

Strategic Objective Close-Out Report

USAID/Russia

Name: "Improved Economic Infrastructure to Support Market-Oriented Growth"
Number: SO 118-140
SO Approval Date: 1999
SO Completed: FY 1999 – FY 2002
Geographic Area: Russian Federation
Total Cost: Freedom Support Act - \$23,618,000

1. Principal Implementing Partners:

Center for Fiscal Policy
Institution for the Economy in Transition
Financial Services Volunteer Corps
Georgia State University
Moscow Public Science Foundation
Deloitte & Touche
Carana Corporation
American Chamber of Commerce
Development Alternatives Incorporated

2. Summary of Overall Impact at SO and IR level

118-014-01 Improved economic infrastructure to support market-oriented growth.

This SO met or exceeded its targets on all key indicators.

IR 1.4.1 Tax system fair and efficient.

Met target.

IR 1.4.2 Legal and regulatory framework for the financial sector established and strengthened
Bank licenses revoked by Central Bank of Russia (CBR).

Met target.

IR 1.4.3 International Accounting Standards will properly match revenues and expenses to improve existing operations and will make financial reporting transparent to domestic and international investors
International Accounting Standards adopted by companies.

Met target.

IR 1.4.4 Economic Think Tanks' analytical and policy advice capabilities strengthened to support sound policy formulation.

Met target.

3. Summary of Activities and Success Stories

During the life of this SO, the federal government of Russia enacted major laws advancing economic policy, pension reform, tax reform and deregulation. Capitalizing on this situation, USAID-supported

policy institutes had a major hand in building an economic, legal and regulatory infrastructure for broad-based private sector growth.

Through these successes the Government of Russia (GOR) is reaping a return on almost a decade of economic policy work. The policy institutes supported by USAID have had significant success in shaping fiscal policy. Russia's regions are placing increasing importance on intergovernmental fiscal policy, as evidenced by the fact that 16% of the regions have adopted transparent formulas to distribute their funds to municipalities. The Ministry of Finance incorporated several recommendations from the Center for Fiscal Policy into the Russian Budget Code. A new tax law developed by the Institute for the Economy in Transition (IET) reduces the corporate profit tax rate from 35% to 24%. Seven months after a new 13% personal income tax rate developed by IET took effect, revenues had increased by 54%. Russia's current tax regime is now considered the most liberal in Europe.

Through USAID's Loan Portfolio Guarantee Program, BIN Bank has made 75 loans totalling \$3 million to small and medium-sized enterprises (SMEs) through its branches in four regions. BIN Bank's success demonstrated that SME lending could be profitable; three more commercial banks have been accepted into this program to provide at least \$5 million in loans to the cash-starved SME sector. Following recommendations developed with USAID's technical assistance, the CBR mandated that all commercial banks adopt international accounting standards by 2004.

Twenty-seven USAID-funded policy institutes and analysts disseminated 180 publications to government officials and developed key reform legislation. In July 2000, the Parliament's lower chamber (Duma) passed laws developed by the National Project Institute, which greatly lowered administrative barriers to businesses by example by: reducing the activities subject to state licensing from over 500 to 104; easing business registration procedures; and limiting the number of state inspections.

Under this objective, USAID also supported regional economic development on Sakhalin Island in the Russian Far East to help foster the spread of economic benefits from the island's oil and gas sector. USAID funded a comprehensive workforce assessment for the Sakhalin oil and gas industry. In addition, the Sakhalin Duma enacted the Sakhalin Fund for Future Development. Modeled on the Alaska Permanent Fund, the fund allocates a portion of Sakhalin's future revenues to educational and sustainable development projects, including a technical training college.

Although personal deposits in Russian banks grew by 40% over the last year, banking sector reform, crucial to Russia's economic development, remains the most complicated and politically sensitive of the economic reforms. Because there is some modest movement — e.g., the GOR's acceptance of a banking reform strategy — USAID will support a small amount of policy work in the banking sector. Most of our work in the sector will, however, shift to regional commercial banks. The challenge of increasing the quality of economic analyses will require exposing policy institutes to international economic policy through visits by experts. Meanwhile the top institutes will require continued institutional strengthening to become self-sustaining.

The final challenge, to promote wide public discussions on the benefits of economic reform, requires that staff of policy institutes be trained in dissemination and advocacy. USAID's think tank program will seek to address these challenges facing the policy institutes through working with select institutes.

4. Prospects for the Future

Challenges

The banking sector reform, crucial to Russia's economic development, was one of the most complicated and politically sensitive of the economic reforms. To promote wide public discussions on the benefits of economic reform required that staff of policy institutes be trained in dissemination and advocacy.

5. Lessons learned for application to other SOs

A follow-on objective, SO 1.4 *Market-oriented Reforms Developed and Implemented in Selected Sectors* was approved in 2003.

6. Summary of indicators and their usefulness for performance management

118-014-01 *Improved economic infrastructure to support market-oriented growth*

This SO-level indicator measured the investment in fixed assets and the improved capital accounts in balance of payments. The data, from International Monetary Fund reports, indicated a steady increase in fixed assets investments as well as a positive balance of payments in capital accounts.

Intermediate Result 1.4.1: Tax system fair and efficient.

Indicator: The reduction of tax exemptions and the taxpayer cost of tax filing.

Comments: This indicator proved useful in following the changes and simplification of the tax code over time.

Intermediate Result 1.4.1.3: Objective criteria and system developed for transfer of resources from center to regions.

Indicator: Transparent criteria for distribution of federal funds to regions by formula.

Comments: This indicator measured the percentage of Russia's regions that adopted transparent formulas to distribute regional funds to municipalities. This proved to be a useful indicator to measure transparency and objectivity of intergovernmental fiscal relations at the regional-municipal level of government.

Intermediate Result 1.4.2: Legal and regulatory framework for the financial sector established and strengthened.

Indicator: Bank licenses revoked by CBR.

Comments: This indicator measured the annual percentage change in personal deposits in Russian banks. It provided clear evidence that personal deposits in Russian banks steadily climbed through the life of this project.

Intermediate Result 1.4.3: International Accounting Standards (IAS) will properly match revenues and expenses to improve existing operations and will make financial reporting transparent to domestic and international investors.

Indicator: International Accounting Standards adopted by companies.

Comments: This indicator measured the number of banks that adopted International Accounting Standards as required by the CBR. It helped to more accurately reflect USAID efforts to promote IAS as the cornerstone of the Russia commercial bank regulatory system.

Intermediate Result 1.4.4: Economic Think Tanks' analytical and policy advice capabilities strengthened to support sound policy formulation.

Indicator: Number of publications presented to government officials.

Comments: This indicator was useful in understanding the productivity of economic think tanks in their policy advocacy role.

7. Appendix

USAID/Russia Annual Reports 1999 – 2002

Assessments conducted:

- 2001: Evaluation of Strengthening Economic Think Tanks Program, conducted by Management Systems International

Progress reports and final reports:

- Strengthening Economic Think Tanks Program project Final Report for the period September 1999 –September 2002
- Improvement of Economic Policy through Think Tank Partnerships project reports for the period September 2001-September 2004
- Economic Policy Reform project with the Institute for the Economy in Transition reports for the period July 1998 – August 2000.

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Center for Fiscal Policy - Quarterly Reports 2003 - until now
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Deloitte & Touche (DTT) – USAID/Russia Quarterly Reports 2000 -2003 and Final Report
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Carana Corporation – [This is Washington-managed contract that was scheduled to be closed in September 2005. However the Mission has not yet received their final report].
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