# Productive Investment, Despite Debt Burden, Is Priority for Russia

by Rachel Douglas and Jonathan Tennenbaum

Academician Dmitri Lvov and State Duma (lower house of Parliament) Economic Policy Committee Chairman Sergei Glazyev will take part in Russian government deliberations on social and economic policy for 2002-04. These two leading advocates of dirigist credit-direction to rescue and develop the real sector of the economy, were earlier invited to the March 22 cabinet debate of long-term economic policy. The newspaper *Vedomosti* reported on May 29, that Prime Minister Mikhail Kasyanov is currently conducting the preparatory discussions on budget policy for the 2002-04 period behind closed doors, and suggested that the confidential nature of the talks means that fundamental questions of state economic policy are on the table.

According to *Vedomosti,* the government will not try to reduce social spending in this immediate period ahead, despite pressures to do so from the free-market liberals. *Vedomosti* commentator A. Becker observed, "The presence of Academician Dmitri Lvov at the meeting suggests a resumed discussion on redistribution of the so-called natural rent, from the fuel sector to the devastated production sphere. Sergei Glazyev, head of the State Duma's Economic Committee, will certainly raise the issue of 'managing excess liquidity,' suggesting that the real economy should receive credits through a system of state-run banks, in particular, using the assets of Sberbank [the state Savings Bank]."

The May 28 meeting of the government was devoted to this year's and the 2002 budget—both the revenue side, and the enormous, mounting pressures for spending. President Vladimir Putin told the cabinet, "It is better to tell the truth to the population, to say sincerely what the budget will be able to provide, and what will not be covered." The meeting occurred three days after Putin returned from touring the flood-devastated Yakutsk region, where budget-busting multibillion-ruble damages have occurred. Putin has brought up the need for the country's main diamond company, based in that area, to sell gems, and maybe stock shares, to raise funds for repairs.

At the May 28 session, Putin criticized the government for working every day on the budget, but with "no visible results." *Vedomosti,* among other sources, interpreted his remark as a blast at Finance Minister Aleksei Kudrin, who was responsible for completing the budget calculations by the end of May.

## Debt Service . . .

During May, Kudrin boasted about Russia's high debt-paying ability. On May 17, he said that Moscow has no plans to apply for IMF loans either this year or next, and would continue to do without such loans if spending can be controlled. On May 22, Kudrin stated that Russia may drop its demand for rescheduling of its Paris Club (Soviet-era, state-to-state) debts, and still be able to make all foreign debt payments on schedule.

In a speech to the European Business Club on May 25, Glazyev demonstrated that to make all payments on all debts that are on the books, would demand that 80% of all of Russia's budget spending in 2003 go for debt service. That being simply impossible, the prospect of default would loom. Since international creditors have no interest in a Russian default, Glazyev advised that they support a workable alternative. He presented the proposals for "avoiding default," developed with his participation, by the Russian Association of Foreign Economic Organizations.

## . . . or Debt-for-Investment?

Glazyev pointed to the agreement reached during the visit of Spanish Prime Minister José María Aznar to Moscow, in May, as a model for what could be done on a much bigger scale. "Although the role of the debt to Spain within the overall structure of Russian foreign debt is relatively small (about $900 million), the agreement can become a serious step toward the realization of the scheme of 'exchanging debt for investment,' whose necessity was pointed out by President Putin at the end of last year," Glazyev said.

The basic concept, is that foreign investors would purchase portions of Russian debt, receiving in return "adequate sums" of Russian rubles, to be invested in Russia, on the condition that the money be kept in Russia for a minimum of five years. The investor can freely choose what to invest in, but the Russian government would provide tax breaks, state guarantees, and other privileged treatment for investments into sectors and projects, deemed to be particularly beneficial to the Russian economy. Such schemes are well-known in international practice, Glazyev noted.

Russia has applied the debt-for-investment principle to Algeria's debt owed to Russia. Deputy Prime Minister Ilya Klebanov, visiting Algiers in May, signed an agreement to restructure part of Algeria's some $4 billion of debts to Russia, and convert the remainder into investment, particularly in industry and irrigation projects. Klebanov noted that the agreement would significantly improve trade and economic cooperation between the two countries. In addition, Russian firms have started to bid on contracts in Algeria for the construction of energy infrastructure.