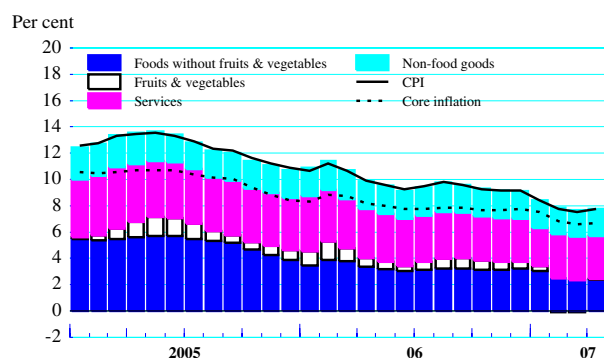
now firmly in single digits. This outcome owes much to continuing de-dollarisation, lower regulated price hikes and moderate food-price increases over the winter. The central bank's decision to allow a small appreciation of the nominal exchange rate in early 2006 also played a role, but the bank has since stuck to its policy of trying to hold the nominal effective exchange rate roughly constant. Declining inflation therefore brought with it a slowdown in the rate of real rouble appreciation and reduced the pressure on the bank to alter its stance. Disinflation was also facilitated by the fact that budgetary spending was significantly below the level set in the revised budget for 2006. Thus, the non-oil budget balance deteriorated by only about 1% of GDP.

Medium-term fiscal rules are being strengthened

The most important policy developments of recent months concern the framework for fiscal policy. Russia has this year begun the transition to budgeting within a medium-term (three-year) framework, in an effort to reduce uncertainty about future policy and raise the efficiency of budget execution. The government is also proceeding with the development of a promising new framework for governing the Stabilisation Fund. The Fund is to be split in two. A fiscal "reserve", probably totalling around 10% of GDP, is to be maintained in order to insure the budget against an oil-price drop, while the balance of surplus

Russian Federation

Inflation is now firmly in single digits¹

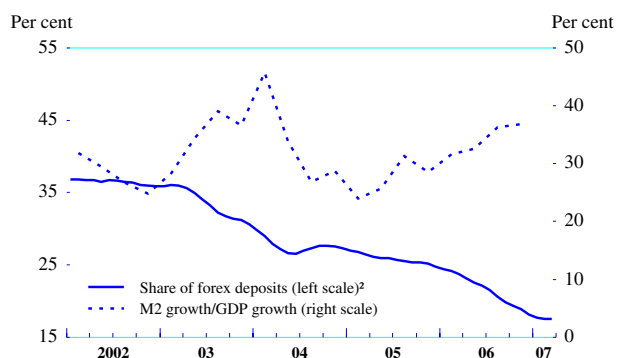



1. Year-on-year percentage change.

2. Share of foreign deposits in total deposits (6-m MA).

Source: Central Bank of Russia, Economic Expert Group and OECD calculations.

Rouble M2 growth partly reflects de-dollarisation




StatLink  <http://dx.doi.org/10.1787/032644201707>

Russian Federation: External indicators

	2004	2005	2006	2007	2008
	\$ billion				
Goods and services exports	204	268	332	364	394
Goods and services imports	131	165	209	260	305
Foreign balance	72	104	124	104	88
Invisibles, net	-14	-20	-28	-35	-42
Current account balance	59	83	96	69	46
	Percentage changes				
Goods and services export volumes	11.8	6.4	7.0	5.8	6.3
Goods and services import volumes	22.0	17.0	20.3	18.5	15.2
Terms of trade	16.0	15.4	10.2	-1.5	-0.1

Source: National sources and OECD projections.

StatLink  <http://dx.doi.org/10.1787/035570230510>

hydrocarbon revenues are to be invested in an income-generating “Fund for Future Generations”. Russia will continue to finance a good deal of current expenditure from oil revenues, but the transfer of oil and gas revenues to the budget is to peak at 6.1% of GDP before falling to a long-run level below 4% by 2011. The current plan represents an important attempt to create an institutional basis for sustaining fiscal discipline and the prudent management of oil windfalls over the long run. However, the new proposals have coincided with a revision of the three-year budget plan to allow for substantially faster spending growth than previously envisaged, particularly this year.

Structural reform has been modest

The last half-year has seen little movement on major structural policy issues. The authorities are not expected to press ahead with major reforms before the parliamentary and presidential elections of December 2007 and March 2008; moreover, there are few indications to suggest that the post-election period will see a major reinvigoration of structural reform efforts. Perhaps the most significant recent development was the adoption of the long-awaited Part IV of the Civil Code, which aims to bring Russia’s intellectual property legislation into line with international norms and thus to facilitate accession to the World Trade Organisation (WTO). Some recent tax changes will have a positive effect on the business climate, and March 1 marked the beginning of a ten-month income-tax amnesty. However, the amnesty will probably have only a limited effect, and the major problem for entrepreneurs is in any case tax administration. The rules governing tax inspections have recently been revised, but the new rules leave the tax authorities with much the same arbitrary power as before.

Growth is projected to moderate slightly in 2007 and slow further in 2008

Very high year-on-year industrial output growth in January-February was largely the product of a base effect: activity in many sectors was depressed in early 2006 as a result of exceptionally cold weather and power-supply problems. Assuming that oil prices do not move much from their current levels, the terms of trade are likely to stabilise this year, but

the absence of any further impulse from commodity prices will be partly offset by an increase in public spending. The growth of household incomes and consumption is therefore likely to decelerate only slightly. The degree of fiscal easing in 2007-08 will, however, be much smaller than the reduction in the consolidated surplus, which will result mainly from lower oil windfalls. Investment growth is likely to remain strong, particularly in services and resource extraction. Real GDP growth is therefore expected to be close to last year's level, although it is likely to slow further in 2008, as the momentum generated by the terms-of-trade shifts of 2003-06 should be largely dissipated by then and the medium-term fiscal plan envisages a less expansionary stance next year. Smaller current-account surpluses and lower increases in regulated prices should make disinflation somewhat easier, although the former will be partly offset by rising net capital inflows.

**Electoral politics constitute
the major source of
uncertainty**

Apart from oil-price movements, the electoral cycle of 2007-08 is the major source of uncertainty. Whatever the outcome of the elections, the contest could lead to actions by various political groupings that would damage the investment environment and undermine confidence. On the upside, WTO accession could provide a boost to both domestic and foreign investor confidence, as would the speedy implementation of a credible medium-term fiscal framework along the lines described above.

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This book has...



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Conventional signs

\$	US dollar	.	Decimal point
¥	Japanese yen	I, II	Calendar half-years
£	Pound sterling	Q1, Q4	Calendar quarters
€	Euro	Billion	Thousand million
mb/d	Million barrels per day	Trillion	Thousand billion
..	Data not available	s.a.a.r.	Seasonally adjusted at annual rates
0	Nil or negligible	n.s.a.	Not seasonally adjusted
–	Irrelevant		

Summary of projections

	2006	2007	2008	2007			2008				Fourth quarter		
				Q2	Q3	Q4	Q1	Q2	Q3	Q4	2006	2007	2008
	Per cent												
Real GDP growth													
United States	3.3	2.1	2.5	2.5	2.3	2.5	2.5	2.6	2.7	2.7	3.1	2.1	2.6
Japan	2.2	2.4	2.1	1.8	1.9	2.0	2.1	2.2	2.1	2.2	2.5	2.0	2.2
Euro area	2.8	2.7	2.3	2.6	2.5	2.4	2.3	2.2	2.1	2.1	3.3	2.5	2.2
Total OECD	3.2	2.7	2.7	2.7	2.6	2.7	2.7	2.7	2.7	2.7	3.2	2.6	2.7
Inflation													
United States	2.9	2.6	2.2	2.3	2.0	2.2	2.4	2.2	2.1	2.1	2.5	2.6	2.2
Japan	-0.9	-0.4	0.2	-0.4	0.0	0.1	0.2	0.3	0.4	0.6	-0.5	-0.3	0.4
Euro area	1.7	2.0	2.0	1.0	2.0	2.0	2.0	2.1	2.2	2.2	1.6	2.0	2.1
Total OECD	2.2	2.1	2.0	1.9	2.0	2.0	2.0	2.0	2.0	2.0	1.8	2.3	2.0
Unemployment rate													
United States	4.6	4.6	4.8	4.5	4.6	4.7	4.8	4.8	4.8	4.9	4.5	4.7	4.9
Japan	4.1	3.8	3.6	3.8	3.7	3.7	3.6	3.6	3.6	3.6	4.1	3.7	3.6
Euro area	7.8	7.1	6.7	7.1	7.0	6.9	6.9	6.8	6.7	6.6	7.5	6.9	6.6
Total OECD	5.9	5.6	5.5	5.6	5.6	5.6	5.5	5.5	5.5	5.4	5.7	5.6	5.4
World trade growth	9.6	7.5	8.3	7.7	8.2	8.4	8.3	8.3	8.2	8.2	8.6	7.7	8.3
Current account balance													
United States	-6.5	-6.1	-6.2										
Japan	3.9	4.8	5.4										
Euro area	0.1	0.4	0.4										
Total OECD	-1.9	-1.5	-1.5										
Cyclically-adjusted fiscal balance													
United States	-2.5	-2.8	-2.8										
Japan	-2.2	-2.7	-3.2										
Euro area	-1.0	-0.8	-0.7										
Total OECD	-1.7	-1.8	-1.9										
Short-term interest rate													
United States	5.2	5.3	5.0	5.3	5.3	5.2	5.1	5.1	5.0	4.9	5.3	5.2	4.9
Japan	0.2	0.5	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.7	0.4	0.6	0.7
Euro area	3.1	4.1	4.3	4.0	4.2	4.3	4.3	4.3	4.3	4.3	3.6	4.3	4.3

Note: Real GDP growth, inflation (measured by the increase in the GDP deflator) and world trade growth (the arithmetic average of world merchandise import and export volumes) are seasonally and working-day-adjusted annual rates. The "fourth quarter" columns are expressed in year-on-year growth rates where appropriate and in levels otherwise. The unemployment rate is in per cent of the labour force while the current account balance is in per cent of GDP. The cyclically-adjusted fiscal balance is in per cent of potential GDP. Interest rates are for the United States: 3-month eurodollar deposit; Japan: 3-month certificate of deposits; euro area: 3-month interbank rate.

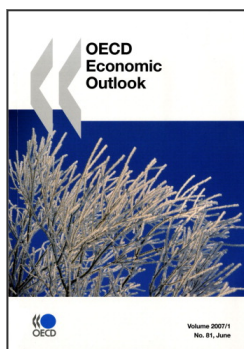
Assumptions underlying the projections include:

- no change in actual and announced fiscal policies;

- unchanged exchange rates as from 9 May 2007; in particular 1\$ = 119.72 yen and 0.74 euros;

The cut-off date for other information used in the compilation of the projections is 15 May 2007.

Source: OECD Economic Outlook 81 database.



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