Russia exchange rate system

Russia Exchange rate system Russia used to pledge its nominal exchange rate with some main currencies such as US dollar. However, the Russian crisis has forced Russia to develop managed floating exchange rate system, where the exchange rate driven by market forces of the Ruble's demand and supply with the help of government intervention. With this exchange rate, the government can ensure stability and predictability of ruble exchange rate and prevent abrupt fluctuation of the Ruble rate.

Moreover, this system could achieve the target set of money supply growth, and further ensure that the economic agents comply with the Russian legislation regulating foreign exchange operation.

The emerging markets financial crises of the 1990s had remarkable similarities. Attracted by high domestic interest rates, a sense of stability stemming from rigid exchange rates, and what at the time appeared to be rosy prospects, large volumes of foreign portfolio funds moved into Russia. This helped propel stock market booms and helped finance large current account deficits.

At some point, and for a number of reasons, these funds slowed down and/or were reversed. This change in conditions required significant corrections in macroeconomics policies. Invariably, however, adjustment was delayed or was insufficient, increasing the level of uncertainty and the degree of country risk.

As a result, massive volumes of capital left the country in question, international reserves dropped to dangerously low levels and real exchange rates became acutely overvalued.

Eventually, pegged nominal exchange rate of Russia had to be abandoned, and the country was forced to float its currency. According to the current account on Q4 2009 to Q1 2010, the export of both goods and services are slightly falling, whereas the import of both goods and service are sharply rising from –USD 60. 34 billion to – USD 45.

7 billion and –USD 17 billion to –USD 13. 8 billion respectively. The low export and high import decrease the demand of Ruble and increase its supply. As a consequence, the Ruble is pushed to the depreciation.

Conversely, due to the higher investment income, receivable, and lower payable have leaded Russia current account to a surplus of USD 17. 35 billion. Financial account records the dramatically high net outflow of USD 23 billion during Q4 2009 and Q1 2010. This was resulted from the slump Russia's asset value in all dimensions of general government, monetary authority and bank. As Standard and Poor's degrade on the Russia credit rating to BBB+ from A- in 2009 and further lower credit rating to BBB , the foreign demand for Ruble decline significantly and have a huge impact on its currency to depreciate.

High inflation causes an increase in price and affect the international trade of Russia. The inflation creates more import and less export, which finally result in Ruble depreciation. The little drop in liability with the co finance with IMF could not offset the crisis of its assets. Therefore, the government try to taking the control by inject USD 500 billion into the market, cutting down tax to be maximum at 18% from 24% in 2008, and extend unsecured stabilization loan to stimulate the economy.

Government Intervention on Exchange Rate Refinancing Budget Capital

Russia’s central bank cut its main interest rates for the fourth time in less than three months and the government estimated the economy contracted an annual 10. 2 percent in the January-May, 2010. Bank Rossii lowered the refinancing rate to 11 percent from 11. 5 percent following an initial reduction on April 24, 2010 and two further cuts on May 13 and June 5, 2010.

But the striking thing here is that today’s ruble surge followed seven consecutive days when it fell which dropped 0. 5 percent against the euro and 0. 1 percent against the dollar to hit the lowest close against the central bank’s currency basket since May 4. 010. Last week the ruble posted its steepest slide against the euro and dollar since January as oil prices fell and Russia’s budget deficit continued to widen.

Since the government has reduced the refinancing rate which make the country has greater budget deficit. Its show that the country has more debt than what they earn and it’s affects the income level of the country. The income level reduce make the Russian currency appreciate against the others. Tax and State Budget Policy November 20, 2009 Vladimir Putin announced government package of tax reforms.

Corporate profit tax rate (24% in 2009) is to be reduced to 20%. Profit tax base will decrease for companies investing in capital assets as the immediately-recoverable depreciation allowance is raised from 10% to 30% of the asset cost. There will be no change in value added tax rates (maximum 18%) in 2009, but the government considered changing VAT accrual rules in favor of the taxpayers. When the government reduced income and dividend tax, it'll attract foreign investors to invest in the country and it'll affect the demand of Russian currency.

The greater demand of Russian currency makes the currency appreciate against the others. Government Imposing Tax Barriers In December 2009, the government lifted import tariffs on industrial equipment imported by metallurgy, construction, forestry and textile industry, at the same time enforcing increased tariffs on imported cars. The government controls the import products by increasing the tariffs rate on some types of good. The import of the Russian has been restricted and makes the Russia demand for foreign currency reduce which make the Russia currency appreciate. 60 day graph [pic] Base on the graph, Ruble was strength during November 2009, however it keeps declining continuously and bottom out on the end of 2009.

This Ruble weaken is because of the the trade deficit as Russia's export is much lower than its import in both goods and services. Then the graph is fluctuated around the beginning of 2010. After that the government takes more control of the situation and coming up with more effective policies such as smooth out inflation, and impose more government trade restriction.