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Impact of Monetary Policy of the Central Bank on the Economic Growth in Russia in the Conditions of Unstable Economy

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Abstract

The purpose of this Article is to identify major trends in monetary management and to analyze the main directions in monetary policy of the Bank of Russia and their correspondence to Russia's economic and political realities. In the course of the research, statistical method was used as the basic one, as well as methods of scientific abstraction, analogy, comparison, and diagram analysis. The Article analyzes Russian practices of applying monetary policy tools by the Bank of Russia and evaluates the efficiency of this policy. The impact of monetary management tools on the scope of bank crediting to businesses and the pace of economic growth are investigated. The Author underlines negative aspects of the Bank of Russia's policy based on the analysis of statistical data characterizing Russia's economy status, and describes the effects of the Bank of Russia's policy in regard to inflation targeting. In accordance with international experience and major tendencies in this area, there possible directions of improving Russia's monetary policy are proposed, in particular, the shift of milestones towards achieving positive pace of economic growth and pursuing a double-purpose policy, which, in the Author's opinion, is of paramount importance at the present stage of Russia's economy development in the conditions of economic and political instability, crisis and shocks.

Keywords: monetary policy, interest rate, inflation targeting, refinancing, economic growth

1. Introduction

In international practices, monetary policy has been traditionally one of the most important tools of governmental influence on economic life. Despite a long path of development of economics as self-sufficient science, the very concept as to the necessity and reasonability of monetary management on financial market by the government started to be actively developed only in the 20th century, during the time of prevalence of liberal model not involving any deep penetration of "the machinery of government" into economic processes. Economic crises between the late 19th and early 20th century, in particular, the Great Depression in the United States (1929-1933), revealed the vulnerability of this model and its inability to cope with severe consequences of crises without governmental intervention. Precisely since then, the use of various tools of governmental influence on financial market, including monetary stock in the economy, on which both inflation process and the pace of production expansion and economic growth depend, became one of the basic functions of national regulators on financial market.

Questions of the issues associated with the theory and practice of state monetary policy were reflected in works of many authors. Among Russian economists, the following can be distinguished: M. A. Abramova, J. S. Golikova, S. R. Moiseyev, A. V. Ulyukayev, A. J. Simanovsky, G. A. Tosunyan, etc. In foreign countries, the specific issues of monetary policy were worked out at different times by W. Allen, S. L. Brue, C. R. Mcconnell, F. Mishkin, N. Mogud, S. Rinhart, G. Sather, W. Smith, J. I. Harris, D. L. Hicks, G. Hogarth, J. Schumpeter, etc.

It should be noted that, in this day and age, major economies still place special emphasis on monetary policy and its target-oriented constituent (for example, the United States, China, the United Kingdom, Japan, Switzerland, etc.).

However, some important aspects of monetary policy, in particular, conformance to the requirements of modern economic status of Russia, flexibility in the conditions of unstable economy and crisis on financial market, are underrepresented in the works available. Both the Russian government and the Central Bank underestimate the potential of monetary management tools.

In view of the pressure on Russian economy, monetary policy tools may currently become active means of influencing the rates of industrial production growth.

Despite the analysis of Russia's financial market statistics and mainly Russian experience in terms of the impact of monetary policy on economic growth, the present study may be of practical importance also for other economies belonging to the group of countries with developing markets.

2. Principal Directions of Monetary Policy of the Bank of Russia at the Present Stage

Unfortunately, despite the critical condition of domestic economy, which is especially exacerbated by geopolitical events, Russia's monetary policy is still pursued by the Bank of Russia as a tool for restricting rather than facilitating economic growth (Note 1). The steps made by the Bank of Russia during exchange market crisis in November and December of 2014, confirm this point once again.

Economic growth, price stability and high employment rate are usually distinguished as basic and long-run objectives of monetary policy. In accordance with the applicable legislation, i.e. the federal law No. 86-FZ "Concerning the Central Bank of the Russian Federation (the Bank of Russia)" dated July 10, 2002, the main purpose of Russia's monetary policy consists in "*... protecting and ensuring ruble sustainability by maintaining price stability, in particular, for creating conditions of balanced and sustainable economic growth...*" This target-oriented priority is also enshrined in the main program document "Main directions of governmental monetary policies for 2014 and for the period of 2015 to 2016", and laid down in the same document for the upcoming three-year period of 2015 to 2017 as well. Thus, among the variants of target-oriented goals for monetary management, the Bank of Russia chose *to maintain price stability*, which was called the Inflation Targeting.

Within the framework of the policy pursued by the Bank of Russia, quantitative objectives of achieving inflation rates were marked as follows: 5.0% in 2014, 4.5% in 2015, and 4.0% in 2016. With due regard for unfavorable economic and political situation in the country, these targets were shifted to 2017. All other monetary tools are used by the Bank of Russia to the extent necessary to ensure the performance of the preset targets.

It is important to note that the inflation targeting policy itself implies reducing of monetary stock in the economy, and tightening of credit conditions means, or higher interest rates, respectively, which does happen in practice. Thus, during 2014, key interest rate was increased six times by the Bank of Russia: from 5.5% (as of February 03, 2014) to 17% (December 16, 2014). On December 16, unprecedented rate increase by 6.5% at a time happened. Thus, during 2014, the rate grew up more than threefold. Such serious increase in interest rates has not happened in Russia since 1998. Despite the fact that such a significant increase in key interest rates was due to the need to stabilize the situation on Russia's currency market and reduce the speculative appetites of major players, this tool is primarily used for monetary management, and therefore, its influence extends far beyond foreign exchange market.

The restrictive nature of monetary policy is also confirmed by the scale of absorbing by the Bank of Russia as to banking sector liquidity: during the period between January 01, 2014, and December 01, 2014, absolute cash outflow from banking system through the tools of the Bank of Russia was 16.5 trillion rubles.

According to the Bank of Russia, for the ten months of 2014, inflation has already reached 7.1%. Based on the forecasts of the Ministry of Finance of the Russian Federation, by the end of 2014, inflation will exceed 9%, and it may become double-digit in 2015. Recent activities of the Bank of Russia show that real situation may become even more adverse.

Therefore, targets as to inflation level will not be reached either this year or in the years to come. Moreover, for over 20 years of its activities, the Bank of Russia has never been able at any stage to reach the inflation rate which is optimal for mature economies (1-2% per annum), or even to come close to the average rate of 3 to 5% in developing economies.

It should be noted that such a substantial and abrupt increase in key interest rates may have the reverse effect. The increase in key interest rates will lead to the increase in market borrowing rates, first for credit institutions through interbank market (this has already happened, as Mosprime Rate grew to 30% per annum, see Figure 1), as well as deposits, and then, for end consumers—the population and businesses. The increased borrowing costs will be added to the prime costs of products by manufacturers, and therefore, it will lead to the increase in costs with regard to only financial resources, as well as goods, works and services. At the same time, such panic-like increase in interest rates will lead to exponential increase in inflation expectations. Thus, instead of constraining inflation and stabilizing prices, further ruble devaluation and strengthening of inflation expectations will take place, which will ultimately lead to even more dramatic growth of inflation.

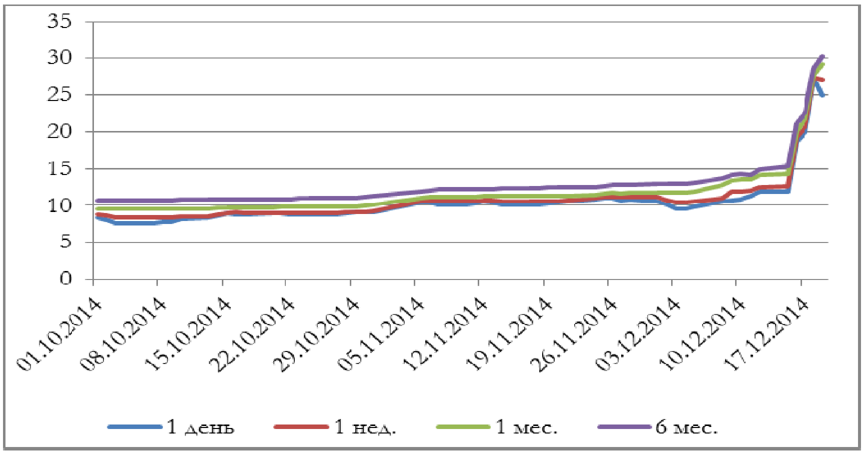

Figure 1. Dynamics of the change in interest rates on interbank market, %

3. Current Status of Russian Economy

Currently, Russia's economy is in diseased state.

The comparison of rates of economic growth and inflation in a number of countries shows negative tendencies in the development of Russian economy. The World Bank predicts that inflation in Russia will be at the rate of 8.3% with GDP growth of 0.7% at year-end 2014, which is comparably worse than in India, China and RSA being part of the BRICS as well (Figure 2).

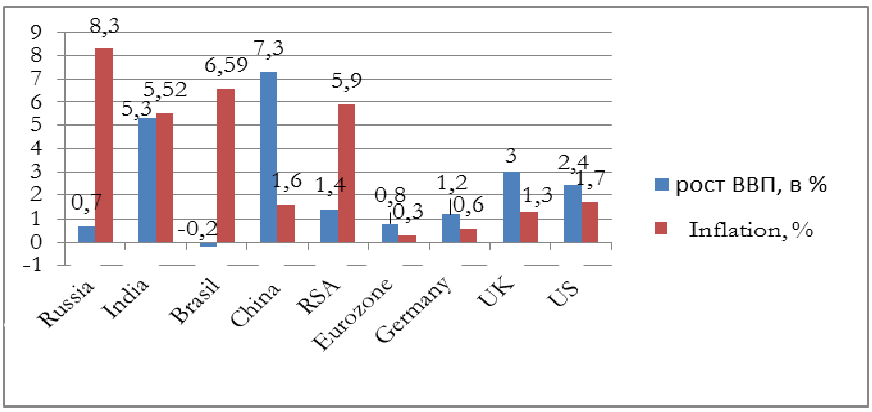

Figure 2. Predicted values of GDP growth and inflation at year-end 2014

The dynamics of changes in these indices for the period between 2000 and 2014 is as follows: considerable deviations and abrupt drop-downs point at the instability of Russian economy compared to India, Brazil and China. During financial and economic crisis of 2008 to 2010, the drop-down of Russia's GDP was more noticeable as compared to that of the countries under consideration (see Figure 3).

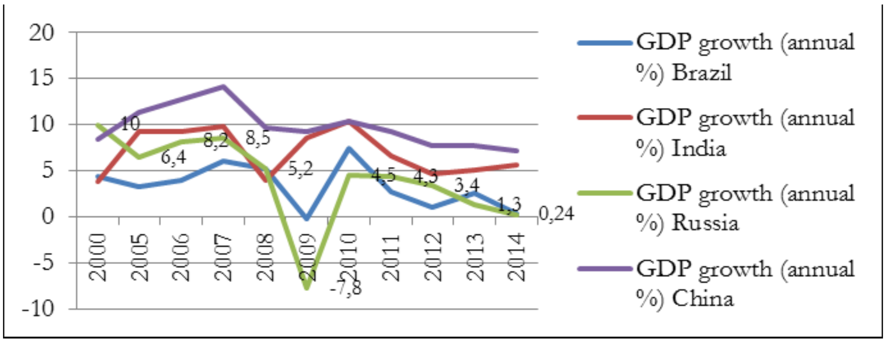

Figure 3. GDP growth rate for the period between 2000 and 2014

Similar situation is observed, when analyzing the dynamics of changes in inflation rate for the period under consideration (Figure 4).

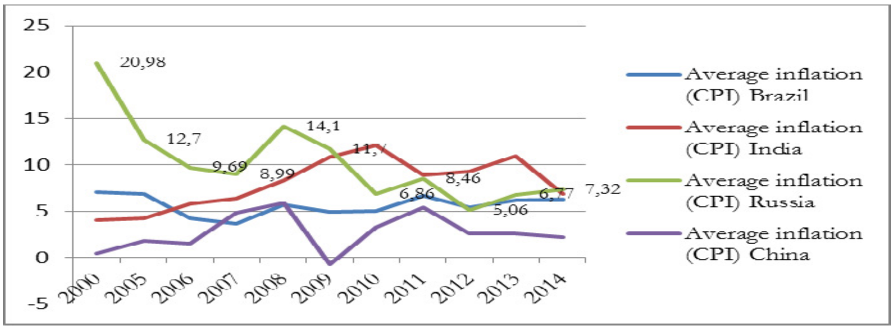

Figure 4. Inflation rate for the period between 2000 and 2014

According to the estimates given by a number of economists, begun stagnation has already begun in the country. Possible recession is anticipated for the years to come. Without doubt, external factors (geopolitical risks) (Note 2) make a significant impact on current situation. However, it is not just them, it is the problems accumulated within the country. The Russian government has been turning a blind eye to these problems a long while, just stating them as facts, but it has made no effective steps to solve them.

The main problem lies in the structural imbalance of Russian economy, its high dependence on energy source exports and, respectively, on currency incomings, and lack of the country's own internal industries in major sectors.

The energy prices that have been increasing over nearly 15 years allowed to successfully finance all expenditures of national budget (over half of which is formed based on oil and gas transfers), to maintain acceptable rates of economic growth, and to increase salaries for the population, despite the fact that the economy was not developing de facto.

However, the situation in Russia has changed dramatically. What do we see?

• The pressure of sanctions, including the closure of capital market for the country's largest financial institutions and the entities with state participation, as well as technologies;

• The limitedness of internal borrowing market: internal market is not profitable, interest rates are high;

• The reduction of oil prices, and other energy sources, subsequently: since the beginning of 2014, oil prices has been decreased by more than 30% (Note 3);

• Ruble devaluation with regard to foreign currencies: since the beginning of the year, by over 50%;

• The reduction of investment capital inflow to the country (Note 4), and significant capital outflow, respectively, including the transfer of funds into foreign currency (Note 5) by Russian entities;

• The disruption of Russian stock market: since the beginning of the year, the index of Russian Trading System has decreased by over 40%. The most significant decrease occurred in the following economy sectors: electric-power industry—24.6%; banks and finance—28.4%; telecommunications—31%; machine-building industry—40% (Moscow Exchange, 2014);

• Performance indices of Russia's economy going down: since 2006, labor productivity index has been decreasing continuously (the drop-down compared to the maximum of 2006 is 4%); fixed-assets renewal coefficient is only 4.7%, with depreciation rate of 48.2% (Federal State Statistics Service, 2014);

• By the end of the first half of 2014, the decrease in the consolidated index of output intensity of goods and services in basic types of economic activities compared to the same period of previous year has reached 4.8%, as compared to the same period of previous year (Monthly report, 2014, p. 5).

As a result:

• Increase in inflation level and decrease in the purchasing power of national currency;

• Decrease in real disposable money income of citizens;

• Growth rate reduction in the economy.

The above aspects in aggregate determine the reduction of currency inflow in Russia, that, with the persisting demand for the currency on the part of economic entities (in particular, to service external corporate debts attracted from international capital markets; the demand on the part of individuals for the purposes of savings, which is driven by inflation expectations and adverse dynamics of ruble exchange rate), and speculative attacks on ruble put pressure on ruble exchange rate and promote its further devaluation (see Figure 4).

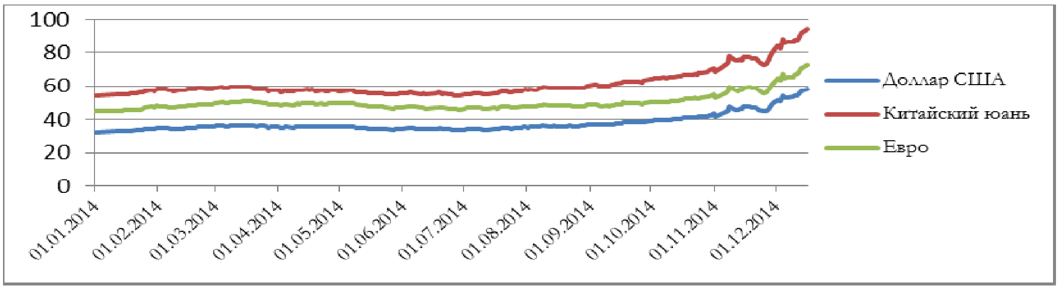

Figure 5. Dynamics of changes in ruble exchange rate with regard to main world currencies (The dynamics of the official exchange rate, 2014)

Unless we move away from the dependence on energy source exports and, respectively, from currency incomings, the amounts of which can be significantly influenced by external operators, we will not have a chance for fundamental improvements in Russian economy.

It is necessary to develop internal market, which requires investments. Until recently, such resources have been actively attracted from foreign markets (the consequences of such tactics are described above). Currently, in the changed political and economic situation, resources for financing the investments need to be generated internally within the country, not in external markets. However, due to current monetary policy, finding the opportunity for such financing does not seem possible.

4. Role of Banking Sector in Ensuring Economic Growth

The role of banking sector in ensuring economic growth is to transform the temporarily free funds of various economic entities, including short-term funds, into long-term capital, which in turn is the source of investments in the real sector of economy. At the same time, by loan granting and the possibility to participate in stock market as investors, credit institutions create the channels for floating temporarily free funds to the businesses of real sector, which are in need of investments for the purpose of modernization, as well as overcoming the consequences of crisis.

Investments are exactly the main driving mechanism of the economy. Thus, the role of banking sector in ensuring economic growth is to accumulate funds from various entities and transform them into investments.

Global practice shows that banking sector actively copes with the above role. For example, according to various estimates, the contribution of European banks to economic development is 250 to 500% of GDP (Rakhmetova, 2014, p. 74). In the source-based structure of investment financing, the share of bank loans in the USA is 32.5%, and in Germany—41.8 %.

A reverse trend is typical of Russia. According to the Federal State Statistics Service, Russia's current investment financing is carried out mainly due to internal sources of business entities and their parent companies—58%; budgetary funds account for 19%; stock market accounts for only 1%; bank loans account for 10%.

The ratio of banking sector assets to GDP as of 2014 is 86%. It is noteworthy that assets exceed twofold the value of consolidated national budget. Loans (excluding loans granted to financial institutions) make 48.6% of GDP. However, only about 3% of credit resources are allocated to investment financing, which is manyfold lower than in other countries. Within the structure of corporate loans granted by banks, only 1.5% are used in machine-building industry. The share of bank loans as to investments in fixed assets of entities makes only 1.5% against GDP. At that, Russia's GDP value is considerably lower than that of the world's major economies (Note 6).

During the economic forum held in St. Petersburg in 2014, President Vladimir Putin specified that "...Russia needs real technological revolution..." To implement these large-scale modernization activities, enormous resources are required. In this regard, major hopes are traditionally laid on banking sector and loans. In such circumstances, Russian banking sector has often been criticized for its inability to fulfill its most important purpose—to meet the financial needs of the economy, thus restraining economic growth. However, are banks the only ones to blame?

Unfortunately, it has to be said that, due to current interest rates, effective demand is also lacking on the part of business entities for credit resources necessary to make investments. High interest rates represent the significant obstacle, if not major limitation, on the way to increasing the pace of crediting the economy. Earlier, we mentioned that key interest rate has already reached 17%. At such level of rates, actual loans will be provided for end recipients at the rate of 20 to 30%. With the profitability of sales in general in the Russian economy at the level of 7.7% at year-end of 2013, and in key sectors that are in need of investments, at the level of 6 to 10%, such high interest rates are back-breaking and inexpedient (see Table 1).

Table 1. Sales profitability level in key sectors of Russian economy at year-end o2013 (Legal information portal GARANT.RU, 2014)

Economy sector	**2013**
Total,	7.7
including:	
Agriculture, hunting and forestry	6.3
Fishing and fish-farming	21.5
Mining	25.1
Manufacturing industries	9.5
including:	
Production of foods, including beverages, and tobacco	10.1
Textile and garment manufacture	7.1
Manufacture of leather, leather products and footwear production	6.2
Woodworking and manufacture of wooden products	8.1
Pulp and paper production; publishing and printing activities	9
Manufacture of coke and oil products	9.6
Chemical production	16.7
Manufacture of rubber and plastic products	8.7
Manufacture of other non-metallic mineral products	9.8
Metallurgic production and manufacture of finished metal products	9.9
Including: metallurgical production	10.3
Manufactureof finished metal products	8.2
Manufacture of machinery and equipment	7.5
Manufacture of electrical, electronic and optical equipment	8.9
Manufacture of transport means and equipment	5.8
Production and distribution of water	4.7

Building and construction	4.8
Wholesale and retail trade; repairs of motor vehicles, motorcycles, household goods and personal demand items	7.1
Transport and communications	9.9
Financial activities	0.4
Education	5.3
Healthcare and social services	5.9

In these circumstances, due to the lack of any specific measures of government support to subsidize interest rates of investment loans for business entities in key sectors of economy, economic growth becomes totally impossible.

On the other hand, long-term monetary policy announced by the Bank of Russia implies further fighting against the inflation and, consequently, further increase in interest rates. Thus, in fact, the Bank of Russia's policy contradicts Russia's interests with regard to the development of internal economy and solving of realized, long-standing problems.

Apart from direct impact on interest rates on the market (through key interest rate), the Bank of Russia also can actively apply tools for refinancing credit institutions. Refinancing is of dual nature. On the one hand, it is an efficient measure to regulate the liquidity in banking sector, and, on the other hand, it is an effective tool of monetary management.

The two key factors influencing the scope of refinancing are as follows: the demand on the part of credit institutions themselves, which may be at the same time artificially limited by high interest rates, and the offering of funds by the Bank of Russia.

As a tool of monetary policy, the scope of crediting by the Bank of Russia as to credit institutions is of paramount importance, since the scope of crediting various economic entities by commercial banks depends, in a greater degree, just on this index through banking multiplication. The introduction of money into economic circulation through crediting mechanism contributes to the performance of money-specific functions, the expansion of production and of the ensuring of economic growth.

However, in accordance with inflation targeting policy, it is the monetary growth ensured by way of increasing crediting scope that is one of the main inflation factors to be fought with.

Taking into consideration that the reduction of the scope of crediting by the Bank of Russia for credit institutions can lead to serious difficulties with liquidity in banking sector and to banking crisis, the Bank of Russia makes an impact on this market by regulating interest rates (see above—increasing key interest rate).

In our opinion, this policy, as well as the negative perception of credit in the specified context, cut down its positive role as the source of investments and the catalyst of economic development.

Refinancing of credit institutions is mainly performed in two ways-direct lending and repo transactions.

Figure 6 shows the dynamics of changes in credit institutions' indebtedness to the Bank of Russia in repo transactions.

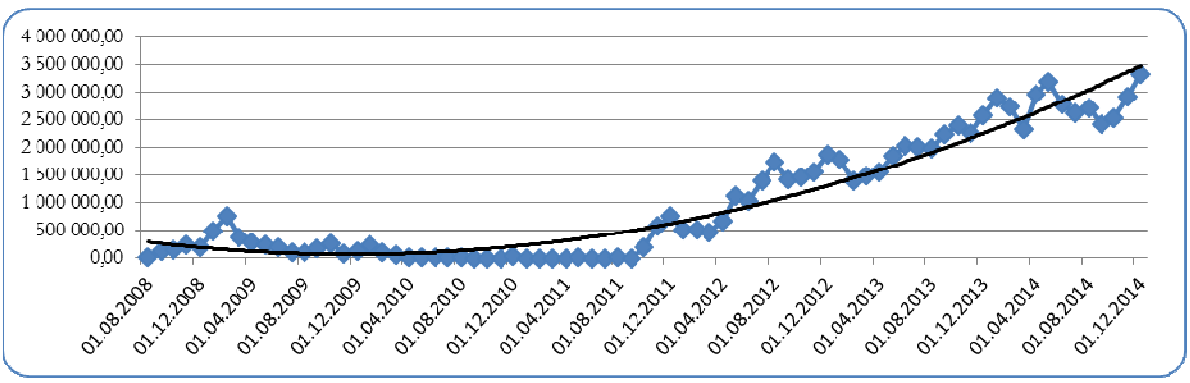

Figure 6. Indebtness of credit institutions to the Bank of Russia in repo transactions (for the period from 01.08.2008, to 01.12.2014, mln. RUR)

The data shows that in 2012 the volume of indebtness was increasing steadily, despite some fluctuations. This was due to liquidity problems in banking sector, the increasing needs of the banks in cash (as evidenced by the rising trend line). As of December 1, 2014, the volume of credit institutions' indebtness to the Bank of Russia in repo transactions has exceeded 3.3 trillion RUR. It is noticeable that 84% of the sum was payable under repo transactions conducted on an auction basis, and transactions conducted at a fixed rate amounted at 16% of the total transactions volume. This situation can be explained by prevailing interest rates. Considering transactions at fixed rates, the cost of the funds attracted under repo transactions would be 10.5%, and considering transactions on auction basis, the average weighted rate on applications approved within the limit at the close of trading held on November 27, 2014, has amounted to 9.9% per annum.

Similar situation is observed in studying the volume of direct lending to credit institutions by the Bank of Russia (see Figure 7): significant volumes—3.1 trillion RUR as of December 01, 2014, and sharp increase in indebtness since the second half of 2013.

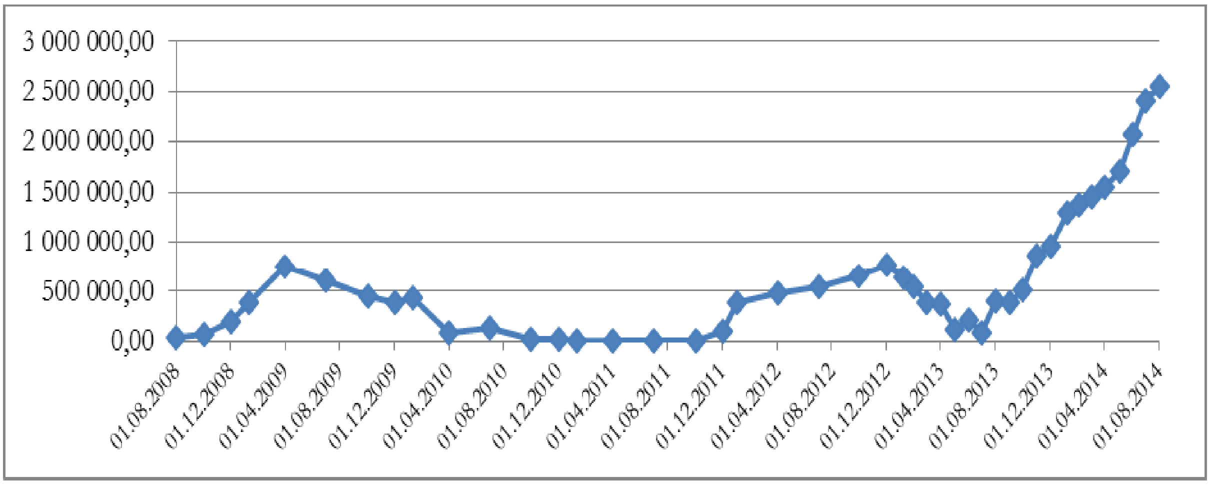

Figure 7. Indebtness of credit institutions to the Bank of Russia on secured loans (for the period from August 1, 2008, till December 1, 2014, mln. RUR.)

However, the existing refinancing volumes are aimed just at ensuring the liquidity of banking sector, and are allocated by banks primarily to cover their current liabilities, and do not allow to use the banking multiplier effect in full directing resources for lending to the economy. Despite the increasing volumes of credits attracted by the banks from the Bank of Russia, the indicators characterizing money supply have the reverse dynamics. According to the Bank of Russia, during the first half of 2014, the money supply (M2) has decreased by 3.1%, amounting to 30.4 trillion RUR as of July 1, 2014. In the third quarter, the decrease continued, and as of December 1, 2014, M2 has amounted to 30.3 trillion RUR. Once again, it's worth mentioning that the decrease in money supply has not led only to a decrease in the inflation rate, but to a significant slowdown in its growth. As compared to inflation indicators of the same period in 2013 (first half), inflation has increased by 0.9 percentage points (see Table 2).

Table 2. Comparative characteristics of inflation level in 2013 and 2014 (by months, %)

Period	2013	2014	Absolute deviation compared to the previous year, %
January 1	1	0.6	-0.4
February 1	0.6	0.7	0.1
March 1	0.3	1	0.7
April 1	0.5	0.9	0.4
May 1	0.7	0.9	0.2
June 1	0.4	0.6	0.2
July 1	0.8	0.5	-0.3

August 1	0.1	0.2	0.1
September 1	0.2	0.7	0.5
October 1	0.6	0.8	0.2
Total			**1.7**

At the same time, the above measures have led to the increase in the cost of resources in the interbank market (see Fig. 1). Only in 2014, the rates in the interbank market for all terms of borrowing have increased over 4 fold.

Appreciation and decrease in resources volume have obviously affected the size of lending to the economy. Thus, analyzing the total volume of lending to resident legal entities and individual entrepreneurs (in RUR), including the industries related to manufacturing, descending trend with a negative outlook for further development has been identified (see Figure 8).

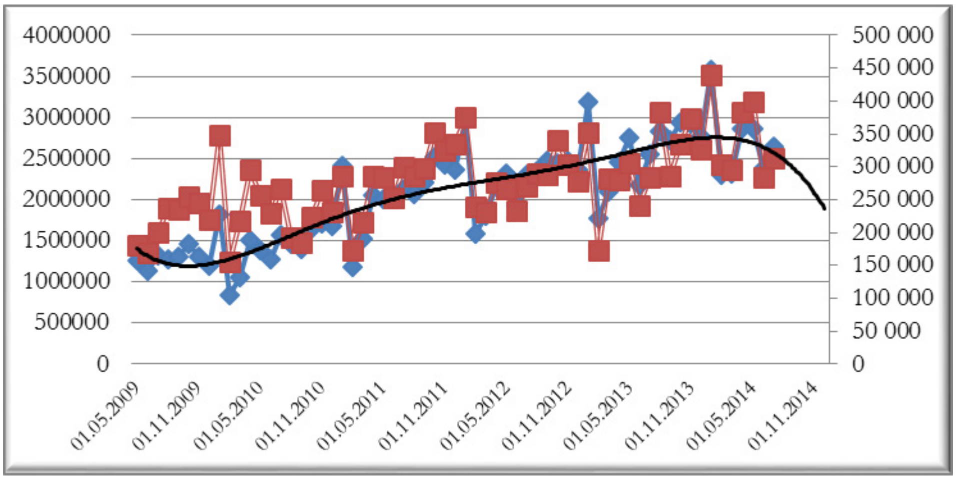

Figure 8. Monthly volume of lending to legal entities and individual entrepreneurs, mln.RUR. Blue line—Monthly volume of credits provided, total. Red line—Credits to manufacturing sector

5. Global Practice

The practice of implementing the policies of long-term money expansion in the economy and long financial resources emissions by national regulators in developed countries is quite interesting. We know a lot about the role of money in the monetary transmission mechanism during periods of quantitative easing (Money creation in the modern economy, 2013).

Unfortunately, the Bank of Russia has been acting in the reverse way. As to refinancing instruments, short-term and super-short-term instruments were primary applied.

During the post-crisis period, there appeared a worldwide tendency of attracting the interest of entities, including commercial banks, to invest in internal economy, also known as *home bias*. For example, the standards making financial investments abroad less attractive for banks were applied in Switzerland.

In order to provide access for the real sector enterprises to bank loans, the Swedish National Bank has introduced the world's first negative rate on deposits of commercial banks at the central bank equal to minus 0.25%, and the base repo rate was reduced from 0.5% to 0.25%. This extraordinary measure of the Central Bank of Sweden was aimed at stimulating the real economy crediting by banking sector.

The British Government, together with the Bank of England, has launched a program of lending to banks at interest rates lower than in the market, providing the latter allocate resources for lending to non-financial sectors of the economy, i.e. to the real sector—Funding for Lending, FLS. This program was not aimed just at stimulating lending, and it consisted of several stages: at the first stage, banks could receive only 5% of the total volume of their loan portfolio, at the second stage, 100% of the newly provided loans to the real sector from the moment of the receipt of the first loan until the end of 2013. Herewith, banks were obtaining loans at 0.25% per annum, provided the loan volume at least was not reduced. In case the loan portfolio volume was reduced, for example by

5% or more, the rate would increase to a maximum level of 1.5% (Note 7). Not only large UK banks, such as HSBC, Royal Bank of Scotland Group PLC, and Lloyds Banking Group PLC, have taken part in the implementation of this scheme, as it was designed to encourage lending interaction between banking and real sectors of economy by providing cheap central financing in the limited resources conditions, but also the European Central Bank, which decided to launch similar program Longer-term refinancing operations (LTRO), with the only difference that the access to the preferential terms would be provided to those banks that would agree to lend to the real sector of the economy, and provide shorter crediting period (4 years for FLS, and 3, 6, 9 and 12 months for LTRO) (Note 7). Thus, the rate shall vary, depending on the dynamics of the loan portfolio: the initial rate is 0.25%, and, in case of reduction of the loan portfolio by 1%, the rate shall be increased by 0.25% to the maximum level of 1.5%. It is believed that the new technology of bank lending will allow for the expansion of volumes and accessibility of lending for the real sector enterprises by providing cheap central financing. The majority of UK banks have joined the implementation of this scheme.

6. Conclusions

Summarizing the above, it should be mentioned that, despite the declared objectives to promote economic growth, the current monetary policy implemented by the Bank of Russia does not reach its goals de facto. Along with the rising inflation, the interest rates continue to grow, resources are growing in price, money supply and volumes of lending to the real sector are decreasing, the size of the latter is being reduced, and, as a consequence, there is absence of the so much-needed economic growth, which is particularly complicated due to the geopolitical and international economic situation.

However, in Russia, inflation is of non-monetary nature, and, therefore, the struggle with it by implementing austerity measures does not lead to the desired result, as the current situation proves. Moreover, in current economic situation, the inflation targeting includes more threats than benefits, leading to financial instability, the negative effects of which will ultimately affect entrepreneurs. The latter aggravates business situation more and puts pressure on economic growth. In our opinion, at current stage, it would be reasonable to shift the focus of the monetary regulatory approach from inflation targeting to ensuring economic growth.

The nature of inflation is too complicated and ambiguous. Struggle with it by exclusively fiscal measures leads to mainly negative results, such as the decrease in production, the decline in GDP growth, along with the increasing inflation rate. This trend is confirmed by the dynamics of changes in the figures of inflation indicators and GDP growth rate in Russia and Brazil (see Fig. 9, 10). It is seen from the tables above that the increase of inflation rate is accompanied by the decline in GDP growth rate (2007 to 2009; 2012 to 2014), and, vice versa, the decrease of inflation rate leads to the increase in GDP growth rate (2006 to 2007; 2010 to 2011).

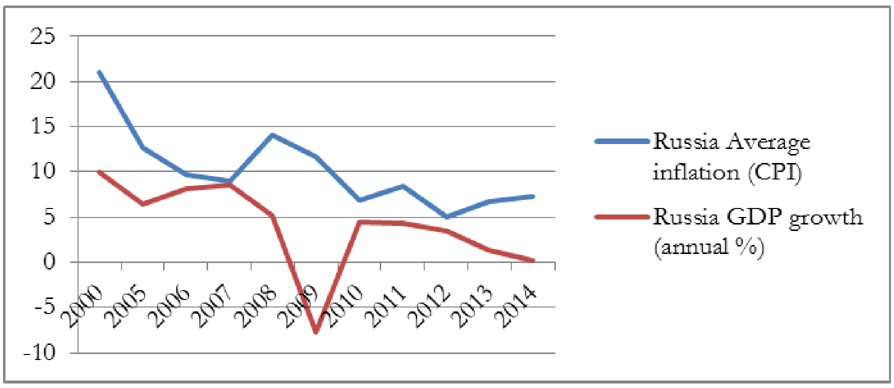

Figure 9. Dynamics of changes in inflation level and GDP growth in Russia, %

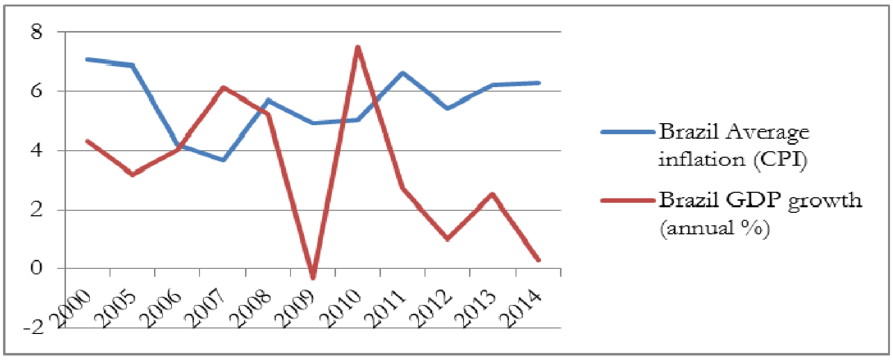

Figure 10. Dynamics of changes in inflation level and GDP growth in Brazil, %

A. G. Agabengyan, Member of the Russian Academy of Sciences, as well as M. V. Ershov, also mentioned the fact of the impossibility of inflation reduction solely by the Bank of Russia in their scientific works. According to their opinion (and we completely agree with it), the level of inflation depends on the national policy and on the antimonopoly legislation to a greater extent, rather than on the monetary policy of the Bank of Russia.

The disproportion between the amount of money in Russia and the size of the market still exists. The reasons for this can be found in the unbalanced money supply, which has been increasing over the past decade due to continuously increasing government spending (Note 8) (during the active phase of the crisis in 2008 to 2009, budget expenditures have increased by 23% and 15%, respectively), and export earnings from the sales of resources, along with the reduction of real domestic production (production of consumer goods and import in 2009 have decreased more than 1.5 fold). As a result, the amount of money in circulation has significantly exceeded the need for them in the existing turnover of goods, works, and services. Herewith, the excess in money supply is distributed unevenly among economic entities. As a result, the real economy industries are experiencing the serious deficiency of resources, along with their general excess in the country, and, with the existing level of interest rate, are not able to act as borrowers.

That's not the amount of money we need fight with, but with the weakness of Russian economy, and serious structural imbalances, as those are the reasons for "invincible" inflation. Consequently, the aim is to ensure economic growth, to allocate resources specifically for these purposes. The fight against inflation will only exacerbate the existing problems (namely, the enterprises of the real sector of the economy suffer from the increasing interest rates and the reduction of financial resources supply in the first place), will lead to greater economic recession, and further spiral increase of inflation.

There are historical examples of focusing monetary policy on more than one key goal (which is considered to be a traditional option for monetary paradigm development) (for example, the USA and China have effectively applied the bi-purpose system within different time periods).

For the purpose of economic recovery and acceptable growth rates within monetary regulation, it is required, in the first place, to focus on refinancing mechanism, to affect its scope and interest rates level correlated with the needs of the economy. Particularly, these tools are major leverages in advanced countries, and they allow to seriously affect financial markets, as well as national economy as a whole.

In our opinion, the Bank of Russia has to revise the fundamental directions of national monetary policy towards ensuring economic growth in the country, in the first place. It is also necessary to pay attention to the best international practice and adopt its positive aspects, in particular, to develop long-term lending to commercial banks for the purpose of providing investment credit resources to the enterprises of the real sector of the economy, as well as to establish various key interest rates, depending on the purposes of attracting resources by commercial banks.

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Notes

Note 1. In general, that corresponds to the Inflation Targeting policy.

Note 2. China successfully coped with economic sanctions applied to in at the end of 1990's . Moreover, since the beginning of 2000's , growth rates in China have been at the level of 8%.

Note 3. According to the estimates of the Ministry of Finance of the Russian Federation, Russia's losses caused by the dropdown of energy prices has already reached nearly USD 90 to 100 billion.

Note 4. According to the estimates of the Ministry of Finance of the Russian Federation—nearly USD 40 billion.

Note 5. According to estimates of the Ministry of Finance of the Russian Federation—nearly USD 130 billion.

Note 6. For reference: Russia's GDP is USD 2.2 trillion; China's GDP is USD 9.2 trillion; Euro zone's GDP is USD 12.8 trillion, including that of Germany—USD 3.6 trillion ; Brazil's GDP is USD 2.1 trillion.; India's GDP is USD 1.9 trillion.

Note 7. British banks will recieve 60 bln. GBP within the framework of Funding for Lending.

Note 8. The increase in government spending in time of crisis in economy on its own is a justified and appropriate measure, provided, however, the funds are directed precisely to economy in order to ensure the normal course of the reproduction process of the real sector of the economy, and to maintain the business activity of economies—The author's note.